

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 1998

| COMMISSION FILE NO. | REGISTRANT AND STATE OF INCORPORATION ADDRESS AND TELEPHONE NUMBER | IRS EMPLOYER IDENTIFICATION NO. |
|------------------------|--|------------------------------------|
| 333-47647 | American States Water Company (A California Corporation) 630 East Foothill Boulevard San Dimas, California 91773-9016 909-394-3600 | 95-4676679 |
| 000-01121 | Southern California Water Company (A California Corporation) 630 East Foothill Boulevard San Dimas, California 91773-9016 909-394-3600 | 95-1243678 |

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

AMERICAN STATES WATER COMPANY
COMMON SHARES, \$2.50 STATED VALUE

NEW YORK STOCK EXCHANGE

Title of Each Class

Name of Each Exchange On Which Registered

Securities registered pursuant to Section 12(g) of the Act: NONE

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

American States Water Company Yes No
Southern California Water Company Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

The aggregate market value of the total voting stock held by non-affiliates of American States Water Company was approximately \$226,836,000 on March 26, 1999. The closing price per Common Share on that date, as quoted in the Western Edition of The Wall Street Journal, was \$25-5/16. Voting Preferred Shares of American States Water Company, for which there is no established market, were valued on March 26, 1999 at \$1,434,000 based on a yield of 5.56%. As of March 26, 1999, the number of Common Shares of American States Water Company, \$2.50 Stated Value, outstanding was 8,957,671. As of that same date, all 100 outstanding Common Shares of Southern California Water Company were owned by American States Water Company.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement filed with the Securities and Exchange Commission on or about March 28, 1999 as to Part III, Item Nos. 10, 11, 12 and 13, in each case as specifically referenced herein.

AMERICAN STATES WATER COMPANY
AND
SOUTHERN CALIFORNIA WATER COMPANY

FORM 10-K

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ITEM 1. BUSINESS

This annual report on Form 10-K is a combined report being filed by two separate Registrants: American States Water Company (hereinafter "AWR") and Southern California Water Company (hereinafter "SCW"). References in this report to "Registrant" are to AWR and SCW, collectively, unless otherwise specified. SCW makes no representations as to the information contained in this report relating to AWR and its subsidiaries, other than SCW.

GENERAL

AWR was incorporated in 1998 in connection with the formation of a holding company by SCW and became a public company on July 1, 1998. AWR has no material assets other than the common stock of SCW. SCW is a public utility company engaged principally in the purchase, production, distribution and sale of water (SIC No. 4941). SCW also distributes electricity in one customer service area (SIC No. 4911). SCW is regulated by the California Public Utilities Commission ("CPUC") and was incorporated on December 31, 1929 under the laws of the State of California. AWR has another subsidiary, American States Utility Services, Inc. ("ASUS") which contracts to lease, operate and maintain governmentally owned water and wastewater systems and to provide other services to local governments to assist them in the operation and maintenance of their water and wastewater systems. Neither AWR nor ASUS are regulated by the CPUC.

SCW is organized into three regions operating within 75 communities in 10 counties in the State of California and provides water service in 21 customer service areas. Region I incorporates 7 customer service areas in northern and central California, Region II has 6 customer service areas located in Los Angeles and Orange counties; and Region III incorporates 8 water customer service areas and the Bear Valley Electric customer service area. As of December 31, 1998, about 73% of SCW's water customers were located in the greater metropolitan areas of Los Angeles and Orange Counties. SCW also provides electric service to the City of Big Bear Lake and surrounding areas in San Bernardino County. All electric energy sold by SCW to customers in its Bear Valley Electric customer service area in 1998 was purchased under an energy brokerage contract with Sempra Energy Corporation.

SCW's utility operations exhibit seasonal trends. Although SCW's water utility operations have a diversified customer base, revenues derived from commercial and residential water customers accounted for approximately 91% and 93% of total water revenues in 1998 and 1997, respectively.

SCW served 242,634 water customers and 20,865 electric customers at December 31, 1998, or a total of 263,499 customers, compared with 262,279 total customers at December 31, 1997.

COMPETITION

The business of SCW is substantially free from direct and indirect competition with other public utilities, municipalities and other public agencies. AWR's other subsidiary, ASUS, actively competes with other investor-owned utilities and governmental entities on the basis of price and quality of service.

EMPLOYEE RELATIONS

Registrant had 470 employees as of December 31, 1998 as compared to 467 at December 31, 1997. Seventeen positions in SCW's Bear Valley Electric customer service area are covered by a collective bargaining unit agreement, which expires in 1999, with the International Brotherhood of Electrical Workers. Forty-nine positions in SCW's Metropolitan ratemaking district are covered by a collective bargaining unit agreement, which expires in 2001, with the Utility Workers of America. Registrant has no other unionized employees.

ITEM 2 - PROPERTIES

FRANCHISES, COMPETITION, ACQUISITIONS AND CONDEMNATION OF PROPERTIES

SCW holds all necessary franchises from the incorporated communities and the counties which it serves. SCW holds certificates of public convenience and necessity granted by the CPUC in each of the ratemaking districts it serves. SCW's certificates, franchises and similar rights are subject to alteration, suspension or repeal by the respective governmental authorities having jurisdiction.

The laws of the State of California provide for the acquisition of public utility property by governmental agencies through their power of eminent domain, also known as condemnation. Registrant has not been, within the last three years, involved in activities related to the condemnation of any of its water customer service areas or in its Bear Valley Electric customer service area.

ELECTRIC PROPERTIES

SCW's electric properties are all located in the Big Bear area of San Bernardino County. As of December 31, 1998, SCW operated 28.7 miles of overhead 34.5 KV transmission lines, 0.6 miles of underground 34.5 KV transmission lines, 172.4 miles of 4.16 KV or 2.4 KV distribution lines, 39.5 miles of underground cable and 14 sub-stations. There are no generating plants in SCW's system.

OFFICE BUILDINGS

Registrant's general offices are housed in a single-story office building located in San Dimas, California. The land and the building, which was completed and occupied in early 1990, are owned by SCW. SCW also owns and occupies certain facilities housing regional, district and customer service offices while other such facilities are housed in leased premises.

WATER PROPERTIES

As of December 31, 1998, SCW's physical properties consisted of water transmission and distribution systems which included 2,768 miles of pipeline together with services, meters and fire hydrants and 437 parcels of land, generally less than 1 acre each, on which are located wells, pumping plants, reservoirs and other water utility facilities including five surface water treatment plants.

As of December 31, 1998, SCW owned and operated 294 active wells equipped with pumps with an aggregate capacity of approximately 180 million gallons per day. SCW has 52 connections to the water distribution facilities of the Metropolitan Water District of Southern California ("MWD") and other municipal water agencies. SCW's storage reservoirs and tanks have an aggregate capacity of approximately 95 million gallons. SCW owns no dams in its customer service areas. The following table provides, in greater detail, selected water utility plant of SCW for each of its water ratemaking districts:

| | Pumps | | Distribution Facilities | | | | Reservoirs | |
|---------------|-------|---------|-------------------------|---------|----------|----------|------------|----------|
| | Well | Booster | Mains (ft.) | Meters | Services | Hydrants | Tanks | Capacity |
| Arden Cordova | 25 | 17 | 473,391 | 3,389 | 8,337 | 1,175 | 3 | 4,000 |
| Barstow | 25 | 37 | 866,308 | 14,404 | 10,765 | 997 | 13 | 8,025 |
| Bay Point | 1 | 16 | 139,299 | 5,150 | 3,034 | 300 | 7 | 4,046 |
| Calipatria | 0 | 8 | 134,879 | 1,133 | 1,664 | 73 | 1 | 150 |
| Claremont | 27 | 35 | 722,899 | 16,394 | 11,229 | 1,175 | 16 | 16,082 |
| Clearlake | 0 | 13 | 189,418 | 2,549 | 915 | 74 | 4 | 647 |
| Desert | 17 | 22 | 749,165 | 7,408 | 4,562 | 572 | 14 | 1,477 |
| Los Osos | 10 | 10 | 195,812 | 3,916 | 1,385 | 154 | 8 | 834 |
| Metro | 79 | 83 | 4,743,429 | 150,102 | 108,328 | 7,440 | 41 | 25,209 |
| Ojai | 5 | 12 | 234,318 | 5,120 | 3,434 | 348 | 5 | 1,494 |
| Orange | 33 | 37 | 2,176,187 | 59,498 | 40,762 | 4,433 | 18 | 11,903 |
| San Dimas | 11 | 37 | 1,198,326 | 20,571 | 7,901 | 861 | 16 | 10,149 |
| San Gabriel | 23 | 10 | 551,101 | 12,827 | 12,849 | 784 | 3 | 1,520 |
| Santa Maria | 29 | 23 | 956,414 | 21,628 | 7,617 | 767 | 8 | 2,541 |
| Simi | 1 | 22 | 470,091 | 13,940 | 9,492 | 826 | 6 | 6,210 |
| Wrightwood | 8 | 5 | 216,809 | 5,428 | 670 | 76 | 7 | 1,546 |
| Total | 294 | 387 | 14,017,846 | 343,457 | 232,944 | 20,055 | 170 | 95,833 |

Capacity is measured in thousands of gallons

MORTGAGE AND OTHER LIENS

As of December 31, 1998, Registrant had no mortgage debt outstanding, and its properties were free of any liens securing indebtedness.

ITEM 3 - LEGAL PROCEEDINGS

WATER QUALITY-RELATED LITIGATION

On April 24, 1997, a complaint in multiple counts seeking recovery for negligence, wrongful death, strict liability, trespass, public nuisance, private nuisance, negligence per se, strict liability for ultrahazardous activities and fraudulent concealment was filed in Los Angeles Superior Court on behalf of approximately 145 plaintiffs (the "Adler Matter"). After preliminary Demurrers and Motions to Strike, these same plaintiffs filed a First Amended Complaint on or about October 16, 1997 seeking recovery on essentially the same theories. Plaintiffs allege SCW has provided and continues to provide them with allegedly contaminated water from wells located in an area of the San Gabriel Valley that has been designated a federal environmental superfund site, and that the maintenance of this contaminated well water has resulted in contamination of the soil, subsurface soil, and surrounding air, with trichloroethylene ("TCE"), perchloroethene ("PCE"), carbon tetrachloride and other solvents. Plaintiffs further allege that SCW's actions have caused, and continue to cause, injuries to the plaintiffs. Plaintiffs seek damages, including general, special, and punitive damages, according to proof at trial, as well as attorney's fees on certain causes of action, costs of suit, and other unspecified relief.

On June 24, 1998, the judge assigned to the Adler Matter, acting on the Court's own motion, issued a stay until June 15, 1999 of all proceedings in the Adler matter pending the outcome of the CPUC's Order Instituting Investigation ("OII") proceeding described below. Plaintiffs in the Adler matter petitioned the Second District Court of Appeal for a Writ of Mandamus to have the stay lifted. Prior to hearings before the Appellate Court, the Court advised all parties of a potential conflict of interest due to the fact that two clerical staff members of the Court were plaintiffs in one of the consolidated cases, Santamaria v. Suburban Water Systems. As a result, the Adler matter and all the

consolidated cases were transferred to the First District Court of Appeal in San Francisco. The Writ of Mandamus is scheduled to be heard by the First District Appellate Court on April 19, 1999. In addition, the Appellate Court has requested argument as to why the lower courts issued a stay in the Adler matter rather than dismissing the case.

SCW was served on November 3, 1997 as Doe 1 in the matter of Santamaria v. Suburban Water Systems which was filed in Los Angeles Superior Court (the "Santamaria Matter"). On August 27, 1998, the judge assigned to the Santamaria Matter sustained SCW's demurrer without leave to amend and dismissed the action against SCW. Plaintiff's filed a Notice of Appeal with the Second District Court of Appeals and this matter was consolidated with the Adler and other cases. A conflict of interest arose as was mentioned previously. As a result, the Notice of Appeal was transferred to the First District Court of Appeal. The Santamaria matter was requested to be heard by the First District Appellate Court on April 19, 1999, along with the other cases. There has been no word as yet as to whether the plaintiffs will agree to have the Santamaria matter heard at the same time as Adler and the other cases since they are appealing the dismissal and not responding to Writ petitions.

In January 1998 SCW was named a defendant in the matter of Nathaniel Allen, Jr., et al. v. Aerojet-General Corporation, et al which was filed in Sacramento Superior Court. The complaint makes claims based on wrongful death, personal injury, property damage as a result of nuisance and trespass, medical monitoring, and diminution of property values (the "Allen Matter"). Plaintiffs allege that SCW and other defendants have delivered water to plaintiffs which allegedly is, or has been in the past, contaminated with a number of chemicals, including TCE, PCE, carbon tetrachloride, perchlorate, Freon-113, hexavalent chromium and other, unnamed, chemicals. SCW filed Demurrers and Motion to Strike in this matter on June 5, 1998. On August 31, 1998, the judge assigned to the Allen Matter, acting on the Court's own motion, issued a stay until June 15, 1999 of all proceedings in the Allen matter pending the outcome of the CPUC's OII proceeding. The plaintiff's petitioned the Third District Court of Appeal for a Writ of Mandamus to overrule the stay. The Court denied the petition. Plaintiff's then petitioned the California Supreme Court for relief from the Appellate Court's ruling. The California Supreme Court denied plaintiff's petition. Thus the stay in the Allen Matter remains in effect.

In April 1998, SCW was named a defendant in the matter of Daphne Adams, et al. v. Aerojet General, et al. which was filed in Sacramento Superior Court (the "Adams Matter"). The complaint makes claims based on negligence, strict liability, trespass, public nuisance, private nuisance, negligence per se, absolute liability for ultrahazardous activity, fraudulent concealment, violation of California Business and Professions Code section 17200 et seq., intentional infliction of emotional distress, intentional spoilage of evidence, negligent destruction of evidence needed for prospective civil litigation, wrongful death and medical monitoring. Plaintiff's seek damages, including general, punitive and exemplary damages, as well as attorney's fees, costs of suit, injunctive and restitutionary relief, disgorged profits and civil penalties, medical monitoring according to proof and other unspecified relief. SCW filed its Demurrers and Motion to Strike in this matter on June 5, 1998. On August 31, 1998, the judge assigned to the Adams Matter, acting on the Court's own motion, issued a stay until June 15, 1999 of all proceedings in the Adams matter pending the outcome of the CPUC's OII proceeding. The plaintiff's petitioned the Third District Court of Appeal for a Writ of Mandamus to overrule the stay. The Court denied the petition. Plaintiff's then petitioned the California Supreme Court for relief from the Appellate Court's ruling. The California Supreme Court denied plaintiff's petition. Thus the stay in the Adams Matter remains in effect.

On July 30, 1998, a complaint in multiple counts, styled Georgianna Dominguez, et al. v. Southern California Water Company, et al., was filed in Los Angeles Superior Court seeking recovery for negligence, wrongful death, strict liability, permanent trespass, continuing trespass, public permanent nuisance, public continuing nuisance, private permanent nuisance, private continuing nuisance, negligence per se, absolute liability for ultrahazardous activity and fraudulent concealment on behalf of six plaintiffs

(the "Dominguez Matter"). Plaintiff's seek damages, including general and special damages according to proof, punitive and exemplary damages, as well as attorney's fees, costs of suit and other unspecified relief. SCW was served with the complaint on September 21, 1998.

By Stipulation, the Dominguez Matter has been "attached" to the Adler Matter, and the parties have agreed that the Dominguez Matter will be bound by actions taken in the Adler Matter. Parties to the Stipulation have, however reserved any rights that might be distinct in the Dominguez Matter. Thus, the Dominguez matter is presently under the same stay order as was issued in the Adler Matter.

On October 13, 1998, a complaint in multiple counts was filed in Los Angeles Superior Court, styled Anderson, et al. v. Suburban Water Systems, et al., which seeks recovery for negligence, wrongful death, strict liability, permanent trespass, continuing trespass, continuing nuisance, permanent nuisance, negligence per se, absolute liability for ultrahazardous activity, fraudulent concealment, conspiracy/fraudulent concealment, battery and unfair business practices on behalf of 180 plaintiffs (the "Anderson Matter"). Plaintiff's seek damages, including general and special damages according to proof, punitive and exemplary damages, as well as attorney's fees, costs of suit and other unspecified relief. SCW has not yet been served in this matter.

On December 30, 1998, SCW was named as a defendant in a complaint in multiple counts, styled Abarca, et al. v. City of Pomona, et al., filed in Los Angeles Superior Court which seeks recovery for negligence, wrongful death, strict liability, permanent trespass, continuing trespass, continuing nuisance, permanent nuisance, negligence per se, absolute liability for ultrahazardous activity, fraudulent concealment, conspiracy/fraudulent concealment, battery and unfair business practices on behalf of 383 plaintiffs (the "Abarca Matter"). Plaintiff's seek damages, including general and special damages according to proof, punitive and exemplary damages, as well as attorney's fees, costs of suit and other unspecified relief. SCW has not yet been served in this matter.

SCW was served on March 19, 1999 as Doe 1 in the matter styled Celi, et al. v. San Gabriel Valley Water Company, et al., filed in Los Angeles Superior Court which seeks recovery for negligence, wrongful death, strict liability, permanent trespass, continuing trespass, public continuing nuisance, public permanent nuisance, private permanent nuisance, private continuing nuisance, negligence per se, absolute liability for ultrahazardous activity and fraudulent concealment (the "Celi Matter"). Plaintiff's seek damages, including general and special damages according to proof, punitive and exemplary damages, as well as attorney's fees, costs of suit and other unspecified relief.

SCW was served on March 19, 1999 as Doe 3 in the matter styled Boswell, et al. v. Suburban Water Systems, et al., filed in Los Angeles Superior Court which seeks recovery for negligence, wrongful death, strict liability, permanent trespass, continuing trespass, public continuing nuisance, public permanent nuisance, private permanent nuisance, private continuing nuisance, negligence per se, absolute liability for ultrahazardous activity and fraudulent concealment (the "Boswell Matter"). Plaintiff's seek damages, including general and special damages according to proof, punitive and exemplary damages, as well as attorney's fees, costs of suit and other unspecified relief.

SCW was served on March 19, 1999 as Doe 1 in the matter styled Demciuc, et al. v. Suburban Water Systems, et al., filed in Los Angeles Superior Court which seeks recovery for negligence, wrongful death, strict liability, permanent trespass, continuing trespass, public continuing nuisance, public permanent nuisance, private permanent nuisance, private continuing nuisance, negligence per se, absolute liability for ultrahazardous activity and fraudulent concealment (the "Demciuc Matter"). Plaintiff's seek damages, including general and special damages according to proof, punitive and exemplary damages, as well as attorney's fees, costs of suit and other unspecified relief.

SCW was served on March 19, 1999 as Doe 1 in the matter styled Criner, et al. v. San Gabriel Valley Water Company, et al., filed in Los Angeles Superior Court which seeks recovery for negligence, wrongful death, strict liability, permanent trespass, continuing trespass, public continuing nuisance, public permanent nuisance, private permanent nuisance, private continuing nuisance, negligence per se, absolute liability for ultrahazardous activity and fraudulent concealment (the "Criner Matter"). Plaintiff's seek damages, including general and special damages according to proof, punitive and exemplary damages, as well as attorney's fees, costs of suit and other unspecified relief.

The Celi, Boswell, Domcuic and Criner Matters will be bound by actions taken in the Adler Matter, although the parties have reserved any rights that might be distinct in these matters.

In light of the breadth of plaintiff claims in these matters, the lack of factual information regarding plaintiff's claims and injuries, if any, and the fact that no discovery has yet been completed, SCW is unable at this time to determine what, if any, potential liability it may have with respect to these claims. Registrant intends to vigorously defend against these claims.

ORDER INSTITUTING INVESTIGATION

In March 1998, the CPUC issued an Order Instituting Investigation (OII) to regulated water utilities in the state of California, including SCW. The purpose of the OII is to determine whether existing standards and policies regarding drinking water quality adequately protect the public health and whether those standards and policies are being uniformly complied with by those water utilities. The OII delineates the constitutional and statutory jurisdiction of the CPUC and the California Department of Health Services ("DOHS") in establishing and enforcing adherence to water quality standards. The CPUC's jurisdiction provides for the establishment of rates which permit water utilities to furnish safe water meeting the established water quality standards at prices which are both affordable and allow the utility to earn a reasonable return on its investment. SCW has provided its response to a series of questions dealing with the adequacy of current drinking water standards, compliance by water utilities with such standards, appropriate remedies for failure to comply with safe drinking water standards and whether increased enforcement and additional drinking water standards are necessary. SCW anticipates a final decision by the CPUC on this matter in or about June 1999. See Note 8 to the Notes to Financial Statements contained in Part II, Item 8.

OTHER LITIGATION

Registrant is also subject to ordinary routine litigation incidental to its business. Other than as disclosed above, no legal proceedings are pending, except such incidental litigation to which Registrant is a party or of which any of its properties is the subject which are believed to be material.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matter was submitted during the fourth quarter of the fiscal year covered by this report to a vote of security holders through the solicitation of proxies or otherwise.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

(a) MARKET INFORMATION RELATING TO COMMON SHARES -

Common shares of American States Water Company are traded on the New York Stock Exchange under the symbol "AWR". The high and low sales prices of the

Common Shares of AWR for the third and fourth quarters of 1998 and of SCW for all other periods for the past two years are as follows:

| | STOCK PRICES | |
|----------------|--------------|------------|
| | HIGH | LOW |
| 1998 | | |
| First Quarter | \$ 26 | \$ 23-1/16 |
| Second Quarter | 27-1/8 | 21-1/8 |
| Third Quarter | 27 | 23-1/4 |
| Fourth Quarter | 29-1/4 | 24-7/8 |
| 1997 | | |
| First Quarter | \$ 23 | \$ 20-5/8 |
| Second Quarter | 24-1/2 | 20-1/4 |
| Third Quarter | 24-5/8 | 20-1/2 |
| Fourth Quarter | 25-5/8 | 21-1/2 |

All of the outstanding Common Shares of SCW and ASUS are owned by AWR. Hence, there is no market for the Common Shares of either entity.

(b) APPROXIMATE NUMBER OF HOLDERS OF COMMON SHARES -

As of February 26, 1999, there were 3,691 holders of record of Common Shares of AWR. All of the outstanding Common Shares of SSCW and ASUS are owned by AWR.

(c) FREQUENCY AND AMOUNT OF ANY DIVIDENDS DECLARED AND DIVIDEND RESTRICTIONS

For the last three years, Registrant has paid dividends on its Common Shares on March 1, June 1, September 1 and December 1. The following table lists the amount of dividends paid on Common Shares of AWR for the third and fourth quarters of 1998 and of SCW for all other periods for the last two years:

| | 1998 | 1997 |
|----------------|----------|----------|
| First Quarter | \$ 0.315 | \$ 0.310 |
| Second Quarter | 0.315 | 0.310 |
| Third Quarter | 0.315 | 0.310 |
| Fourth Quarter | 0.315 | 0.315 |
| Total | \$ 1.260 | \$ 1.245 |

Information on dividend restrictions for AWR and SCW may be found in Note 2 captioned "Capital Stock" of the Notes to Financial Statements in Part II, Item 8 Financial Statements and Supplementary Data.

ITEM 6. SELECTED FINANCIAL DATA

| (\$ in thousand, except per share amounts) | 1998 | 1997 | 1996 | 1995 | 1994 |
|--|-----------|-----------|-----------|-----------|-----------|
| INCOME STATEMENT INFORMATION | | | | | |
| Total Operating Revenues | \$148,060 | \$153,755 | \$151,529 | \$129,813 | \$122,675 |
| Total Operating Expenses | 122,999 | 130,297 | 128,100 | 108,425 | 103,745 |
| Operating Income | 25,061 | 23,458 | 23,429 | 21,388 | 18,930 |
| Other Income | 769 | 758 | 531 | 336 | 236 |
| Interest Charges | 11,207 | 10,157 | 10,500 | 9,559 | 7,828 |
| Net Income | 14,623 | 14,059 | 13,460 | 12,165 | 11,338 |
| Preferred Dividends | 90 | 92 | 94 | 96 | 98 |
| Earnings Available for Common Shareholders | 14,533 | 13,967 | 13,366 | 12,069 | 11,240 |
| Basic Earnings per Common Share | \$ 1.62 | \$ 1.56 | \$ 1.69 | \$ 1.54 | \$ 1.43 |
| Dividends Declared per Common Shares | \$ 1.26 | \$ 1.25 | \$ 1.23 | \$ 1.21 | \$ 1.20 |
| BALANCE SHEET INFORMATION | | | | | |
| Total Assets | \$484,671 | \$457,074 | \$430,922 | \$406,255 | \$383,627 |
| Common Shareholders' Equity | 154,299 | 151,053 | 146,766 | 121,576 | 118,962 |
| Long-Term Debt | 120,809 | 115,286 | 107,190 | 107,455 | 92,891 |
| Preferred Shares-Not subject to Mandatory Redemption | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 |
| Preferred Shares-Mandatory Redemption | 400 | 440 | 480 | 520 | 560 |
| Total Capitalization | \$277,108 | \$268,379 | \$256,036 | \$231,151 | \$214,013 |
| Book Value per Common Share | \$ 17.23 | \$ 16.86 | \$ 16.52 | \$ 15.50 | \$ 15.16 |
| Average Shares Outstanding | 8,958 | 8,957 | 7,891 | 7,845 | 7,842 |
| OTHER INFORMATION | | | | | |
| Ratio of Earnings to Fixed Charges | 3.21% | 3.35% | 3.26% | 3.19% | 3.58% |
| Ratio of Earnings to Total Fixed Charges | 3.17% | 3.30% | 3.21% | 3.14% | 3.50% |
| Return on Average Common Equity | 9.6% | 9.5% | 10.7% | 10.3% | 9.7% |

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION

Unless specifically noted, the following discussion and analysis provides information on AWR's consolidated operations and assets. There are no material differences between the consolidated operations and assets of AWR and the operations and assets of SCW.

FORWARD-LOOKING INFORMATION

Certain matters discussed in this report (including the documents incorporated herein by reference) are forward-looking statements intended to qualify for the "safe harbor" from liability established by the Private Securities Litigation Reform Act of 1995. These forward-looking statements can generally be identified as such because the context of the statement will include words such as the Company or Registrant "believes," "anticipates," "expects" or words of similar import. Similarly, statements that describe the Company's future plans, objectives, estimates or goals are also forward-looking statements. Such statements address future events and conditions concerning capital expenditures, earnings, litigation, rates, water quality and other regulatory matters, adequacy of water supplies, liquidity and capital resources, opportunities related to operations of municipally-owned water systems and accounting matters. Actual results in each case could differ materially from those currently anticipated in such statements, by reason of factors such as utility restructuring, including ongoing local, state and federal activities; future economic conditions, including changes in customer demand; future climatic conditions; legislative, regulatory and other circumstances affecting anticipated revenues and costs; and abilities of other companies to remain or become year 2000 ready.

RESULTS OF OPERATIONS

YEARS ENDED DECEMBER 31, 1998 AND 1997

Basic earnings per common share in 1998 increased by 3.8% to \$1.62 per share as compared to \$1.56 per share for the comparable period last year. Although wet weather significantly impacted revenues in 1998, lower supply costs and modest increases in other operating expenses partially offset the decline in revenues.

Water operating revenues decreased by 4.3% in 1998 to \$134.9 million from the \$141.0 million reported in 1997. Water sales volumes in 1998 were 9.9% lower than 1997 due to extremely wet weather during the first half of 1998. The decrease in sales was partially offset by rate increases effective during 1998.

Electric operating revenues of \$13.2 million were 3.4% higher in 1998 as compared to 1997 due to the impact of a general rate increase effective January 1998 as well as a 2.0% increase in kilowatt-hour sales.

Purchased water costs decreased in 1998 to \$30.8 million as compared to \$38.3 million in 1997 due to a 20.8% decrease in volumes purchased and refunds received from SCW's wholesale water supplier during 1998 of approximately \$1.4 million. Refunds of \$2.0 million were received in 1997.

Costs of power purchased for pumping decreased by 7.2% to \$7.0 million in 1998 chiefly as the result of the reduced energy costs from SCW's suppliers.

Costs of power purchased for resale in 1998 decreased by 3.4% to \$5.0 million from the \$5.2 million recorded in 1997 due to reduced costs from SCW's energy providers, which partially offset the effects of increased kilowatt-hour sales volumes recorded during the year.

Groundwater production assessments increased 10.5% to \$7.6 million in 1998 from \$6.8 million in 1997 due to the increased amounts of pumped water in SCW's resource mix as well as additional assessments associated with increased pumping in SCW's Metropolitan and Orange County customer service areas.

A positive entry for the provision for supply cost balancing accounts reflects recovery of previously under-collected supply costs. Conversely, a negative entry for the provision for supply cost balancing accounts reflects an under-collection of previously incurred supply costs. Recovery of previously under-collected supply costs was lower in 1998 than 1997 due to the expiration in January 1998 of a surcharge designed to recover those costs. It is anticipated that new rates, effective January 1999, will increase collection of these under-collected costs. The balancing account mechanism insulates earnings from changes in the unit cost of supply costs which are outside of the immediate control of Registrant. However, the balancing account is not designed to insulate earnings against changes in supply mix, as occurred during the first eight months of 1997.

Other operating expenses increased by 10.6% from the \$13.1 million recorded in 1997 due to employee time charged to this category. Reversals in 1997 of costs associated with recovery of water quality expenditures through the CPUC's memorandum account mechanism also contributed to the increase. There were no such reversals of equal magnitude in 1998.

Administrative and general expenses decreased slightly by 0.7% to \$22.0 million in 1998 from the \$22.1 million recorded in 1997. The decrease is due to stability in costs associated with health insurance, post-retirement medical benefits, pension and 401(k) plan costs and to a reduction of time charge by employees to this category.

In 1998, maintenance expense remained at approximately the \$7.3 million level recorded in 1997 due principally to the wet weather conditions during the first part of the year that hampered planned maintenance activity.

Depreciation expense in 1998 increased by 14.5% to \$12.5 million reflecting the effects of recording approximately \$38 million in net plant additions during 1997, depreciation on which began in 1998. In addition, amortization of start-up and organizational costs associated with the formation of AWR is reflected in 1998. There were no similar amortization costs in 1997.

Taxes on income increased by approximately 3.1% to \$10.1 million in 1998 as compared to the \$9.8 million in 1997 due to a 5.7% increase in operating income partially offset by a lower effective tax rate.

Property and other taxes decreased by 2.5% in 1998 to \$6.1 million due primarily to reduced franchise tax payments directly attributable to reduced revenues.

Other income increased by 1.5% in 1998 due principally to the flow-through of tax benefits related to refinancing of long-term debt which was partially offset by an increase in reserves against costs associated with SCW's non-regulated activities.

Interest expense increased by 10.3% to \$11.2 million primarily due to increased short-term bank borrowing and the issuance of \$15 million in long-term debt in March 1998.

YEARS ENDED DECEMBER 31, 1997 AND 1996

Basic earnings per common share in 1997 decreased by 7.7% to \$1.56 per share as compared to \$1.69 per share for the comparable period in 1996, directly attributable to significantly increased supply costs during the first eight months of 1997.

Water operating revenues increased by 0.7% in 1997 to \$141.0 million from the \$140.0 million reported in 1996. Although water sales volumes were 2.7% higher in 1997, in 1996 SCW began recovery of previously incurred supply costs, in accordance with rules of the CPUC. In 1997, recovery of these costs was completed in several customer service areas and rates were accordingly reduced, partially offsetting rate increases effective during 1997 in other customer service areas.

Electric operating revenues of \$12.8 million were 10.7% higher in 1997 as compared to 1996 due to the impact of a general rate increase effective January 1997 as well as a 3.6% increase in kilowatt-hour sales.

Purchased water costs remained relatively the same at \$38.3 million in 1997 as compared to \$38.4 million in 1996, despite a 6.4% increase in volumes purchased, due to refunds received from SCW's wholesale water supplier during 1997 of approximately \$2.0 million, which reduced recorded purchased water costs. There were no such refunds received during 1996.

Costs of power purchased for pumping decreased by 2.0% to \$7.6 million in 1997, chiefly as the result of the reduced amounts of water produced from pumped sources in SCW's resource mix. During 1997, SCW had several wells out of service due to water quality issues which significantly affected its ability to fully utilize its groundwater resources.

Costs of power purchased for resale in 1997 decreased by 10.9% to \$5.2 million from the \$5.8 million recorded in 1996 due to reduced costs from SCW's energy provider which partially offset the effects of increased kilowatt-hour sales volumes recorded during the year.

Groundwater production assessments increased 15.2% to \$6.8 million in 1997 from \$5.9 million in 1996 due to additional assessments associated with increased pumping in SCW's San Gabriel Valley and San Dimas customer service areas.

The positive entry for supply cost balancing accounts for 1997 is a result of approval by the CPUC of rate increases sufficient to recover previously under-collected purchased supply costs, as well as refunds received during 1997 from wholesale suppliers. The balancing account mechanism insulates earnings from changes in the unit costs of supply costs which are outside of the immediate control of SCW. However, the balancing account is not designed to insulate earnings against changes in supply mix, as occurred during the first eight months of 1997.

Administrative and general expenses increased by 7.7% to \$22.1 million in 1997 from the \$20.5 million recorded in 1996. This increase reflects higher labor costs. In addition, during 1997 SCW incurred costs for consulting on water quality litigation for which there was no corresponding amount in 1996.

In 1997, maintenance expense decreased by 5.7% to \$7.3 million from \$7.7 million recorded in 1996 due principally to increased emphasis being placed on SCW's meter replacement and capital improvement program which partially offset increased maintenance on SCW's water supply sources.

Depreciation expense in 1997 increased by 8.4% to \$11.0 million reflecting the effects of recording approximately \$31.0 million in net plant additions during 1996, on which depreciation began in 1997.

Taxes on income decreased by approximately 4.4% to \$9.8 million in 1997 as compared to the \$10.3 million in 1996 as a result of lower pre-tax income. Other taxes increased by 3.0% in 1997 to \$6.3 million due primarily to increased property taxes resulting from higher valuation assessments in 1997.

Other income increased by 42.7% in 1997 due principally to an increase in billings to the City of Folsom for the lease of a portion of SCW's water rights in the American River.

Interest expense decreased by 3.3% to \$10.2 million primarily due to reduced short-term bank borrowing and the lower borrowing rates experienced during 1997.

LIQUIDITY AND CAPITAL RESOURCES

AWR funds its operating expenses, dividends on its outstanding Common and Preferred Shares and makes its mandatory sinking fund payments principally through dividends from SCW. In December 1998, AWR filed a Registration Statement with the Securities and Exchange Commission (SEC) for issuance, from time to time, of up to \$60 million in Common Shares, Preferred Shares and/or debt securities. The proceeds will be used primarily for investment in its subsidiaries.

SCW funds the majority of its operating expenses, interest payments on its debt and dividends on its outstanding Common Shares through internal sources. SCW continues to rely on external sources,

including short-term bank borrowing, contributions-in-aid-of-construction, advances for construction and install-and-convey advances, to fund the majority of its construction expenditures.

Because of the seasonal nature of its water and electric operations, SCW utilizes its short-term borrowing capacity to finance current operating expenses. The aggregate short-term borrowing capacity available to SCW under its three bank lines of credit was \$47 million as of December 31, 1998 of which a total of \$38 million was outstanding. SCW routinely employs short-term bank borrowing as an interim financing source prior to executing either a long-term debt or equity issue. SCW issued long-term debt totaling \$15.0 million in March 1998. The funds were used initially to repay short-term bank borrowings, after which construction expenditures were funded.

In December 1998, SCW redeemed, at a premium, the entire \$10 million outstanding of its 10.10% Notes. These Notes were refinanced in January 1999.

In December 1998, SCW filed a Registration Statement with the SEC for issuance, from time to time, of up to \$60 million in long-term debt with the net proceeds being used to repay short-term bank borrowings and fund construction needs. In January 1999, SCW issued \$40 million of long-term debt pursuant to this Registration Statement, all of which was used to reduce bank borrowing.

Registrant has no derivative financial instruments, financial instruments with significant off-balance sheet risks or financial instruments with concentrations of credit risk.

CONSTRUCTION PROGRAM

SCW's construction program is designed to ensure its customers high quality service. A program for water pipeline replacement is on-going throughout the 22 customer service areas, based on priority of leaks detected, fire protection enhancements and reflection of the underlying replacement schedule. In addition, general upgrades in SCW's water supply facilities are anticipated to be on-going. SCW's Board of Directors has approved anticipated net capital expenditures of \$42.1 million in 1999. Neither AWR nor ASUS have material capital requirements.

REGULATORY MATTERS

SCW is subject to regulation by the CPUC, which has broad powers with respect to service and facilities, rates, classifications of accounts, valuation of properties, the purchase, disposition and mortgaging of properties necessary or useful in rendering public utility service, the issuance of securities, the granting of certificates of convenience and necessity as to the extension of services and facilities and various other matters. AWR and ASUS are not directly regulated by the CPUC. The CPUC does, however, regulate certain transaction between SCW and its unregulated affiliates.

The 22 customer service areas of SCW are grouped into 16 water districts and one electric district for ratemaking purposes. Water rates vary among the 16 ratemaking districts due to differences in operating conditions and costs. SCW monitors operations on a regional basis in each of these districts so that applications for rate changes may be filed, when warranted. Under the CPUC's practices, rates may be increased by three methods: general rate case increases (GRC's), offsets for certain expense increases and advice letter filings related to certain plant additions. GRC's are typically for three-year periods, which include step increases for the second and third year. Rates are based on projected expenses and capital costs. GRC's have a typical regulatory lag of one year. Offset rate increases typically have a two to four month regulatory lag. The following table lists information on estimated annual rate changes during 1998, 1997 and 1996:

| Year | Supply Cost Offset | Balancing Account Amortization | General and Step Increases | Advice Letters | Total |
|--------------------------|--------------------------|--------------------------------------|----------------------------------|-------------------|----------|
| (Amounts are in \$000's) | | | | | |
| 1998 | \$ 786 | \$(2,852) | \$ 3,590 | \$ 713 | \$ 2,237 |
| 1997 | \$ 183 | \$ 64 | \$ 1,332 | \$ (126) | \$ 1,453 |
| 1996 | \$ 103 | \$ (758) | \$16,805 | \$ 913 | \$17,063 |

New water rates were implemented in three of SCW's customer service areas in January 1, 1998 to recover costs associated with capital projects in those areas. Step increases in rates were effective in April 1998 in Barstow and in May 1998 in Santa Maria. Increased rates for six additional water ratemaking districts and recovery of costs associated with SCW's general office functions were effective January 1, 1999.

Applications to increase water rates were filed for four water ratemaking districts in February 1999. The new rates, if authorized in total or in part by the CPUC, would be effective January 1, 2000.

SCW has filed an application with the CPUC to combine tariff schedules into regional rates for the customer service areas that make up SCW's Region III. A final decision from the CPUC is anticipated by the fourth quarter of 1999.

Hearings were held before the CPUC in November 1998 on SCW's filing seeking recovery through rates of \$1.8 million in costs associated with its participation in the coastal aqueduct extension of the State Water Project (the "Project"). In February 1999, the Administrative Law Judge assigned to the application issued his proposed decision which denied recovery of SCW's costs in the Project. SCW is continuing to pursue alternative forms of recovery of its investment in the Project including sale of its interests therein to other participants in the Project. A final order from the CPUC is anticipated in the second quarter of 1999. See Note 8 of the Notes to Financial Statements in Part II, Item 8.

ENVIRONMENTAL MATTERS

1996 Amendments to Federal Safe Drinking Water Act

On August 6, 1996, amendments (the "1996 SDWA amendments") to the Safe Drinking Water Act (the "SDWA") were signed into law. The 1996 SDWA revised the 1986 amendments to the SDWA with a new process for selecting and regulating contaminants. The U. S. Environmental Protection Agency ("EPA") can only regulate contaminants that may have adverse health effects, are known or likely to occur at levels of public health concern, and the regulation of which will provide "a meaningful opportunity for health risk reduction." The EPA has published a list of contaminants for possible regulation and must update that list every five years. In addition, every five years, the EPA must select at least five contaminants on that list and determine whether to regulate them. The new law allows the EPA to bypass the selection process and adopt interim regulations for contaminants in order to address urgent health threats. Current regulations, however, remain in place and are not subject to the new standard-setting provisions. The DOHS, acting on behalf of the EPA, administers the EPA's program in California.

The 1996 SDWA amendments allow the EPA for the first time to base primary drinking water regulations on risk assessment and cost/benefit considerations and on minimizing overall risk. The EPA must base regulations on best available, peer-reviewed science and data from best available methods. For proposed regulations that involve the setting of maximum contaminant levels ("MCL's"), the EPA must use, and seek public comment on, an analysis of quantifiable and non-quantifiable risk-reduction benefits and cost for each such MCL.

SCW currently tests its wells and water systems according to requirements listed in the SDWA. Water from wells found to contain levels of contaminants above the established MCLs is treated before it is delivered to customers.

Since the SDWA became effective, SCW has experienced increased operating costs for testing to determine the levels, if any, of the constituents in SCW's sources of supply and additional expense to lower the level of any contaminants in order to meet the MCL standards. Such costs and the costs of controlling any other contaminants may cause SCW to experience additional capital costs as well as increased operating costs.

Registrant is currently unable to predict the ultimate impact that the 1996 SDWA amendments might have on its financial position or its results of operation. The CPUC ratemaking process provides SCW with the opportunity to recover prudently incurred capital and operating costs associated with water quality. Management believes that such incurred costs will be authorized for recovery by the CPUC.

Proposed Enhanced Surface Water Treatment Rule

On July 29, 1994, the EPA proposed an Enhanced Surface Water Treatment Rule ("ESWTR") which would require increased surface-water treatment to decrease the risk of microbial contamination. The EPA has proposed several versions of the ESWTR for promulgation. The version selected for promulgation will be determined based on data collected by certain water suppliers and forwarded to the EPA pursuant to EPA's Information Collection Rule, which requires such water suppliers to monitor microbial and other contaminants in their water supplies and to conduct certain tests in respect of such contaminants. The EPA has adopted an Interim ESWTR applicable only to systems serving greater than 10,000 persons. The long-term ESWTR, in any of the forms currently proposed, would apply to each of SCW's five surface water treatment plants and is expected to be promulgated by November 2000. However, because it is impossible to predict the version of the ESWTR that will be promulgated, Registrant is unable to predict what additional costs, if any, will be incurred to comply with the ESWTR.

Regulation of Disinfection/Disinfection By-Products

Registrant is also subject to the new regulations concerning disinfection/disinfection by-products ("DBPs"), Stage I of which regulations were effective in November, 1998 with full compliance required by 2001. Stage I requires reduction of tri-halomethane contaminants from 100 micrograms per liter to 80 micrograms per liter. Two of SCW's systems are immediately impacted by this rule. SCW implemented modifications to the treatment process in its Bay Point and Cordova systems. It is anticipated that both systems will be in full compliance by 2001.

The EPA must adopt Stage II rules pertaining to DBPs, according to a negotiated schedule by 2000. The EPA is not allowed to use the new cost/benefit analysis provided for in the 1996 SDWA amendments for establishing the Stage II rules applicable to DBPs but may utilize the regulatory negotiating process provided for in the 1996 SDWA amendments to develop the Stage II rule. The final rule is expected by 2002.

Ground Water Rule

By August 1999, the EPA is scheduled to propose regulations requiring disinfection of certain groundwater systems and provide guidance on determining which systems must provide disinfection facilities. The EPA may utilize the cost/benefit analysis provided in the 1996 SDWA amendments to establish such regulations. It is anticipated that the regulations will apply to several of SCW's systems using groundwater supplies. While no assurance can be given as to the nature and cost of any additional compliance measures, if any, Registrant does not believe that such regulations will impose significant compliance costs, since SCW already currently engages in disinfection of its groundwater systems.

Regulation of Radon and Arsenic

Registrant will be subject to new regulations regarding radon and arsenic. EPA must propose an arsenic rule by January 1, 2000 and adopt a rule one year later. The EPA originally had 180 days after enactment of the 1996 SDWA amendments to develop a plan to study ways to reduce arsenic health risk uncertainties and was authorized to enter into cooperative agreements to carry out the study. It is anticipated that the completed study will be available for review in 1999. Depending on the MCL eventually established for arsenic, compliance could cause Registrant to implement costly well-head treatment remedies such as ion exchange or, alternatively, to purchase additional and more expensive water supplies already in compliance, for blending with well sources.

The EPA has withdrawn its proposed radon rule and has arranged for the National Academy of Sciences to conduct a risk assessment and a study of risk-reduction benefits associated with various mitigation measures. The National Academy of Sciences has completed its study and has agreed with much of EPA's original findings but has slightly reduced the ingestion risk initially assumed by EPA. The EPA is expected to establish an MCL based on the findings of the National Academy of Sciences' risk assessment report and to set an alternative MCL based on potential mitigation measures for overall radon reduction by August 1999. Although Registrant is unable to predict the standard for radon, Registrant itself is currently conducting studies to determine the best treatment for affected wells.

Voluntary Efforts to Exceed Surface Water Treatment Standards

SCW is a voluntary member of the EPA's "Partnership for Safe Water", a national program designed to further protect the public from diseases caused by cryptosporidium and other microscopic organisms. As a volunteer in the program, SCW commits to exceed current regulations governing surface water treatment to ensure that its surface treatment facilities are performing as efficiently as possible.

Fluoridation of Water Supplies

Registrant is subject to State of California Assembly Bill 733 which requires fluoridation of water supplies for public water systems serving more than 10,000 service connections. Although the bill requires affected systems to install treatment facilities only when public funds have been made available to cover capital and operating costs, the bill requires the CPUC to authorize cost recovery through rates should public funds for operation of the facilities, once installed, become unavailable in future years.

Matters Relating to Arden-Cordova System

In January, 1997, SCW was notified that ammonium perchlorate in amounts above the state-determined action level had been detected in three of its 27 wells serving its Arden-Cordova system. Aerojet-General Corporation has, in the past, used ammonium perchlorate in their processing as an oxidizer of rocket fuels. SCW took the three wells detected with ammonium perchlorate out of service at that time. Although neither the EPA nor the DOHS has established a drinking water standard for ammonium

perchlorate, DOHS has established an action level of 18 parts per billion ("ppb") which required SCW to notify customers in its Arden-Cordova customer service area of detection of ammonium perchlorate in amounts in excess of this action level. In April, 1997, SCW found ammonium perchlorate in three additional wells and, at that time, removed those wells from service until it was determined that the levels were below the state-determined action level. Those wells were returned to service. SCW periodically monitors of these wells to determine that levels of perchlorate are below the action level currently in effect.

In February 1998, SCW was informed that a substance called nitrosodimethylemine ("NDMA") had been detected in amounts in excess of the EPA reference dosage for health risks in three of its wells in its Arden-Cordova system. Each of the wells has been removed from service. NDMA is an additional by-product from the production of rocket fuel and it is believed that such contamination is related to the activities of Aerojet-General Corporation. Aerojet-General Corporation has reimbursed SCW for constructing a pipeline to interconnect with the City of Folsom water system to provide an alternative source(s) of water supply in SCW's Arden-Cordova customer service area as well as reimburse SCW for costs associated with the drilling and equipping of two new wells.

SCW and Aerojet-General Corporation are in negotiations on other matters related to procedures to address cleanup of the contaminated wells, costs associated with the cleanup, costs associated with increased costs of purchased water as compared to pumped sources and costs associated with developing new sources of groundwater supply. Registrant is unable to predict when the negotiations will be completed or the likely outcome of such negotiations.

Matters Relating to Culver City System

The compound, methyl tertiary butyl ether ("MTBE"), has been detected in the Charnock Basin, located in the city of Santa Monica and within SCW's Culver City customer service area. MTBE is an oxygenate used in reformulated fuels. At the request of the Regional Water Quality Control Board, the City of Santa Monica and the California Environmental Protection Agency, SCW removed two of its wells in the Culver City system from service in October, 1996 to help in efforts to avoid further spread of the MTBE contamination plume. Neither of these wells has been found to be contaminated with MTBE. SCW is purchasing water from the MWD at an increased cost to replace the water supply formerly pumped from the two wells removed from service.

Several studies are under way to determine the possible sources and causes of the MTBE contamination. The federal EPA is pursuing an enforcement effort to reach a settlement with the potentially responsible parties on matters relating to the cleanup of the contamination. Registrant is unable to predict the outcome of the EPA's enforcement efforts. Pursuant to an agreement with SCW, two of the potentially responsible parties have reimbursed SCW's legal and consulting costs related to this matter as well as for increased costs incurred by SCW in purchasing replacement water. SCW and such parties have negotiated a month-to-month extension of this agreement which is anticipated to remain effective until the underlying groundwater basin contamination is remediated.

Bear Valley Electric

SCW has been, in conjunction with the Southern California Edison unit of Edison International, planning to upgrade transmission facilities to 115kv (the "115kv Project") in order to meet increased energy and demand requirements. The 115kv Project is subject to an environmental impact report ("EIR") and delays in approval of the EIR may impact service in SCW's Bear Valley electric customer service area. SCW has, however, taken other measures, including some measures that will be enacted on an emergency basis, to meet load growth in order mitigate delays in approval of the EIR.

WATER SUPPLY

During 1998, the Company supplied a total of 179,927 acre feet of water. Of this amount, approximately 61% came from pumped sources and 39% was purchased from others, principally the MWD. The remaining amount was supplied by the Bureau of Reclamation (the "Bureau") under a no-cost contract. During 1997, the Company produced 199,146 acre feet of water, 54% of which came from pumped sources, 45% was purchased and the remainder was supplied by the Bureau.

The MWD is a water district organized under the laws of the State of California for the purpose of delivering imported water to areas within its jurisdiction. The Company has 52 connections for the water distribution facilities of MWD and other municipal water agencies. MWD imports water from two principal sources: the Colorado River and the State Water Project ("SWP"). Available water supplies from the Colorado River and the SWP have historically been sufficient to meet most of MWD's requirements and MWD's supplies from these sources are anticipated to remain adequate through 1999. However, MWD has taken a number of steps to secure additional storage capacity and increase available water supplies, including effecting transfers of water rights from other sources.

The 1997-1998 water year, which ended September 1998, was labeled a "wet one" by the California Department of Water Resources. The outlook for water supply in 1999 remains favorable. In those customer services areas of SCW which pump groundwater, overall groundwater conditions remain at adequate levels. However, certain of SCW's groundwater supplies have been affected to varying degrees by various forms of contamination which, in some cases, has caused increased reliance on purchased water in its resource mix.

BUSINESS SEGMENTS

AWR currently has two principal business units: water service and electric distribution utility operations conducted through its SCW subsidiary, and its non-regulated activities through its ASUS subsidiary. All activities of Registrant currently are geographically located within the State of California, except for one contract providing customer service and billing services to a utility located in the state of Arizona. SCW is a regulated utility which operates both water and electric systems. On a stand alone basis, AWR has no material assets other than its investments in its subsidiaries. SCW terminated its Golden State Water Company joint venture effective December 31, 1998.

YEAR 2000 ISSUE

Registrant continues to evaluate its exposure to the Year 2000 (Y2K) problem that arises from the fact that many existing computer systems may contain date sensitive embedded technology that uses only two digits to identify a year in the date field. Based on the assumption that the first two digits of the date field are always "19", such systems may misinterpret dates after December 31, 1999. Because Registrant is dependent upon the proper functioning of these computer systems and other equipment containing date sensitive technology, a failure of these systems could have a material and adverse affect on Registrant resulting in business interruption or shutdown, financial loss, regulatory citations and legal liability.

Registrant has been actively assessing its Y2K readiness since early 1997 and has inventoried its significant computer hardware and software programs. Since Registrant is dependent upon its management information and customer service systems, upgrades to these systems have been a priority. Registrant has, since 1995, been in the process of replacing and/or upgrading as necessary its core business information and operating systems with newer technologies, all of which are intended to be Y2K ready. All major upgrades to these systems are completed and were operational at year-end 1998. Costs associated with the implementation and upgrade of major management information and customer service software systems, as

well as upgrades to mainframe hardware systems, have been approved by the CPUC and are being recovered through rates.

In addition to work being done on its internal systems, Registrant has sought compliance certification from external vendors and service providers. Testing on Registrant's interface with financial and other institutions with which it does business is being conducted to ensure Y2K readiness. In order to more fully address Y2K readiness of its field equipment, major vendors and service providers, Registrant engaged the services of a nationally-recognized business consulting firm and has completed its written plan to address the Y2K issue. Registrant has established a Year 2000 Task Force consisting of senior management and operating personnel which will complete the inventory of computer systems and other devices with embedded technology, as well as other considerations potentially not revealed in preliminary internal analyses.

Registrant's general process for addressing the Y2K issue is (i) to inventory all systems that may have a potential Y2K impact, (ii) to determine the materiality of these non-Y2K ready systems, (iii) to replace and test, correct and test, or prepare for the failure of material items that have been determined to be non-Y2K ready, and (iv) to prepare contingency plans. Some, less critical systems may not be fully Y2K ready, but are not anticipated to materially affect Registrant's operations.

Registrant is significantly dependent on third party suppliers, such as energy and telecommunication companies and wholesale water suppliers. In order to conduct its business, Registrant has initiated due diligence with certain of its major service providers to address their Y2K readiness. In the event that such suppliers might be adversely affected by Y2K, Registrant is preparing its contingency plan which will likely include, among other things, increased staffing during critical periods, manual back-up for automated systems and the use of electric generators capable of providing power during a black-out. Registrant does not have, and may never fully have, sufficient information about the Y2K exposure or remediation plans of these third parties to adequately predict the risks posed by them to Registrant. If the third parties have Y2K problems that are not remedied, resulting problems could include loss of utility services and disruption of water supplies.

To date, there have been no significant costs associated with Y2K readiness that have not been approved by the CPUC for recovery through rates. Registrant estimates that it may incur up to \$800,000 in costs depending on the results of on-going tests, to make critical systems Y2K ready. Registrant believes that the future costs, which are prudently incurred, will also be allowed for recovery through rates. The CPUC has notified all utilities under its jurisdiction, including SCW, that it will review their Y2K preparations.

RISK FACTOR SUMMARY

This report (written in plain English) summarizes certain risks of our business that may affect our future financial results. We also periodically file with the Securities and Exchange Commission documents that include more information on these risks. It is important for investors to read these documents.

Litigation

SCW has recently been sued in nine water-quality related lawsuits:

- a suit filed on April 24, 1997 alleging personal injury and property damage as a result of the sale of water from wells located in an area of the San Gabriel Valley that has been designated a federal superfund site

- a suit filed on November 3, 1997 alleging personal injury and property damage as a result of the sale of water; few of our systems are located in the geographical area covered by this suit
- a suit filed on January 8, 1998 alleging personal injury and property damage as a result of the delivery of contaminated water in SCW's Arden-Cordova service area
- a suit filed on February 2, 1998 alleging personal injury and property damage as a result of the sale of water from wells located in an area of the San Gabriel Valley that has been designated a superfund site
- a suit filed on February 4, 1998 alleging personal injury and property damage as a result of the sale of water from wells located in an area of the San Gabriel Valley that has been designated a superfund site
- a suit filed in April 1998 alleging personal injury and property damage as a result of the delivery of contaminated water in SCW's Arden-Cordova service area
- three suits filed on July 30, 1998 alleging personal injury and property damage as a result of the sale of water from wells located in an area of the San Gabriel Valley that has been designated a superfund site

In March 1998, the CPUC issued an order instituting investigation (the "OII") as a result of these types of suits being filed against water utilities in California. The CPUC is seeking to determine:

- whether existing standards and policies regarding drinking water quality adequately protect the public health
- whether water utilities are following existing standards

The lawsuits have been stayed pending the outcome of the OII and a hearing before the First District Court of Appeal on April 19, 1999. We anticipate that the CPUC will issue a decision in the OII on or about June 1999. We are unable to predict the nature of the CPUC's final decision or the outcome of the lawsuits. An adverse outcome in this type of litigation is, however, likely to be material.

The CPUC has authorized a memorandum account for legal expenses incurred by water utilities, including SCW, in the water quality lawsuits. Under the memorandum account procedure, SCW may recover litigation costs from ratepayers to the extent authorized by the CPUC. The CPUC has not yet authorized SCW to recover any of its litigation costs.

Environmental Regulation

We are subject to increasingly stringent environmental regulations that will result in increasing capital and operating costs. These regulations include:

- the 1996 amendments to the Safe Drinking Water Act that require increased testing and treatment of water to reduce specified contaminants to minimum containment levels
- interim regulations expected to be adopted before the end of 1998 requiring increased surface-water treatment to decrease the risk of microbial contamination; these regulations will affect SCW's five surface water treatment plants
- additional regulation of disinfection/disinfection byproducts expected to be adopted before the end of 1998; these regulations will potentially affect two of SCW's systems
- additional regulations expected to be adopted before the end of 1998 requiring disinfection of certain groundwater systems; these regulations will potentially impact several of SCW's systems using groundwater supplies
- potential regulation of radon and arsenic

- new California requirements to fluoridate public water systems serving over 10,000 customers

We may be able to recover costs incurred to comply with these regulations through the ratemaking process for our regulated systems. We may also be able to recover certain of these costs under our contractual arrangements with municipalities. In certain circumstances, we may recover costs from parties responsible or potentially responsible for contamination.

Rates and Regulation

SCW is subject to regulation by the CPUC. AWR and ASUS are not directly subject to CPUC regulation. The CPUC may, however, regulate transactions between SCW and AWR, including the manner in which overhead costs are allocated between SCW and AWR and the pricing of services rendered by SCW to AWR.

SCW's revenues depend substantially on the rates that it is permitted to charge its customers. SCW may increase rates in three ways:

- by filing for a general rate increase
- by filing for recovery of certain expenses
- by filing an "advice letter" for certain plant additions, thereby increasing rate base

In addition, SCW recovers certain supply costs through a balancing account mechanism. Supply costs include the cost of purchased water and power and groundwater production assessments. The balancing account mechanism is intended to insulate SCW's earnings from changes in supply costs that are beyond SCW's control. The balancing account is not, however, designed to insulate SCW's earnings against changes in supply mix. As a result, SCW may not recover increased costs due to increased use of purchased water through the balancing account mechanism. In addition, balancing account adjustments, if authorized by the CPUC, may result in either increases or decreases in revenues attributable to supply costs incurred in prior periods, depending upon whether there has been an undercollection or overcollection of supply costs.

There are also a number of matters pending before the CPUC that may affect our future financial results. These matters include:

- applications filed by SCW to increase rates in four of its 16 rate-making jurisdictions; a final decision is not expected until near year-end 1999
- an application filed to consolidate the rate-making jurisdictions located in SCW's Region III area into a single tariff
- an application filed by SCW for permission to recover certain costs of SCW's participation in the coastal aqueduct extension of the state water project; the ALJ assigned to this matter has issued a proposed decision that denies recovery of our costs for participation in the project; the final order could differ uphold the ALJ's decision or differ materially from his proposed decision
- the OII
- new guidelines under consideration by the CPUC for the acquisition and merger of water utilities and for privatization transactions

Adequacy of Water Supplies

The adequacy of water supplies varies from year to year depending upon a variety of factors, including

- rainfall
- the amount of water stored in reservoirs
- the amount used by our customers and others
- water quality, and
- legal limitations on use.

As a result of heavier than normal rainfall in the winter of 1997-1998, most of California's reservoirs are near capacity and the outlook for water supply in the near term is generally favorable. Population growth and increases in the amount of water used have, however, increased limitations on use to prevent overdrafting of groundwater basins. The import of water from the Colorado River, one of our important sources of supply, is expected to decrease in future years due to the requirements of the Central Arizona Project. We also have in recent years taken wells out of service due to water quality problems.

Water shortages affect us in several ways:

- they adversely affect supply mix by causing us to rely on more expensive purchased water
- they adversely affect operating costs
- they may result in an increase in capital expenditures for building pipelines to connect to alternative sources of supplies and reservoirs and other facilities to conserve or reclaim water

We may be able to recover increased operating and construction costs for our regulated systems through the ratemaking process. We may also be able to recover certain of these costs under the terms of our contractual agreements with municipalities.

In certain circumstances, we may recover these costs from third parties that may be responsible, or potentially responsible, for groundwater contamination. We are currently in negotiations with Aerojet General Corporation regarding costs associated with the cleanup of the groundwater supply for our Arden-Cordova System and for the increased costs of purchasing water and developing new sources of groundwater supply. We are also negotiating with two potentially responsible parties on matters relating to the clean-up and purchase of replacement water in the Charnock Basin located in the cities of Santa Monica and Culver City. These two potentially responsible parties have previously reimbursed us for replacement water and certain legal and consulting expenses. The Charnock Basin is in SCW's service territory.

Water Quality

SCW has detected ammonium perchlorate and nitrosodimethylemine in amounts in excess of certain state or federal limits in wells serving its Arden-Cordova system. Both substances are byproducts from the production of rocket fuel. SCW has taken wells out of service, increased monitoring of other wells and drilled new wells in the area. In addition, SCW is constructing a new pipeline to the City of Folsom's water system in order to obtain an alternative source of supply for its Arden-Cordova customers. Aerojet General Corporation has reimbursed SCW for certain of these costs. Negotiations with Aerojet General Corporation are continuing with respect to other costs.

The compound methyl tertiary butyl ether has been detected in the Charnock Basin. SCW has taken two wells out of service in this area and is purchasing more expensive groundwater from the Metropolitan Water District to replace the water supply formerly obtained from these wells. SCW is negotiating with two of the potentially responsible parties for continuation of recovery of its increased costs.

SCW has recently been sued on water quality issues. In addition, we are subject to increasing regulation relating to water quality matters.

Weather

Our business may be affected by weather in a variety of ways. For instance:

- water volumes sold decrease during wet weather
- water volumes sold decrease during cold weather
- water volumes sold may also decrease during drought conditions if mandatory rationing is imposed
- we may be required to purchase more expensive water and to use less groundwater during drought conditions
- kilowatt-hour sales of electricity decrease if winters are warmer than normal or summers are cooler than normal
- maintenance and capital expenditures decrease during periods of inclement weather
- adverse weather conditions may result in damage to our water and electric systems resulting in increased repair and capital replacement costs, loss of sales and loss of water from broken reservoirs and mains

Weather patterns in California are inherently uncertain. It is therefore difficult to predict from year to year the impact of weather on our financial results.

Unregulated Activities

ASUS was formed for the purpose of, among other things, operating and maintaining municipally-owned water systems and providing billing, meter reading and other services for municipalities and special water districts and making investments in subsidiaries and other entities. These activities present different risks than CPUC-regulated activities. ASUS does not have extensive experience in engaging in these types of activities and must compete with other private parties with more experience and greater capital resources. It must also compete with special water districts and other government agencies that may have a lower cost of funds and other competitive advantages afforded governmental entities.

AWR's ability to earn a profit on these activities will depend upon a variety of factors, including

- its ability to obtain contracts in a competitive marketplace
- its ability to price its services at a level sufficient to enable it to earn a profit
- its ability to recover the costs of obtaining contracts in a competitive marketplace
- the cost of developing the privatization market in California
- its ability to operate in a cost effective matter
- its ability to negotiate contracts containing favorable terms

Our unregulated activities are not currently profitable. As a result, our unregulated activities cannot currently be financed from AWR's earnings. Under California law, SCW is not permitted to issue securities to finance unregulated activities. Our unregulated activities must therefore be financed directly by

AWR or its unregulated subsidiaries or from dividends received by AWR from SCW. To the extent that AWR's activities are financed from dividends from SCW, the funds available for the payment of dividends to AWR's shareholders will be reduced.

Potential Year 2000 Risks

We are currently addressing the effect of the Year 2000 ("Y2K") issue on our reporting systems and operations. We are also assessing operational risks related to our suppliers and vendors and developing contingency plans in order to mitigate this risk. We have not currently experienced significant costs with respect to addressing these issues. We anticipate completion of our assessment of risks related to our suppliers and vendors and our operational contingency plan by June 1999.

The primary business risk associated with Y2K is our ability to continue to treat, transport and distribute water to our customers without interruption. Our operations could be significantly impacted if

- we are unable to resolve or fail to identify all Y2K problems prior to January 1, 2000
- any of our critical suppliers and vendors, such as suppliers of chemicals for water treatment or electric utilities, are unable to resolve or fail to identify all Y2K problems affecting our business prior to January 1, 2000
- we are unable to mitigate or fail to address all operational risks in our contingency plans

Capital Expenditures

We anticipate spending approximately \$46.5 million on capital expenditures during the next 12 months. We anticipate that approximately 45 to 60% of these funds will come from developers and other external sources. The price and terms of this funding will depend upon conditions in the capital markets at the time funds are needed.

We anticipate that capital expenditures will continue to increase due to a variety of factors, including:

- the need to replace aging infrastructure
- the need to comply with increasingly stringent environmental requirements
- the need to address potential water shortage problems
- the need to address water quality problems

Capital expenditures may also increase if AWR is successful in its privatization efforts since many municipalities view privatization as a means to finance needed capital improvements.

Economic Conditions

Our ability to finance capital expenditures, unregulated activities and other matters will depend upon general economic conditions and conditions in the capital markets. Conditions in the capital markets are currently uncertain. We are unable to predict to what extent this uncertainty may impact our access to capital or financing costs or our ability to compete in the privatization market.

Interest rates have recently been declining. Declining interest rates are generally believed to be favorable for utilities because of their high capital costs. On the other hand, SCW's authorized rate of return may be reduced because of lower interest rates. As a result, funds available for the payment of dividends may be reduced.

Sales may also be adversely affected by unfavorable economic conditions if business activity and employment are reduced.

Condemnation

Under California law, a governmental agency may acquire public utility property through the power of eminent domain, also known as condemnation. Although we have not had any of our systems condemned during the past three years, the potential for condemnation nevertheless remains.

ACCOUNTING STANDARDS

In February 1997, the Financial Accounting Standards Board (FASB) issued SFAS No. 130, "Reporting Comprehensive Income," which establishes standards for the reporting and displaying of comprehensive income and its components, such as minimum pension liability, in a full set of general-purpose financial statements. Adoption of this statement, effective for fiscal years beginning after December 15, 1997, did not have a significant impact on the Company's financial statements.

In June 1997, the FASB issued SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," which establishes standards for the method of reporting information about operating segments in annual financial statements and in interim reports issued to shareholders. Adoption of this statement, effective for fiscal years beginning after December 15, 1997, did not have a significant impact on disclosure of segment related information.

In February 1998, the FASB issued SFAS No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits," which amends SFAS No. 87 and SFAS No. 109 and revises employers' disclosure concerning pension and other postretirement benefits plans. Adoption of this statement, effective for fiscal years beginning after December 15, 1997, did not have a significant impact on the Company's financial statements.

In June 1998, the FASB issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," which establishes a new model for accounting for derivative and hedging activities, and supersedes and amends a number of existing standards. Adoption of this statement, effective for fiscal years beginning after June 15, 1999, will not have a significant impact on financial position or results of operation.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Registrant has no derivative financial instruments, financial instruments with significant off-balance sheet risks or financial instruments with concentrations of credit risk. The disclosure required is, therefore, not applicable.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

American States Water Company - Consolidated

Balance Sheets - December 31, 1998 and 1997

Statements of Capitalization - December 31, 1998 and 1997

Statements of Income - for the years ended December 31, 1998, 1997 and 1996

Statements of Changes in Common Shareholders' Equity - for the years ended December 31, 1998, 1997 and 1996

Statements of Cash Flows - for the years ended December 31, 1998, 1997 and 1996

American States Water Company - Parent Company - Condensed

Balance Sheets - December 31, 1998

Statements of Capitalization - December 31, 1998

Statements of Income - for the six months ended December 31, 1998

Statements of Changes in Common Shareholders' Equity - for the six months ended December 31, 1998

Statements of Cash Flows - for the six months ended December 31, 1998

Southern California Water Company

Balance Sheets - December 31, 1998 and 1997

Statements of Capitalization - December 31, 1998 and 1997

Statements of Income - for the years ended December 31, 1998, 1997 and 1996

Statements of Changes in Common Shareholders' Equity - for the years ended December 31, 1998, 1997 and 1996

Statements of Cash Flows - for the years ended December 31, 1998, 1997 and 1996

Notes to Financial Statements

Report of Independent Public Accountants

AMERICAN STATES WATER COMPANY
CONSOLIDATED

BALANCE SHEETS

| (\$ in thousands) | For the years ended December 31, | |
|---|----------------------------------|------------|
| | 1998 | 1997 |
| | ----- | ----- |
| Assets | | |
| UTILITY PLANT, AT COST | | |
| Water | \$ 482,989 | \$ 446,605 |
| Electric | 35,171 | 34,137 |
| | ----- | ----- |
| | 518,160 | 480,742 |
| Less - Accumulated depreciation | (138,423) | (125,020) |
| | ----- | ----- |
| | 379,737 | 355,722 |
| Construction work in progress | 35,016 | 27,901 |
| | ----- | ----- |
| Net utility plant | 414,753 | 383,623 |
| | ----- | ----- |
| OTHER PROPERTY AND INVESTMENTS | 1,077 | 1,355 |
| | ----- | ----- |
| CURRENT ASSETS | | |
| Cash and cash equivalents | 620 | 4,186 |
| Accounts receivable-Customers, less reserves of \$403 in 1998; and \$466 in 1997 | 7,626 | 8,544 |
| Other | 5,301 | 3,614 |
| Unbilled revenue | 9,303 | 9,106 |
| Materials and supplies, at average cost | 994 | 1,299 |
| Supply cost balancing accounts | 4,300 | 4,286 |
| Prepayments | 5,988 | 7,676 |
| Accumulated deferred income taxes - net | 5,156 | 5,783 |
| | ----- | ----- |
| Total current assets | 39,288 | 44,494 |
| | ----- | ----- |
| DEFERRED CHARGES | | |
| Regulatory tax-related assets | 21,506 | 22,337 |
| Other | 8,047 | 5,265 |
| | ----- | ----- |
| Total deferred charges | 29,553 | 27,602 |
| | ----- | ----- |
| Total Assets | \$ 484,671 | \$ 457,074 |
| | ===== | ===== |

The accompanying notes are an integral part of these financial statements

AMERICAN STATES WATER COMPANY
CONSOLIDATED

BALANCE SHEETS

| (\$ in thousands) | For the years ended December 31, | |
|---|----------------------------------|-----------|
| | 1998 | 1997 |
| | ----- | ----- |
| Capitalization and Liabilities | | |
| CAPITALIZATION | | |
| Common shareholders' equity | \$154,299 | \$151,053 |
| Preferred shares | 1,600 | 1,600 |
| Preferred shares - mandatory redemption | 400 | 440 |
| Long-term debt | 120,809 | 115,286 |
| | ----- | ----- |
| Total capitalization | 277,108 | 268,379 |
| | ----- | ----- |
| CURRENT LIABILITIES | | |
| Notes payable to banks | 38,000 | 26,000 |
| Long-term debt and preferred shares - current | 260 | 231 |
| Accounts payable | 10,218 | 11,770 |
| Taxes payable | 5,900 | 9,115 |
| Accrued interest | 1,405 | 1,868 |
| Other | 7,985 | 7,196 |
| | ----- | ----- |
| Total current liabilities | 63,768 | 56,180 |
| | ----- | ----- |
| OTHER CREDITS | | |
| Advances for construction | 54,743 | 55,574 |
| Contributions in aid of construction | 36,530 | 28,467 |
| Accumulated deferred income taxes - net | 46,902 | 42,984 |
| Unamortized investment tax credits | 3,155 | 3,246 |
| Regulatory tax-related liability | 1,906 | 1,950 |
| Other | 559 | 294 |
| | ----- | ----- |
| Total other credits | 143,795 | 132,515 |
| | ----- | ----- |
| TOTAL CAPITALIZATION AND LIABILITIES | \$484,671 | \$457,074 |
| | ===== | ===== |

The accompanying notes are an integral part of these financial statements

AMERICAN STATES WATER COMPANY
CONSOLIDATED

STATEMENTS OF CAPITALIZATION

| (\$ in thousands) | For the years ended 1998 | December 31, 1997 |
|--|-----------------------------|----------------------|
| | ----- | ----- |
| COMMON SHAREHOLDERS' EQUITY: | | |
| Common shares, \$2.50 stated value-- | | |
| Authorized 30,000,000 shares | | |
| Outstanding 8,957,671 in 1998 and 1997 | \$ 22,394 | \$ 22,394 |
| Additional paid-in capital | 74,937 | 74,937 |
| Earnings reinvested in the business | 56,968 | 53,722 |
| | ----- | ----- |
| | 154,299 | 151,053 |
| | ----- | ----- |
| PREFERRED SHARES: \$25 PAR VALUE | | |
| Authorized 64,000 shares | | |
| Outstanding 32,000 shares, 4% Series | 800 | 800 |
| Outstanding 32,000 shares, 4 1/4% Series | 800 | 800 |
| | ----- | ----- |
| | 1,600 | 1,600 |
| | ----- | ----- |
| PREFERRED SHARES SUBJECT TO MANDATORY REDEMPTION | | |
| Requirements: \$25 par value | | |
| Authorized and outstanding 17,600 shares in 1998 and 19,200 shares in 1997, 5% Series | 440 | 480 |
| Less: Preferred shares to be redeemed within one year | (40) | (40) |
| | ----- | ----- |
| | 400 | 440 |
| | ----- | ----- |
| LONG-TERM DEBT | | |
| 5.82% notes due 2003 | 12,500 | 12,500 |
| 10.10% notes due 2009 | -- | 10,000 |
| 6.64% notes due 2013 | 1,100 | 1,100 |
| 6.80% notes due 2013 | 2,000 | 2,000 |
| 8.50% fixed rate obligation due 2013 | 1,882 | 1,947 |
| Variable rate obligation due 2014 | 6,000 | 6,000 |
| Variable rate obligation due 2018 | 630 | -- |
| 6.87% notes due 2023 | 5,000 | 5,000 |
| 7.00% notes due 2023 | 10,000 | 10,000 |
| 7.55% notes due 2025 | 8,000 | 8,000 |
| 7.65% notes due 2025 | 22,000 | 22,000 |
| 5.50% notes due 2026 | 8,000 | 8,000 |
| 6.81% notes due 2028 | 15,000 | -- |
| 9.56% notes due 2031 | 28,000 | 28,000 |
| Other | 917 | 930 |
| | ----- | ----- |
| | 121,029 | 115,477 |
| Less: Current maturities | (220) | (191) |
| | ----- | ----- |
| | 120,809 | 115,286 |
| | ----- | ----- |
| TOTAL CAPITALIZATION | \$ 277,108 | \$ 268,379 |
| | ===== | ===== |

The accompanying notes are an integral part of these financial statements

AMERICAN STATES WATER COMPANY
CONSOLIDATED

STATEMENTS OF INCOME

(\$ in thousand, except per share amounts)

| | For the years ended December 31, | | |
|---|----------------------------------|------------|------------|
| | 1998 | 1997 | 1996 |
| | ----- | ----- | ----- |
| OPERATING REVENUES | | | |
| Water | \$ 134,859 | \$ 140,988 | \$ 139,997 |
| Electric | 13,201 | 12,767 | 11,532 |
| | ----- | ----- | ----- |
| Total operating revenues | 148,060 | 153,755 | 151,529 |
| | ----- | ----- | ----- |
| OPERATING EXPENSES | | | |
| Water purchased | 30,833 | 38,318 | 38,355 |
| Power purchased for resale | 5,013 | 5,188 | 5,825 |
| Power purchased for pumping | 7,009 | 7,554 | 7,711 |
| Groundwater production assessment | 7,567 | 6,847 | 5,946 |
| Supply cost balancing accounts | 28 | 2,813 | 2,064 |
| Other operating expenses | 14,459 | 13,074 | 13,421 |
| Administrative and general expenses | 21,987 | 22,138 | 20,549 |
| Depreciation | 12,538 | 10,952 | 10,102 |
| Maintenance | 7,311 | 7,301 | 7,745 |
| Taxes on income | 10,130 | 9,830 | 10,283 |
| Property and other taxes | 6,124 | 6,282 | 6,099 |
| | ----- | ----- | ----- |
| Total operating expenses | 122,999 | 130,297 | 128,100 |
| | ----- | ----- | ----- |
| OPERATING INCOME | 25,061 | 23,458 | 23,429 |
| | ----- | ----- | ----- |
| OTHER INCOME | | | |
| Total other income - net | 769 | 758 | 531 |
| | ----- | ----- | ----- |
| Income before interest charges | 25,830 | 24,216 | 23,960 |
| | ----- | ----- | ----- |
| INTEREST CHARGES | | | |
| Interest on long-term debt | 9,612 | 8,821 | 8,551 |
| Other interest and amortization of debt expense | 1,595 | 1,336 | 1,949 |
| | ----- | ----- | ----- |
| Total interest charges | 11,207 | 10,157 | 10,500 |
| | ----- | ----- | ----- |
| NET INCOME | 14,623 | 14,059 | 13,460 |
| Dividends on Preferred Shares | (90) | (92) | (94) |
| | ----- | ----- | ----- |
| EARNINGS AVAILABLE FOR COMMON SHAREHOLDERS | \$ 14,533 | \$ 13,967 | \$ 13,366 |
| | ----- | ----- | ----- |
| BASIC EARNINGS PER COMMON SHARE | \$ 1.62 | \$ 1.56 | \$ 1.69 |
| | ----- | ----- | ----- |
| WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING | 8,958 | 8,957 | 7,891 |

The accompanying notes are an integral part of these financial statements

AMERICAN STATES WATER COMPANY
CONSOLIDATED

STATEMENTS OF CHANGES IN COMMON SHAREHOLDERS' EQUITY

| (in thousands) | Common Number of Shares ----- | Shares Amount ----- | Additional Paid-in Capital ----- | Earnings Reinvested in the Business ----- |
|---|--|---------------------------|---|---|
| BALANCES AT DECEMBER 31, 1995 | 7,845 | \$19,613 | \$54,753 | \$47,210 |
| Add: | | | | |
| Net Income | | | | 13,460 |
| Issuance of Common Shares for public offering | 1,000 | 2,500 | 18,090 | |
| under Dividend Reinvestment and 401(k) Plans | 41 | 102 | 802 | |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 94 |
| Dividends on Common Shares - \$1.225 per share | | | | 9,670 |
| | ----- | ----- | ----- | ----- |
| BALANCES AT DECEMBER 31, 1996 | 8,886 | \$22,215 | \$73,645 | \$50,906 |
| Add: | | | | |
| Net Income | | | | 14,059 |
| Issuance of Common Shares for public offering | 72 | 179 | 1,292 | |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 92 |
| Dividends on Common Shares - \$1.245 per share | | | | 11,151 |
| | ----- | ----- | ----- | ----- |
| BALANCES AT DECEMBER 31, 1997 | 8,958 | \$22,394 | \$74,937 | \$53,722 |
| Add: | | | | |
| Net Income | | | | 14,623 |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 90 |
| Dividends on Common Shares - \$1.26 per share | | | | 11,287 |
| | ----- | ----- | ----- | ----- |
| BALANCES AT DECEMBER 31, 1998 | 8,958 | \$22,394 | \$74,937 | \$56,968 |
| | ===== | ===== | ===== | ===== |

The accompanying notes are an integral part of these financial statements

AMERICAN STATES WATER COMPANY
CONSOLIDATED

STATEMENTS OF CASH FLOWS

| (\$ in thousands) | For the years ended December 31, | | |
|---|----------------------------------|-----------|-----------|
| | 1998 | 1997 | 1996 |
| | ----- | ----- | ----- |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | |
| Net income | 14,623 | \$ 14,059 | \$ 13,460 |
| Adjustments for non-cash items: | | | |
| Depreciation and amortization | 12,929 | 11,387 | 10,389 |
| Deferred income taxes and investment tax credits | 5,241 | 826 | 577 |
| Other - net | 2,036 | (1,426) | (1,660) |
| Changes in assets and liabilities: | | | |
| Customer receivables | 918 | (673) | 368 |
| Supply cost balancing accounts | (14) | 1,987 | 1,800 |
| Accounts payable | (1,552) | (1,095) | 6,026 |
| Taxes payable | (3,215) | 3,338 | 215 |
| Other - net | 438 | 341 | 122 |
| | ----- | ----- | ----- |
| Net cash provided | 31,404 | 28,744 | 31,297 |
| | ----- | ----- | ----- |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | | |
| Construction expenditures | (41,826) | (34,717) | (31,953) |
| | ----- | ----- | ----- |
| Net cash used | (41,826) | (34,717) | (31,953) |
| | ----- | ----- | ----- |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | | |
| Issuance of Common Shares | -- | 1,472 | 21,494 |
| Issuance of long-term debt and lease obligations | 15,000 | 8,000 | -- |
| Receipt of advances for and contributions in aid of construction | 3,381 | 1,302 | 2,462 |
| Refunds on advances for construction | (2,651) | (2,957) | (2,088) |
| Retirement or repayments of long-term debt and redemption of preferred shares - net | (9,488) | (198) | (15,447) |
| Net change in notes payable to banks | 12,000 | 10,000 | 7,500 |
| Common and preferred dividends paid | (11,386) | (11,243) | (9,825) |
| | ----- | ----- | ----- |
| Net cash provided | 6,856 | 6,376 | 4,096 |
| | ----- | ----- | ----- |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | (3,566) | 403 | 3,440 |
| CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR | 4,186 | 3,783 | 343 |
| | ----- | ----- | ----- |
| CASH AND CASH EQUIVALENTS, END OF YEAR | 620 | 4,186 | \$ 3,783 |
| | ----- | ----- | ----- |
| TAXES AND INTEREST PAID: | | | |
| Income taxes paid | \$ 5,430 | \$ 6,338 | \$ 10,767 |
| Interest paid | \$ 11,391 | 9,451 | 10,128 |
| | ----- | ----- | ----- |
| NON-CASH TRANSACTIONS: | | | |
| Property installed by developers and conveyed to Company | \$ 1,797 | \$ 2,082 | \$ 957 |
| | ===== | ===== | ===== |

The accompanying notes are an integral part of these financial statements

AMERICAN STATES WATER COMPANY
CONDENSED FINANCIAL INFORMATION OF THE PARENT

BALANCE SHEET

| (\$ in thousands) | December 31, 1998 |
|---|----------------------|
| | ----- |
| Assets | |
| OTHER PROPERTY AND INVESTMENTS | \$ 156,035 |
| CURRENT ASSETS | |
| Cash and cash equivalents | 96 |
| Accounts receivable | 128 |
| Other | 28 |
| Accumulated deferred income taxes - net | (17) |
| | ----- |
| Total current assets | 235 |
| DEFERRED CHARGES | 50 |
| | ===== |
| TOTAL ASSETS | \$ 156,320 |
| | ===== |
| Capitalization and Liabilities | |
| CAPITALIZATION | |
| Common shareholders' equity | \$ 154,299 |
| Preferred shares | 1,600 |
| Preferred shares - mandatory redemption | 400 |
| | ----- |
| Total capitalization | 156,299 |
| | ----- |
| CURRENT LIABILITIES | |
| Intercompany Payable | 104 |
| Accounts payable | 164 |
| Taxes payable | (247) |
| | ----- |
| Total current liabilities | 21 |
| | ----- |
| TOTAL CAPITALIZATION AND LIABILITIES | \$ 156,320 |
| | ===== |

The accompanying notes are an integral part of these financial statements

AMERICAN STATES WATER COMPANY
CONDENSED FINANCIAL INFORMATION OF PARENT

STATEMENT OF CAPITALIZATION

| (\$ in thousands) | December 31, 1998 |
|---|----------------------|
| | ----- |
| COMMON SHAREHOLDERS' EQUITY: | |
| Common shares, \$2.50 stated value-- | |
| Authorized 30,000,000 shares | |
| Outstanding 8,957,671 | \$ 22,394 |
| Additional paid-in capital | 74,937 |
| Earnings reinvested in the business | 56,968 |
| | ----- |
| | 154,299 |
| | ----- |
| PREFERRED SHARES: \$25 PAR VALUE | |
| Authorized 64,000 shares | |
| Outstanding 32,000 shares, 4% Series | 800 |
| Outstanding 32,000 shares, 4 1/4% Series | 800 |
| | ----- |
| | 1,600 |
| | ----- |
| PREFERRED SHARES SUBJECT TO MANDATORY REDEMPTION | |
| Requirements: \$25 par value | |
| Authorized and outstanding 17,600 shares in 1998, 5% Series | 440 |
| Less: Preferred shares to be redeemed within one year | (40) |
| | ----- |
| | 400 |
| | ----- |
| TOTAL CAPITALIZATION | 156,299 |
| | ===== |

The accompanying notes are an integral part of these financial statements

AMERICAN STATES WATER COMPANY
CONDENSED FINANCIAL INFORMATION OF PARENT

STATEMENT OF INCOME

| (\$ in thousand, except per share amounts) | For the six months ended December 31, 1998 |
|--|---|
| | ----- |
| OPERATING REVENUES | |
| Management Fees | \$ 65 |
| OPERATING EXPENSES | |
| Other operating expenses | 3 |
| Customer accounts expense | 21 |
| Administrative and general expenses | 102 |
| Employees' pension and benefits | 1 |
| Maintenance | 1 |
| Amortization | 268 |
| Taxes on income | (231) |
| Property and other taxes | 1 |
| | ----- |
| Total operating expenses | 166 |
| | ----- |
| OPERATING INCOME | (101) |
| | ----- |
| OTHER INCOME | |
| Total other income - net | (462) |
| Dividends from SCW | 5,889 |
| | ----- |
| NET INCOME/(LOSS) | 5,326 |
| Dividends on Preferred Shares | (45) |
| | ----- |
| EARNINGS AVAILABLE FOR COMMON SHAREHOLDERS | \$ 5,282 |
| | ===== |
| BASIC EARNINGS PER COMMON SHARE | \$ 0.59 |
| | ----- |
| WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING | 8,958 |
| | ----- |

Included in Net Income are intercompany dividends which are eliminated as part of the consolidated financial statements

The accompanying notes are an integral part of these financial statements

AMERICAN STATES WATER COMPANY
CONDENSED FINANCIAL INFORMATION OF THE PARENT

STATEMENT OF CHANGES IN COMMON SHAREHOLDERS' EQUITY

| (in thousands) | Common Shares Number of Shares ----- | Amount ----- | Additional Paid-in Capital ----- | Earnings Reinvested in the Business ----- |
|--|---|----------------------------|---|---|
| BALANCES AT JULY 1, 1998 | 8,958 | \$22,394 | \$74,937 | \$52,643 |
| Add: | | | | |
| Net Income | | | | 5,326 |
| Net Increase in Subsidiary Equity | | | | 4,687 |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 45 |
| Dividends on Common Shares - \$.63 per share | | | | 5,643 |
| BALANCES AT DECEMBER 31, 1998 | ----- 8,958 ===== | ----- \$22,394 ===== | ----- \$74,937 ===== | ----- \$56,968 ===== |

AMERICAN STATES WATER COMPANY
CONDENSED FINANCIAL INFORMATION OF PARENT

STATEMENTS OF CASH FLOWS

| (\$ in thousands) | For the six months ended December 31, 1998 ----- |
|---|--|
| CASH FLOWS FROM OPERATING ACTIVITIES: | |
| Net income | 5,326 |
| Adjustments for non-cash items: | |
| Amortization | 268 |
| Deferred income taxes and investment tax credits | 17 |
| Other - net | 317 |
| Changes in assets and liabilities | (135) |
| | ----- |
| Net cash used | 5,793 |
| | ----- |
| CASH FLOWS FROM FINANCING ACTIVITIES: | |
| Common and preferred dividends paid | (5,697) |
| | ----- |
| Net cash provided | (5,697) |
| | ----- |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 96 |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD | -- |
| | ----- |
| CASH AND CASH EQUIVALENTS, END OF PERIOD | \$ 96 |
| | ----- |

The accompanying notes are an integral part of these financial statements

SOUTHERN CALIFORNIA WATER COMPANY

BALANCE SHEETS

| (\$ in thousands) | For the years ended December 31, | |
|---|----------------------------------|------------|
| | 1998 | 1997 |
| | ----- | ----- |
| Assets | | |
| UTILITY PLANT, AT COST | | |
| Water | \$ 482,989 | \$ 446,605 |
| Electric | 35,171 | 34,137 |
| | ----- | ----- |
| | 518,160 | 480,742 |
| Less - Accumulated depreciation | (138,423) | (125,020) |
| | ----- | ----- |
| | 379,737 | 355,722 |
| Construction work in progress | 35,016 | 27,901 |
| | ----- | ----- |
| Net utility plant | 414,753 | 383,623 |
| | ----- | ----- |
| OTHER PROPERTY AND INVESTMENTS | 763 | 1,355 |
| | ----- | ----- |
| CURRENT ASSETS | | |
| Cash and cash equivalents | 524 | 4,186 |
| Accounts receivable-Customers, less reserves of \$403 in 1998; \$466 in 1997 | 7,498 | 8,544 |
| Other | 5,272 | 3,614 |
| Intercompany receivable | 104 | -- |
| Unbilled revenue | 9,303 | 9,106 |
| Materials and supplies, at average cost | 994 | 1,299 |
| Supply cost balancing accounts | 4,300 | 4,286 |
| Prepayments | 5,988 | 7,676 |
| Accumulated deferred income taxes - net | 5,173 | 5,783 |
| | ----- | ----- |
| Total current assets | 39,156 | 44,494 |
| | ----- | ----- |
| DEFERRED CHARGES | | |
| Regulatory tax-related assets | 21,506 | 22,337 |
| Other | 7,997 | 5,265 |
| | ----- | ----- |
| Total deferred charges | 29,503 | 27,602 |
| | ----- | ----- |
| Total Assets | \$ 484,175 | \$ 457,074 |
| | ===== | ===== |

The accompanying notes are an integral part of these financial statements

SOUTHERN CALIFORNIA WATER COMPANY

BALANCE SHEETS

| (\$ in thousands) | For the years ended December 31, | |
|---|----------------------------------|-----------|
| | 1998 | 1997 |
| Capitalization and Liabilities | | |
| CAPITALIZATION | | |
| Common shareholders' equity | \$155,721 | \$151,053 |
| Preferred shares | - | 1,600 |
| Preferred shares - mandatory redemption | - | 440 |
| Long-term debt | 120,809 | 115,286 |
| Total capitalization | 276,530 | 268,379 |
| CURRENT LIABILITIES | | |
| Notes payable to banks | 38,000 | 26,000 |
| Long-term debt and preferred shares - current | 260 | 231 |
| Accounts payable | 10,054 | 11,770 |
| Taxes payable | 6,147 | 9,115 |
| Accrued interest | 1,405 | 1,868 |
| Other | 7,984 | 7,196 |
| Total current liabilities | 63,850 | 56,180 |
| OTHER CREDITS | | |
| Advances for construction | 54,744 | 55,574 |
| Contributions in aid of construction | 36,530 | 28,467 |
| Accumulated deferred income taxes - net | 46,902 | 42,984 |
| Unamortized investment tax credits | 3,155 | 3,246 |
| Regulatory tax-related liability | 1,906 | 1,950 |
| Other | 558 | 294 |
| Total other credits | 143,795 | 132,515 |
| TOTAL CAPITALIZATION AND LIABILITIES | \$484,175 | \$457,074 |

The accompanying notes are an integral part of these financial statements

SOUTHERN CALIFORNIA WATER COMPANY

STATEMENTS OF CAPITALIZATION

| (\$ in thousands) | For the years ended December 31, | |
|---|----------------------------------|-------------------|
| | 1998 | 1997 |
| | ----- | ----- |
| COMMON SHAREHOLDERS' EQUITY: | | |
| Common shares, no par value | | |
| Outstanding 100 in 1998 | | |
| and 8,957,671 in 1997 | \$ 98,391 | \$ 22,394 |
| Additional paid-in capital | -- | 74,937 |
| Earnings reinvested in the business | 57,330 | 53,722 |
| | ----- | ----- |
| | 155,721 | 151,053 |
| | ----- | ----- |
| PREFERRED SHARES: \$25 PAR VALUE | | |
| Authorized 64,000 shares | | |
| Outstanding 32,000 shares, 4% Series | -- | 800 |
| Outstanding 32,000 shares, 4 1/4 % Series | -- | 800 |
| | ----- | ----- |
| | -- | 1,600 |
| | ----- | ----- |
| PREFERRED SHARES SUBJECT TO MANDATORY REDEMPTION | | |
| Requirements: \$25 par value | | |
| Authorized and outstanding 19,200 shares in 1997, 5% Series | -- | 480 |
| Less: Preferred shares to be redeemed within one year | -- | (40) |
| | ----- | ----- |
| | -- | 440 |
| | ----- | ----- |
| LONG-TERM DEBT | | |
| 5.82% notes due 2003 | 12,500 | 12,500 |
| 10.10% notes due 2009 | -- | 10,000 |
| 6.64% notes due 2013 | 1,100 | 1,100 |
| 6.80% notes due 2013 | 2,000 | 2,000 |
| 8.50% fixed rate obligation due 2013 | 1,882 | 1,947 |
| Variable rate obligation due 2014 | 6,000 | 6,000 |
| Variable rate obligation due 2018 | 630 | -- |
| 6.87% notes due 2023 | 5,000 | 5,000 |
| 7.00% notes due 2023 | 10,000 | 10,000 |
| 7.55% notes due 2025 | 8,000 | 8,000 |
| 7.65% notes due 2025 | 22,000 | 22,000 |
| 5.50% notes due 2026 | 8,000 | 8,000 |
| 6.81% notes due 2028 | 15,000 | -- |
| 9.56% notes due 2031 | 28,000 | 28,000 |
| Other | 917 | 930 |
| | ----- | ----- |
| | 121,029 | 115,477 |
| Less: Current maturities | (220) | (191) |
| | ----- | ----- |
| | 120,809 | 115,286 |
| | ----- | ----- |
| TOTAL CAPITALIZATION | \$ 276,530 | \$ 268,379 |
| | ===== | ===== |

The accompanying notes are an integral part of these financial statements. All information has been adjusted to reflect formation of a holding company in 1998.

SOUTHERN CALIFORNIA WATER COMPANY

STATEMENTS OF INCOME

(\$ in thousand, except per share amounts)

| | For the years ended December 31, | | |
|--|----------------------------------|------------|------------|
| | 1998 | 1997 | 1996 |
| | ----- | ----- | ----- |
| OPERATING REVENUES | | | |
| Water | \$ 134,793 | \$ 140,988 | \$ 139,997 |
| Electric | 13,201 | 12,767 | 11,532 |
| | ----- | ----- | ----- |
| Total operating revenues | 147,994 | 153,755 | 151,529 |
| | ----- | ----- | ----- |
| OPERATING EXPENSES | | | |
| Water purchased | 30,833 | 38,318 | 38,355 |
| Power purchased for resale | 5,013 | 5,188 | 5,825 |
| Power purchased for pumping | 7,009 | 7,554 | 7,711 |
| Groundwater production assessment | 7,567 | 6,847 | 5,946 |
| Supply cost balancing accounts | 28 | 2,813 | 2,064 |
| Other operating expenses | 14,434 | 13,074 | 13,421 |
| Administrative and general expenses | 21,884 | 22,138 | 20,549 |
| Depreciation | 12,270 | 10,952 | 10,102 |
| Maintenance | 7,311 | 7,301 | 7,745 |
| Taxes on income | 10,360 | 9,830 | 10,283 |
| Property and other taxes | 6,124 | 6,282 | 6,099 |
| | ----- | ----- | ----- |
| Total operating expenses | 122,833 | 130,297 | 128,100 |
| | ----- | ----- | ----- |
| OPERATING INCOME | 25,161 | 23,458 | 23,429 |
| | ----- | ----- | ----- |
| OTHER INCOME | | | |
| Total other income - net | 1,231 | 758 | 531 |
| | ----- | ----- | ----- |
| Income before interest charges | 26,392 | 24,216 | 23,960 |
| | ----- | ----- | ----- |
| INTEREST CHARGES | | | |
| Interest on long-term debt | 9,612 | 8,821 | 8,551 |
| Other interest and amortization of debt expense | 1,595 | 1,336 | 1,949 |
| | ----- | ----- | ----- |
| Total interest charges | 11,207 | 10,157 | 10,500 |
| | ----- | ----- | ----- |
| NET INCOME | 15,185 | 14,059 | 13,460 |
| Dividends on Preferred Shares | (46) | (92) | (94) |
| EARNINGS AVAILABLE FOR COMMON SHAREHOLDERS | \$ 15,139 | \$ 13,967 | \$ 13,366 |
| BASIC EARNINGS PER COMMON SHARE | \$ 151.39 | \$ 139.67 | \$ 133.66 |
| WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING | 100 | 100 | 100 |

The accompanying notes are an integral part of these financial statements.
All information has been adjusted to reflect formation of holding company in 1998.

SOUTHERN CALIFORNIA WATER COMPANY

STATEMENTS OF CHANGES IN COMMON SHAREHOLDERS' EQUITY

| (in thousands) | Common Shares | | Additional Paid-in Capital | Earnings Reinvested in the Business |
|---|---------------------|-----------|----------------------------------|--|
| | Number of Shares | Amount | | |
| | ----- | ----- | ----- | ----- |
| BALANCES AT DECEMBER 31, 1995 | 7,845 | \$ 19,613 | \$ 54,753 | \$ 47,210 |
| Add: | | | | |
| Net Income | | | | 13,460 |
| Issuance of Common Shares for public offering under Dividend Reinvestment and 401(k) Plans | 1,000 | 2,500 | 18,090 | |
| | 41 | 102 | 802 | |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 94 |
| Dividends on Common Shares - \$1.225 per share | | | | 9,670 |
| | ----- | ----- | ----- | ----- |
| BALANCES AT DECEMBER 31, 1996 | 8,886 | \$ 22,215 | \$ 73,645 | \$ 50,906 |
| Add: | | | | |
| Net Income | | | | 14,059 |
| Issuance of Common Shares for public offering | 72 | 179 | 1,292 | |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 92 |
| Dividends on Common Shares - \$1.245 per share | | | | 11,151 |
| | ----- | ----- | ----- | ----- |
| BALANCES AT DECEMBER 31, 1997 | 8,958 | \$ 22,394 | \$ 74,937 | \$ 53,722 |
| Add: | | | | |
| Formation of Holding Company | (8,858) | \$ 74,397 | (\$74,397) | |
| Transfer Preferred Shares & Investments | | \$ 1,060 | | |
| Net Income | | | | 15,185 |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 45 |
| Dividends on Common Shares - \$.63 per share | | | | 5,643 |
| Dividends on Common Shares - \$58.89 per share | | | | 5,889 |
| | ----- | ----- | ----- | ----- |
| BALANCES AT DECEMBER 31, 1998 | 100 | \$ 98,391 | \$ 0 | \$ 57,330 |
| | ===== | ===== | ===== | ===== |

The accompanying notes are an integral part of these financial statements

STATEMENTS OF CASH FLOWS

(\$ in thousands)

| | For the years ended December 31, | | |
|---|----------------------------------|-----------|-----------|
| | 1998 | 1997 | 1996 |
| | ----- | ----- | ----- |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | |
| Net income | \$ 15,185 | \$ 14,059 | \$ 13,460 |
| Adjustments for non-cash items: | | | |
| Depreciation and amortization | 12,661 | 11,387 | 10,389 |
| Deferred income taxes and investment tax credits | 5,224 | 826 | 577 |
| Other - net | 1,719 | (1,426) | (1,660) |
| Changes in assets and liabilities: | | | |
| Customer receivables | 1,046 | (673) | 368 |
| Supply cost balancing accounts | (14) | 1,987 | 1,800 |
| Accounts payable | (1,716) | (1,095) | 6,026 |
| Taxes payable | (2,968) | 3,338 | 215 |
| Other - net | 362 | 341 | 122 |
| | ----- | ----- | ----- |
| Net cash provided | 31,499 | 28,744 | 31,297 |
| | ----- | ----- | ----- |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | | |
| Construction expenditures | (41,826) | (34,717) | (31,953) |
| | ----- | ----- | ----- |
| Net cash used | (41,826) | (34,717) | (31,953) |
| | ----- | ----- | ----- |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | | |
| Issuance of Common Shares | -- | 1,472 | 21,494 |
| Issuance of long-term debt and lease obligations | 15,000 | 8,000 | -- |
| Receipt of advances for and contributions in aid of construction | 3,381 | 1,302 | 2,462 |
| Refunds on advances for construction | (2,651) | (2,957) | (2,088) |
| Retirement or repayments of long-term debt and redemption of preferred shares - net | (9,488) | (198) | (15,447) |
| Net change in notes payable to banks | 12,000 | 10,000 | 7,500 |
| Common and preferred dividends paid | (11,577) | (11,243) | (9,825) |
| | ----- | ----- | ----- |
| Net cash provided | 6,665 | 6,376 | 4,096 |
| | ----- | ----- | ----- |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | (3,662) | 403 | 3,440 |
| CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR | 4,186 | 3,783 | 343 |
| | ----- | ----- | ----- |
| CASH AND CASH EQUIVALENTS, END OF YEAR | 524 | 4,186 | \$ 3,783 |
| | ----- | ----- | ----- |
| TAXES AND INTEREST PAID: | | | |
| Income taxes paid | \$ 5,430 | \$ 6,338 | \$ 10,767 |
| Interest paid | \$ 11,391 | 9,451 | 10,128 |
| | ----- | ----- | ----- |
| NON-CASH TRANSACTIONS: | | | |
| Property installed by developers and conveyed to Company | \$ 1,797 | \$ 2,082 | \$ 957 |
| | ===== | ===== | ===== |

NOTES TO FINANCIAL STATEMENTS

In April 1998, shareholders of Southern California Water Company (SCW) voted to approve formation of a holding company. The formation process was completed on July 1, 1998 at which time American States Water Company (AWR) became the parent company. As a result of the holding company formation, SCW became one of AWR's two operating subsidiaries. SCW will continue to be a public utility engaged principally in the purchase, production, distribution and sale of water and also the distributor of electricity in several mountain communities. SCW is regulated by the California Public Utilities Commission (CPUC) as to its water and electric business including properties, rates, services, facilities and other matters. The other subsidiary, American States Utility Services, Inc. (ASUS) is a new company which will perform non-regulated, water related services and operations. The consolidated financial statements include the accounts of SCW which comprise virtually all of AWR's assets and revenues.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements include the accounts of American States Water Company and its wholly-owned subsidiaries, Southern California Water Company and American States Utility Services, Inc., collectively referred to as Registrant. Intercompany transactions and balances have been eliminated.

The accounting records for SCW are maintained in accordance with the Uniform System of Accounts prescribed by the CPUC. The preparation of these financial statements required the use of certain estimates by management in determining the company's assets, liabilities, revenues and expenses.

Property and Depreciation - SCW capitalizes as utility plant the cost of additions and replacements of retirement units. Such cost includes labor, material and certain indirect charges. Depreciation is computed on the straight-line, remaining-life basis. For the years 1998, 1997 and 1996, the aggregate provisions for depreciation approximated 2.79%, 2.77% and 2.71% of beginning of the year depreciable plant, respectively.

Interest - Interest is generally not capitalized for financial reporting purposes as such procedure is usually not followed for rate-making purposes.

Revenues - Revenues include amounts billed to customers and an amount of unbilled revenue representing amounts to be billed for usage from the last meter reading date to the end of the accounting period.

Basic Earnings Per Common Share - Basic Earnings per Common Share are based upon the weighted average number of Common Shares outstanding and net income after deducting preferred dividend requirements. There are no dilutive securities. Accordingly, diluted earnings per share is not calculated.

Supply Cost Balancing Accounts - As permitted by the CPUC, SCW maintains water and electric supply cost balancing accounts to account for under-collections and over-collections of revenues designed to recover such costs. Recoverability of such costs is recorded in income and charged to balancing accounts when such costs are incurred. The balancing accounts are reversed when such costs are recovered through rate adjustments. SCW accrues interest on its supply cost balancing accounts at the rate prevailing for 90-day commercial paper.

Debt Issue Expense and Redemption Premiums - Original debt issue expenses are amortized over the lives of the respective issues. Premiums paid on the early redemption of debt which is reacquired through refunding are deferred and amortized over the life of the debt issued to finance the refunding. The redemption premium on debt reacquired without refunding is amortized over the remaining period the debt would have been outstanding.

Other Credits - Advances for construction represent amounts advanced by developers which are generally refundable at either a rate of 22% of the revenue received from the installations for which funds were advanced or in equal annual installments over a 40-year period. Contributions in aid of construction are similar to advances, but require no refunding and are amortized over the useful lives of the related property.

Cash and Cash Equivalents - For purposes of the Statements of Cash Flows, cash and cash equivalents include short-term cash investments with an original maturity of three months or less.

Financial Instrument Risk - Registrant does not carry any financial instruments with off-balance sheet risk nor does its operations result in concentrations of credit risk.

Fair Value of Financial Instruments - The table below estimates the fair value of each represented class of financial instrument. For cash and cash equivalents, accounts receivable and short-term debt, the carrying amount is used. Otherwise, rates available to Registrant at December 31, 1998 and 1997 for debt with similar terms and remaining maturities were used to estimate fair value for long-term debt. Changes in the assumptions will produce differing results.

| (\$ in thousands) | 1998 | | 1997 | |
|------------------------|-----------------|------------|-----------------|------------|
| | Carrying amount | Fair value | Carrying amount | Fair value |
| Financial assets: | | | | |
| Cash | \$ 620 | \$ 620 | \$ 4,186 | \$ 4,186 |
| Accounts receivable | 22,230 | 22,230 | 21,264 | 21,264 |
| Financial liabilities: | | | | |
| Short-term debt | 38,000 | 38,000 | 26,000 | 26,000 |
| Long-term debt | 120,809 | 135,092 | 115,326 | 126,930 |

NOTE 2 - CAPITAL STOCK

All of the series of Preferred Shares outstanding at December 31, 1998 are redeemable at the option of Registrant. At December 31, 1998, the redemption price per share for each series of \$25 Preferred Shares was \$27.00, \$26.50 and \$25.25 for the 4%, 4 1/4% and 5% Series, respectively. To each of the redemption prices must be added accrued and unpaid dividends to the redemption date.

The \$25 Preferred Shares, 5% Series, are subject to mandatory redemption provisions of 1,600 shares per year. The annual aggregate mandatory redemption requirements for this Series for the five years subsequent to December 31, 1998 is \$40,000 each year.

In 1996, Registrant issued 1,000,000 Common Shares through a secondary public offering. In January 1997, Registrant issued 71,500 Common Shares through a secondary public offering. The net proceeds from this sale were used to repay a portion of short-term debt then outstanding.

For the years ended December 31, 1998 and December 31, 1997, all shares issued under Registrant's Common Share Purchase and Dividend Reinvestment Plan (DRP) and the 401(k) Plan were purchased on the open market. For the year ended December 31, 1996, Registrant issued 20,228 and 20,851 Common Shares, respectively, under the DRP and the 401(k) programs. There are 89,226 and 71,408 Common Shares reserved for issuance under the DRP and the 401(k) Plan, respectively, at December 31, 1998. Shares reserved for the 401(k) Plan are in relation to matching contributions made by Registrant and for investment purposes by participants.

As of December 31, 1998 there were no retained earnings restricted as to the payment of cash dividends on Common Shares.

In August 1998, the Board of Directors adopted a Shareholder Rights Plan (Rights Plan) and authorized a dividend distribution of one right (a "Right") to purchase 1/1000th share of Junior Participating Preferred Stock for each outstanding Common Share. The Rights became effective in September 1998 and will expire in September 2008. The Rights Plan is designed to provide shareholders' protection and to maximize shareholder value by encouraging a prospective acquirer to negotiate with the Board.

Each Right represents a right to purchase 1/1000th of Junior Participating Preferred Stock at the price of \$120, subject to adjustment (the "Purchase Price"). Each share of Junior Participating Preferred Stock is entitled to receive a dividend equal to 1000 times any dividend paid on Common Shares and 100 votes per share in any shareholder election. The Rights become exercisable either (i) ten business days following a public announcement that a person or group of persons has acquired a beneficial ownership of 15% or more of AWR's general voting power, other than pursuant to a "qualified offer" or (ii) ten business days (or such later date as may be determined by AWR's Board of Directors) following the commencement of, or the announcement of an intention to make, a tender offer or exchange offer, the consummation of which would result in the beneficial ownership by a person or group of 15% or more of AWR's general voting power. A "qualified offer" is a tender offer or exchange offer for all outstanding Common Shares of AWR, which is determined by AWR's directors to be fair and otherwise in the best interests of AWR and its shareholders.

Until the occurrence of a an event described above, each Right trades with the Common Shares and is not separately transferable. After an event described above occurs, AWR would distribute separately Rights Certificates to Common Shareholders and the Rights would subsequently trade separately from the Common Shares and each holder of a Right, other than the acquiring person whose Rights will thereafter be void, will have the right to receive upon exercise at its then current Purchase Price that number of Common Shares having a market value of two times the Purchase Price of the Right. If AWR merges into the acquiring person, other than a merger which follows a qualified offer at the same or a higher price, or 50% or more of the consolidated assets or earnings power of AWR is sold, the Right becomes a right to purchase Common Shares of the acquiring person having a market value of two times the Purchase Price.

The Board of Directors may determine that in certain circumstances a proposal which would cause a distribution of the Rights is in the best interest of AWR's shareholders. Therefore, the Board of Directors may, at its option, redeem the Rights at a redemption price of \$0.01 per Right.

NOTE 3 - COMPENSATING BALANCES AND BANK DEBT

At December 31, 1998, SCW maintained \$47.0 million in aggregate borrowing capacity with three commercial banks with no compensating balances required. Of this amount, \$38.0 million was outstanding at year-end. Loans can be obtained at the option of SCW and bear interest at rates based on floating prime borrowing rates or at money market rates. Neither AWR nor ASUS have established short term lines of credit.

Short-term borrowing activities for the last three years were as follows:

| (dollars in thousands, except percent) | December 31, | | |
|--|--------------|----------|----------|
| | 1998 | 1997 | 1996 |
| Balance Outstanding at December 31, | \$38,000 | \$26,000 | \$16,000 |
| Interest Rate at December 31, | 5.86% | 6.39% | 6.17% |
| Average Amount Outstanding | 19,309 | \$15,678 | \$26,109 |
| Weighted Average Annual Interest Rate | 6.78% | 6.27% | 5.97% |
| Maximum Amount Outstanding | \$39,000 | \$32,000 | \$36,000 |

NOTE 4 - LONG TERM DEBT

In December 1996, SCW sold \$8 million in tax-exempt debt that was issued through the California Pollution Control Financing Authority. The funds were deposited with a trustee and were used during 1997 to finance water main replacements.

In March 1998, SCW sold the remaining \$15 million under its Series B Medium Term Note Program and in December 1998, SCW redeemed all of its outstanding 10.10% Notes. In January 1999, \$40 million of Series C Medium Term Notes were sold by SCW. The funds were used initially to repay short-term bank borrowings and, after that, fund construction expenditures. Registrant has no mortgage debt, and leases and other similar financial arrangements are not material.

SCW has posted an Irrevocable Letter of Credit, which expires July 31, 1999, in the amount of \$797,979 as security for its self-insured workers' compensation plan. SCW has also provided an Irrevocable Letter of Credit in the amount of \$6,296,000 to a trustee with respect to the variable rate obligation issued by the Three Valleys Municipal Water District.

Annual maturities of all long-term debt, including capitalized leases, amount to \$220,139, \$227,277, \$236,167, \$230,383 and \$199,841 for the 5 years ending December 31, 1999 through 2003, respectively.

NOTE 5 - TAXES ON INCOME

Registrant provides deferred income taxes for temporary differences under Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" (SFAS No. 109) for certain transactions which are recognized for income tax purposes in a period different from that in which they are reported in the financial statements. The most significant items are the tax effects of accelerated depreciation, the supply cost balancing accounts and advances for and contributions in aid of construction. SFAS No. 109 also requires that rate-regulated enterprises record deferred income taxes for temporary differences accorded flow-through treatment at the direction of a regulatory commission. The resulting deferred tax assets and liabilities are recorded at the expected cash flow to be reflected in future rates. Since the CPUC has consistently permitted the recovery of previously flowed-through tax effects, SCW has established regulatory liabilities and assets offsetting such deferred tax assets and liabilities.

Deferred investment tax credits are being amortized to other income ratably over the lives of the property giving rise to the credits.

The significant components of deferred tax assets and deferred tax liabilities, as reflected in the balance sheets, and the accumulated net deferred income tax liabilities at December 31, 1998 and 1997 were:

| (dollars in thousands) | December 31, | |
|---|--------------|------------|
| | 1998 | 1997 |
| Deferred tax assets: | | |
| Balancing accounts | \$ 33 | \$ 27 |
| State tax effect | 5,123 | 5,756 |
| | ----- | ----- |
| | 5,156 | 5,783 |
| | ----- | ----- |
| Deferred tax liabilities | | |
| Depreciation | (43,442) | (40,822) |
| Advances and contributions | 16,694 | 17,005 |
| Other property related | (11,488) | (9,602) |
| Other non-property related | (8,666) | (9,565) |
| | ----- | ----- |
| | (46,902) | (42,984) |
| | ----- | ----- |
| Accumulated deferred income taxes - net | \$(41,746) | \$(37,201) |
| | ----- | ----- |

The current and deferred components of income tax expense are as follows:

| (dollars in thousands) | December 31, | | |
|--|--------------|-----------|-----------|
| | 1998 | 1997 | 1996 |
| Current | | | |
| Federal | \$ 5,219 | \$ 7,205 | \$ 7,224 |
| State | 1,727 | 2,287 | 2,452 |
| | ----- | ----- | ----- |
| Total current tax expense | 6,946 | 9,492 | 9,676 |
| | ----- | ----- | ----- |
| Deferred - Federal and State: | | | |
| Accelerated depreciation | 3,319 | 2,996 | 3,175 |
| Balancing accounts | 6 | (871) | (798) |
| State Water Project | -- | -- | 296 |
| Advances and contributions | -- | (210) | (894) |
| California privilege year franchise tax | (544) | (617) | (683) |
| Adjustments to prior year provision | -- | -- | 410 |
| Other | (398) | (566) | (732) |
| | ----- | ----- | ----- |
| Total deferred tax expense | 2,383 | 732 | 774 |
| | ----- | ----- | ----- |
| Total income tax expense | \$ 9,329 | \$ 10,224 | \$ 10,450 |
| | ----- | ----- | ----- |
| Income taxes included in operating expenses | \$ 10,130 | \$ 9,830 | \$ 10,283 |
| Income taxes included in other income and expenses | | | |
| - - net | (801) | 394 | 167 |
| | ----- | ----- | ----- |
| Total income tax expense | \$ 9,329 | \$ 10,224 | \$ 10,450 |
| | ----- | ----- | ----- |

Additional information regarding taxes on income is set forth in the following table:

| (dollars in thousands, except percent) | December 31, | | |
|--|--------------|-----------|-----------|
| | 1998 | 1997 | 1996 |
| Federal taxes on pre-tax income at statutory rates | \$ 8,470 | \$ 8,451 | \$ 8,368 |
| Increase (decrease) in taxes resulting from: | | | |
| State income tax expense | 1,654 | 1,864 | 2,051 |
| Depreciation | 944 | 853 | 716 |
| Federal benefit of state taxes | (579) | (652) | (718) |
| Adjustments to prior years' provisions | (97) | (143) | 254 |
| Payment of premium on redemption | (813) | -- | -- |
| Other - net | (250) | (149) | (221) |
| Total income tax expense | \$ 9,329 | \$ 10,224 | \$ 10,450 |
| Pre-tax income | \$ 23,952 | \$ 24,145 | \$ 23,910 |
| Effective income tax rate | 38.9% | 42.3% | 43.7% |

NOTE 6 - EMPLOYEE BENEFIT PLANS

Registrant maintains a pension plan (the Plan) which provides eligible employees (those age 21 and older, with one year of service) monthly benefits upon retirement based on average salaries and length of service. The normal retirement benefit is equal to 2% of the five highest consecutive years average earnings multiplied by the number of years of credited service, up to a maximum of 40 years, reduced by a percentage of primary social security benefits. There is also an early retirement option. Annual contributions are made to the Plan which comply with the funding requirements of the Employee Retirement Income Security Act (ERISA). At December 31, 1998, the Company had 431 employees participating in the Plan, 69 of these employees are covered by collective bargaining agreements, the earliest of which expires in 1999.

Registrant also provides all active employees medical, dental and vision care benefits through a medical insurance plan. Eligible employees who retired prior to age 65, and/or their spouses, were able to retain the benefits under the active plan until reaching age 65. Upon reaching age 65, and for those employees retiring at or after age 65, and/or their spouses, continued coverage was provided through a Medicare supplement insurance policy paid for by Registrant.

The CPUC has issued a decision which provides for the recovery in rates of tax-deductible contributions made to a separately trustee fund. In accordance with that decision, SCW established two separate trusts in 1995, one for those retirees who were subject to a collectively bargained agreement and another for all other retirees. SCW's funding policy is to contribute annually an amount at least equal to the revenues authorized to be collected through rates for post-retirement benefit costs. Post-retirement benefit costs for 1993, 1994 and 1995 were estimated at a total of \$1.6 million and have been recorded as a regulatory asset for recovery over a 20 year period.

The following table sets forth the Plan's funded status and amounts recognized in Registrant's balance sheets and the components of net pension cost and accrued post-retirement liability at December 31, 1998 and 1997:

| (dollars in thousands) | Pension Benefits | | Other Benefits | |
|--|------------------|-----------|----------------|------------|
| | 1998 | 1997 | 1998 | 1997 |
| CHANGE IN BENEFIT OBLIGATION: | | | | |
| Benefit Obligation at beginning of year | \$ 33,410 | \$ 28,733 | \$ 4,503 | \$ 4,013 |
| Service Cost | 1,597 | 1,351 | 112 | 120 |
| Interest Cost | 2,278 | 2,112 | 283 | 295 |
| Actuarial Loss/(Gain) | 2,514 | 2,373 | (368) | 225 |
| Benefits Paid | (1,227) | (1,159) | (167) | (150) |
| Benefit Obligation at end of year | \$ 38,572 | \$ 33,410 | \$ 4,363 | \$ 4,503 |
| CHANGES IN PLAN ASSETS: | | | | |
| Fair Value of Plan Assets at beginning of year | \$ 33,433 | \$ 29,240 | \$ 1,104 | \$ 548 |
| Actual Return of Plan Assets | 6,051 | 4,065 | 44 | 49 |
| Employer Contributions | 1,284 | 1,287 | 461 | 656 |
| Benefits Paid | (1,227) | (1,159) | (167) | (150) |
| Fair Value of Plan Assets at end of year | \$ 39,541 | \$ 33,433 | \$ 1,442 | \$ 1,103 |
| RECONCILIATION OF FUNDED STATUS: | | | | |
| Funded Status | \$ 969 | \$ 23 | \$ (2,921) | \$ (3,399) |
| Unrecognized Transition Obligation | 114 | 171 | 6,707 | 7,126 |
| Unrecognized Net Loss/(Gain) | 677 | 1,538 | (1,860) | (1,644) |
| Unrecognized Prior Service Cost | 400 | 444 | (3,427) | (3,627) |
| Prepaid/(Accrued) Pension Cost | \$ 2,160 | \$ 2,176 | \$ (1,501) | \$ (1,544) |
| WEIGHTED-AVERAGE ASSUMPTIONS AS OF DECEMBER 31: | | | | |
| Discount Rate | 6.50% | 7.00% | 6.50% | 7.00% |
| Long-term Rate of Return | 8.00% | 8.00% | 8.00% | 8.00% |
| Salary Assumption | 4.00% | 4.00% | -- | -- |

A sliding scale for assumed health care cost increases was used for both periods, starting at 11% in 1996 declining 1% per year for five years and then remaining at 6% thereafter.

The components of net periodic post-retirement benefits cost for 1998 and 1997 are as follows:

| (dollars in thousands) | Pension Benefits | | Other Benefits | |
|---|------------------|----------|----------------|--------|
| | 1998 | 1997 | 1998 | 1997 |
| COMPONENTS OF NET PERIODIC BENEFITS COST | | | | |
| Service Cost | \$ 1,597 | \$ 1,351 | \$ 112 | \$ 120 |
| Interest Cost | 2,278 | 2,112 | 283 | 294 |
| Actual Return on Plan Assets | (6,051) | (4,065) | (44) | (48) |
| Net Amortization | 3,476 | 1,873 | 67 | 140 |
| Net Periodic Pension Cost | \$ 1,300 | \$ 1,271 | \$ 418 | \$ 506 |

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

| (dollars in thousands) | 1-Percentage-Point Increase ----- | 1-Percentage-Point Decrease ----- |
|---|---|---|
| Effect on Total of Service and Interest Cost Components | \$13 | \$(11) |
| Effect on Postretirement Benefit Obligation | 206 | (180) |

Registrant has a 401(k) Investment Incentive Program under which employees may invest a percentage of their pay, up to a maximum investment prescribed by law, in an investment program managed by an outside investment manager. Contributions to the 401(k) are based upon a percentage of individual employee contributions and, for 1998, 1997 and 1996, totaled \$874,113, \$785,687, and \$839,000, respectively.

NOTE 7 - BUSINESS RISKS AND CONCENTRATION OF SALES

Registrant's utility operations are engaged in supplying water and electric service to the public. SCW is required to provide service and grant credit to customers within its defined service areas. Although SCW has a diversified base of residential, industrial and other customers, revenues derived from commercial and residential water customers accounted for approximately 91% and 93% of total water revenues in 1998 and 1997. SCW faces additional risks associated with weather conditions, adequacy and quality of water supplies, regulatory decisions, pronouncements and laws, water-related litigation, general business conditions and condemnation.

Approximately 39% of SCW's water supply is purchased from wholesalers of imported water, with the remainder produced from owned wells. The long term availability of imported water supplies is dependent upon, among other things, drought conditions throughout the state, increases in population, water quality standards and legislation that may potentially reduce water supplies. SCW does not anticipate any constraints on its imported water supplies in 1999.

NOTE 8 - CONTINGENCIES

In 1998, ASUS was formed to pursue non-regulated opportunities such as long-term leases and operation and maintenance contracts for governmentally-owned water and wastewater systems. And to provide other services for such systems. SCW terminated its Golden State Water Company joint venture effective December 31, 1998. Accordingly, Registrant reserved approximately \$336,000 against future losses and capital account adjustments.

Hearings were held before the CPUC in November 1998 on SCW's filing seeking recovery through rates of \$1.8 million in costs associated with its participation in the coastal aqueduct extension of the State Water Project (the Project). In February 1999, the Administrative Law Judge in this proceeding issued his proposed decision that denied rate recovery of SCW's costs in the Project. A final order from the CPUC is anticipated in 1999. SCW is unable to predict if the CPUC will authorize recovery of all or any of the costs associated with its participation in the Project. Alternate forms of recovery are also being pursued including assessment of costs to new construction based on an equivalent dwelling unit charge or other applicable unit of measurement, which assessment will require CPUC approval prior to implementation or, failing that, sale of SCW's participation in the Project.

SCW has been named as a defendant in ten lawsuits which allege that the SCW delivered contaminated water to its customers. Plaintiffs in these actions seek damages, including general, special, and punitive damages, according to proof of trial, as well as attorney's fees on certain causes of action, costs of suit, and other unspecified relief. Stays have been issued by the respective courts in eight of these cases pending the outcome of the CPUC's investigation into water quality discussed below. One action has been dismissed against SCW and SCW has petitioned for dismissal in the remaining case. Most activity related to these lawsuits has ceased due to the stays although SCW anticipates that plaintiff's attorneys will petition the courts to reconsider their prior decisions. In light of the breadth of plaintiff's claims, the lack of factual information regarding plaintiff's claims and injuries, if any, the fact that no discovery has yet been completed, SCW is unable to determine at this time what, if any, potential liability it may have with respect to these claims. SCW intends to vigorously defend itself against these allegations. Management can not predict the outcome of these proceedings and if SCW is found liable, SCW would pursue recovery through its insurance coverage providers.

In response to those lawsuits and similar actions, in March 1998 the CPUC issued an Order Instituting Investigation (OII) directed to all Class A and B water utilities in the state of California, including SCW, into whether existing standards and policies regarding drinking water quality adequately protect the public health and whether those standards and policies are being uniformly complied with by those water utilities. The OII notes the constitutional and statutory jurisdiction of the CPUC and the DOHS to establish and enforce adherence to water quality standards for water delivered by utilities to their customers and, in the case of the CPUC, to establish rates which permit water utilities to furnish safe water, meeting the established water quality standards at prices which are both affordable and that allow the utility to earn a reasonable return on its investment. SCW has made its filing in this proceeding on a series of questions dealing with the safety of current drinking water standards, compliance by water utilities with such standards, appropriate remedies for failure to comply with safe drinking standards and whether stricter or additional safety drinking water standards are required. The Water Division of the CPUC has issued its report based on these filings by the utilities. Although the OII leaves open the possibility of evidentiary hearings and further action by the CPUC, SCW is currently unable to predict the outcome of this proceeding.

Management believes that proper insurance coverage and reserves are in place to insure against anticipated property, general and product liability and workers' compensation claims.

NOTE 9 - CONSTRUCTION PROGRAM

SCW's 1999 construction budget provides for gross expenditures of approximately \$46.5 million of which \$4.4 million is anticipated to be obtained from developers and others. AWR and ASUS have no material capital expenditure programs.

NOTE 10 - ALLOWANCE FOR DOUBTFUL ACCOUNTS

The table below presents SCW's provision for doubtful accounts charged to expense and accounts written off, net of recoveries for the last three years.

| (dollars in thousands) | December 31, | | |
|---|--------------|--------|--------|
| | 1998 | 1997 | 1996 |
| Balance at beginning of year | \$ 466 | \$ 387 | \$ 648 |
| Provision charged to expense | 631 | 707 | 571 |
| Accounts written off, net of recoveries | (694) | (628) | (832) |
| Balance at end of year | \$ 403 | \$ 466 | \$ 387 |

Neither AWR nor ASUS have established any provision for doubtful accounts.

NOTE 11 - BUSINESS SEGMENTS

Registrant has no material operations other than its SCW subsidiary. The tables below set forth information relating to SCW's operating segments. SCW manages its operations on a regional basis using the five categories below as broad-level measures of profitability. In addition to the amounts set forth, certain assets have been allocated. The identifiable assets are net of respective accumulated provisions for depreciation.

| (dollars in thousands) | Year Ended December 31, 1998 | | | |
|--------------------------------------|------------------------------|--------------------|------------|-----------|
| | Region I | Water Region II | Region III | Electric |
| Operating revenues | \$ 24,927 | \$ 76,304 | \$ 33,552 | \$ 13,211 |
| Operating income before income taxes | 6,799 | 15,615 | 9,261 | 3,847 |
| Identifiable assets | 97,463 | 176,832 | 115,475 | 26,719 |
| Depreciation expense | 2,551 | 4,755 | 3,324 | 1,640 |
| Capital additions | \$ 13,206 | \$ 20,650 | \$ 9,714 | \$ 1,699 |

| (dollars in thousands) | Year Ended December 31, 1997 | | | |
|--------------------------------------|------------------------------|--------------------|------------|-----------|
| | Region I | Water Region II | Region III | Electric |
| Operating revenues | \$ 24,340 | \$ 81,200 | \$ 35,436 | \$ 12,779 |
| Operating income before income taxes | 5,897 | 13,032 | 10,270 | 4,089 |
| Identifiable assets | 87,039 | 162,037 | 109,436 | 25,095 |
| Depreciation expense | 2,306 | 4,483 | 3,162 | 1,001 |
| Capital additions | \$ 10,065 | \$ 18,882 | \$ 8,139 | \$ 2,140 |

| (dollars in thousands) | Year Ended December 31, 1996 | | | |
|--------------------------------------|------------------------------|--------------------|------------|-----------|
| | Region I | Water Region II | Region III | Electric |
| Operating revenues | \$ 23,536 | \$ 81,474 | \$ 34,980 | \$ 11,540 |
| Operating income before income taxes | 4,705 | 14,813 | 10,776 | 3,418 |
| Identifiable assets | 79,974 | 148,078 | 104,390 | 25,333 |
| Depreciation expense | 2,109 | 4,131 | 2,939 | 924 |
| Capital additions | \$ 5,975 | \$ 19,370 | \$ 6,537 | \$ 2,492 |

NOTE 12 - SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

The quarterly financial information presented below is unaudited. The business of Registrant is of a seasonal nature and it is management's opinion that comparisons of earnings for the quarterly periods do not reflect overall trends and changes in Registrant's operations.

| (in thousands, except per share amounts) | Operating Revenues | | Operating Income | | Net Income | | Earnings per Share | |
|--|-----------------------|-----------|---------------------|-----------|------------|-----------|-----------------------|--------|
| | 1998 | 1997 | 1998 | 1997 | 1998 | 1997 | 1998 | 1997 |
| First Quarter | \$ 29,955 | \$ 32,206 | \$ 4,382 | \$ 3,738 | \$ 1,843 | \$ 1,312 | \$0.20 | \$0.14 |
| Second Quarter | 35,001 | 39,343 | 5,586 | 5,372 | 2,767 | 3,080 | 0.31 | 0.34 |
| Third Quarter | 47,002 | 45,700 | 9,432 | 8,385 | 6,374 | 6,044 | 0.71 | 0.67 |
| Fourth Quarter | 36,102 | 36,506 | 5,661 | 5,963 | 3,639 | 3,623 | 0.40 | 0.41 |
| Year | \$148,060 | \$153,755 | \$ 25,061 | \$ 23,458 | \$ 14,623 | \$ 14,059 | \$1.62 | \$1.56 |

NOTE 13 - YEAR 2000 READINESS

Registrant continues to evaluate its exposure to the Year 2000 (Y2K) problem that arises from the fact that many existing computer systems may contain date sensitive embedded technology that uses only two digits to identify a year in the date field. Based on the assumption that the first two digits of the date field are always "19", such systems may misinterpret dates after December 31, 1999. Because Registrant is dependent upon the proper functioning of these computer systems and other equipment containing date sensitive technology, a failure of these systems could have a material and adverse affect on Registrant resulting in business interruption or shutdown, financial loss, regulatory citations and legal liability.

Registrant has been actively assessing its Y2K readiness since early 1997 and has inventoried its significant computer hardware and software programs. Since Registrant is dependent upon its management information and customer service systems, upgrades to these systems have been a priority. Registrant has, since 1995, been in the process of replacing and/or upgrading as necessary its core business information and operating systems with newer technologies, all of which are intended to be Y2K ready. All major upgrades to these systems are completed and were operational at year-end 1998. Costs associated with the implementation and upgrade of major management information and customer service software systems, as well as upgrades to mainframe hardware systems, have been approved by the CPUC and are being recovered through rates.

In addition to work being done on its internal systems, Registrant has sought compliance certification from external vendors and service providers. Testing on Registrant's interface with financial and other institutions with which it does business is being conducted to ensure Y2K readiness. In order to more fully address Y2K readiness of its field equipment, major vendors and service providers, Registrant engaged the services of a nationally-recognized business consulting firm and has completed its written plan to address the Y2K issue. Registrant has established a Year 2000 Task Force consisting of senior management and operating personnel which will complete the inventory of computer systems and other devices with embedded technology, as well as other considerations potentially not revealed in preliminary internal analyses.

Registrant's general process for addressing the Y2K issue is (i) to inventory all systems that may have a potential Y2K impact, (ii) to determine the materiality of these non-Y2K ready systems, (iii) to replace and test, correct and test, or prepare for the failure of material items that have been determined to be non-Y2K ready, and (iv) to prepare contingency plans. Some, less critical systems may not be fully Y2K ready, but are not anticipated to materially affect Registrant's operations.

Registrant is significantly dependent on third party suppliers, such as energy and telecommunication companies and wholesale water suppliers. In order to conduct its business, Registrant has initiated due diligence with certain of its major service providers to address their Y2K readiness. In the event that such suppliers might be adversely affected by Y2K, Registrant is preparing its contingency plan which will likely include, among other things, increased staffing during critical periods, manual back-up for automated systems and the use of electric generators capable of providing power during a black-out.

Registrant does not have, and may never fully have, sufficient information about the Y2K exposure or remediation plans of these third parties to adequately predict the risks posed by them to Registrant. If the third parties have Y2K problems that are not remedied, resulting problems could include loss of utility services and disruption of water supplies.

To date, there have been no significant costs associated with Y2K readiness that have not been approved by the CPUC for recovery through rates. Registrant estimates that it may incur up to \$800,000 in costs depending on the results of on-going tests, to make critical systems Y2K ready. Registrant believes that the future costs, which are prudently incurred, will also be allowed for recovery through rates. The CPUC has notified all utilities under its jurisdiction, including SCW, that it will review their Y2K preparations.

REPORT OF MANAGEMENT

The financial statements contained in this annual report were prepared by the management of American States Water Company, which is responsible for their integrity and objectivity. The financial statements were prepared in accordance with generally accepted accounting principles and include, where necessary, amounts based upon management's best estimates and judgments. All other financial information in the annual report is consistent with the financial statements and is also the responsibility of management.

Registrant maintains systems of internal control which are designed to help safeguard the assets of the Company and provide reasonable assurance that accounting and financial records can be relied upon to generate accurate financial statements. These systems include the hiring and training of qualified personnel, appropriate segregation of duties, delegation of authority and an internal audit function which has reporting responsibility to the Audit Committee of the Board of Directors.

The Audit Committee, composed of three outside directors, exercises oversight of management's discharge of its responsibilities regarding the systems of internal control and financial reporting. The committee periodically meets with management, the internal auditor and the independent accountants to review the work and findings of each. The committee also reviews the qualifications of, and recommends to the Board of Directors, a firm of independent accountants.

The independent accountants, Arthur Andersen LLP, have performed an audit of the financial statements in accordance with generally accepted auditing standards. Their audit gave consideration to Registrant's system of internal accounting control as a basis for establishing the nature, timing and scope of their work. The result of their work is expressed in their Report of Independent Public Accountants.

/s/ Floyd E. Wicks

President, Chief Executive Officer

/s/ McClellan Harris III

Chief Financial Officer,
Vice President - Finance,
Treasurer and Corporate Secretary

March 26, 1999

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Shareholders and the Board of Directors of American States Water Company:

We have audited the accompanying consolidated and condensed balance sheets and statements of capitalization of American States Water Company and its subsidiary, Southern California Water Company (California corporations), as of December 31, 1998 and 1997 and the related statements of income, changes in common shareholders' equity and cash flows for each of the three years in the period ended December 31, 1998. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of American States Water Company and its subsidiary, Southern California Water Company, as of December 31, 1998 and 1997, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles.

/s/ Arthur Andersen LLP

Arthur Andersen LLP
Los Angeles, California

March 26, 1999

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

Information responsive to Part III, Item 10 is included in the Proxy Statement, to be filed by Registrant with the Commission pursuant to Regulation 14A, under the captions therein entitled "Election of Directors" and "Executive Officers - Experience, Security Ownership and Compensation" and is incorporated herein by reference pursuant to General Instruction G(3).

ITEM 11. EXECUTIVE COMPENSATION

Information responsive to Part III, Item 11 is included in the Proxy Statement, to be filed by Registrant with the Commission pursuant to Regulation 14A, under the captions therein entitled "Election of Directors" and "Executive Officers - Experience, Security Ownership and Compensation" and "Performance Graph" and is incorporated herein by reference pursuant to General Instruction G(3).

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

Information responsive to Part III, Item 12 is included in the Proxy Statement, to be filed by Registrant with the Commission pursuant to Regulation 14A, under the captions therein entitled "Election of Directors" and "Executive Officers - Experience, Security Ownership and Compensation" and is incorporated herein by reference pursuant to General Instruction G(3).

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Information responsive to Part III, Item 13 is included in the Proxy Statement, to be filed by Registrant with the Commission pursuant to Regulation 14A, under the captions therein entitled "Election of Directors" and is incorporated herein by reference pursuant to General Instruction G(3).

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

- (a)
 1. Reference is made to the Financial Statements incorporated herein by reference to Part II, Item 8 hereof.
 2. All required schedules may be found in the Financial Statements and Notes to Financial Statements incorporated herein by reference to Part II, Item 8 hereof. Schedules I, III, IV, and V are omitted as they are not applicable.
 3. See (c) below.

(b) Registrant filed a Form 8-K with the Securities and Exchange Commission on November 2, 1998 which contained a discussion and summary of certain risks faced by Registrant in the conduct of its businesses all or any one of which could affect future financial results. The risks discussed included litigation, environmental regulation, rates and CPUC regulation, adequacy of water supplies, water quality, weather, unregulated activities, potential Year 2000 risks, capital expenditures, economic conditions and condemnation. Included as exhibits to the form 8-K were the Amended and restated Articles of American States Water Company, the by-laws of American States Water Company, change-in-control agreements between American States Water Company, Southern California Water Company and certain executives, and change-in-control agreements between Southern California Water Company and certain executives. There were no financial statements filed with this Form 8-K.

(c) Exhibits -

- 3.1 By-Laws of American States Water Company incorporated herein by reference to Registrant's Form 8-K, dated November 2, 1998. Commission File No. 333-47647.
- 3.2 By-laws of Southern California Water Company.(1)
- 3.3 Amended and Restated Articles of Incorporation of American States Water Company incorporated herein by reference to Registrant's Form 8-K, dated November 2, 1998. Commission File No. 333-47647.
- 3.3.1 Certificate of Amendment of Articles of Incorporation, dated August 25, 1998, of American States Water Company.(1)
- 3.4 Restated Articles of Incorporation of Southern California Water Company incorporated herein by reference to Registrant's Form 8-K, dated January 20, 1999. Commission File No. 000-01121.
- 4.1 Amended and Restated Rights Agreement, dated January 25, 1999, by and between American States Water Company and ChaseMellon Shareholder Services, L.L.C., as Rights Agent.(1)
- 4.2 Indenture, dated September 1, 1993 between Southern California Water Company and Chemical Trust Company of California incorporated herein by reference to Registrant's Form 8-K. Registration No. 33-62832.
- 10.1 Agreement of Merger dated as of June 25, 1998 by and among Southern California Water Company, SCW Acquisition Corp. and American States Water Company incorporated herein by reference to Registrant's Form 8-K, dated July 1, 1998. Commission File No. 333-47647.
- 10.2 Deferred Compensation Plan for Directors and Executives incorporated herein by reference to Registrant's Registration Statement on Form S-2. Registration No. 33-5151.(2)

- 10.3 Reimbursement Agreement, dated October 3, 1997, between Southern California Water Company and The Bank of Nova Scotia incorporated herein by reference to Registrant's Form 10-K with respect to the year ended December 31, 1997. Commission File No. 000-01121.
- 10.4 Second Sublease dated October 5, 1984 between Southern California Water Company and Three Valleys Municipal Water District incorporated herein by reference to Registrant's Registration Statement on Form S-2. Registration No. 33-5151.
- 10.5 Note Agreement dated as of May 15, 1991 between Southern California Water Company and Transamerica Occidental Life Insurance Company incorporated herein by reference to Registrant's Form 10-Q with respect to the quarter ended June 30, 1991. Commission File No. 000-01121.
- 10.6 Schedule of omitted Note Agreements, dated May 15, 1991, between Southern California Water Company and Transamerica Annuity Life Insurance Company, and Southern California Water Company and First Colony Life Insurance Company incorporated herein by reference to Registrant's Form 10-Q with respect to the quarter ended June 30, 1991. Commission File No. 000-01121.
- 10.7 Loan Agreement between California Pollution Control Financing Authority and Southern California Water Company, dated as of December 1, 1996.(1)
- 10.8 Agreement for Financing Capital Improvement dated as of June 2, 1992 between Southern California Water Company and Three Valleys Municipal Water District incorporated herein by reference to Registrant's Form 10-K with respect to the year ended December 31, 1992. Commission File No. 000-01121.
- 10.9 Water Supply Agreement dated as of June 1, 1994 between Southern California Water Company and Central Coast Water Authority incorporated herein by reference to Registrant's Form 10-K with respect to the year ended December 31, 1994. Commission File No. 000-01121.
- 10.10 Retirement Plan for Non-Employee Directors of Southern California Water Company, as amended, January 25, 1995 incorporated herein by reference to Registrant's Form 10-K with respect to the year ended December 31, 1994. Commission File No. 000-01121.(2)
- 10.11 Dividend Reinvestment and Common Share Purchase Plan incorporated herein by reference to American States Water Company Rule 424 (b) (3) filing dated August 28, 1998. (Registration No. 33-42218).
- 10.12 Key Executive Long-Term Incentive Plan incorporated herein by reference to Registrant's 1995 Proxy Statement, Commission File No. 00 0-01121.(2)
- 10.13 Energy Management Services Agreement between Southern California Water Company and Enova Energy, Inc. incorporated herein by reference to Registrant's Form 10-K with respect to the year ended December 31, 1996. Commission File No. 000-01121.

- 10.14 Change in Control Agreements, dated as of October 27, 1998, between American States Water Company, Southern California Water Company and certain executives incorporated herein by reference to Registrant's Form 8-K filed November 2, 1998. Commission File No. 333-47647.(2)
- 10.15 Change in Control Agreements, dated as of October 27, 1998, between Southern California Water Company and certain executives incorporated herein by reference to Registrant's Form 8-K filed November 2, 1998. Commission File No. 000-01121.(2)
- 13. 1998 Annual Report to Shareholders.(1)
- 21. Subsidiaries of Registrant.
- 23. Consent of Independent Public Accountants.(1)
- 27. Schedule UT.(1)

(d) None.

-
- (1) Filed concurrently herewith
 - (2) Management contract or compensatory arrangement

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

AMERICAN STATES WATER COMPANY
and its subsidiary
SOUTHERN CALIFORNIA WATER COMPANY

By: /s/ McCLELLAN HARRIS III

McClellan Harris III
Vice President - Finance, Treasurer,
Chief Financial Officer and Secretary

Date: March 26, 1999

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of Registrant and in the capacities and on the dates indicated.

/s/ W. V. CAENEY Date: March 26, 1999

W. V. Caveney
Chairman of the Board and Director

/s/ FLOYD E. WICKS March 26, 1999

Floyd E. Wicks
Principal Executive Officer;
President, CEO and Director

/s/ McCLELLAN HARRIS III March 26, 1999

McClellan Harris III
Principal Financial and Accounting Officer;
CFO, VP - Finance, Treasurer and Secretary

/s/ LINDA J. MATLICK March 26, 1999

Linda J. Matlick
Controller - Southern California Water Company

/s/ JAMES L. ANDERSON March 26, 1999

James L. Anderson, Director

/s/ JEAN E. AUER . March 26, 1999

Jean E. Auer, Director

/s/ N. P. DODGE, JR. . March 26, 1999

N. P. Dodge, Jr., Director

/s/ ANNE M. HOLLOWAY . March 26, 1999

Anne M. Holloway, Director

/s/ ROBERT F. KATHOL . March 26, 1999

Robert F. Kathol, Director

/s/ LLOYD E. ROSS . March 26, 1999

Lloyd E. Ross, Director

BYLAWS

for the regulation, except
as otherwise provided by statute or
its Restated Articles of Incorporation,

of

Southern California Water Company
(a California corporation)

ARTICLE I. Offices.

Section 1. PRINCIPAL EXECUTIVE OFFICE. The principal executive office of the corporation shall be fixed and located at such place as the Board of Directors (herein called the "Board") shall determine. The Board is hereby granted full power and authority to change said principal executive office from one location to another.

Section 2. OTHER OFFICES. Branch or subordinate offices may at any time be established by the Board at any place or places.

ARTICLE II. Meetings of Shareholders.

Section 1. PLACE OF MEETINGS. Meetings of shareholders shall be held either at the principal executive office of the corporation or at any other place within or without the State of California which may be designated either by the Board or by the written consent of all persons entitled to vote thereat, given either before or after the meeting and filed with the Secretary.

Section 2. ANNUAL MEETINGS. The annual meetings of shareholders shall be held on such date and at such time as may be fixed by the Board.

Section 3. SPECIAL MEETINGS. Special meetings of the shareholders, for any purpose or purposes whatsoever, may be called at any time by the Board, the Chairman of the Board, the President, or by the holders of shares entitled to cast not less than ten percent of the votes at such meeting.

ARTICLE III. Directors.

Section 1. POWERS. Subject to limitations of the Articles, these Bylaws and of the California General Corporation Law as to action required to be approved by the shareholders or by the outstanding shares, the business and affairs of the corporation shall be managed and all corporate powers shall be exercised by or under the direction of the Board.

Section 2. NUMBER OF DIRECTORS. The authorized number of directors shall be eight (8).

ARTICLE IV. Officers.

Section 1. OFFICERS. The officers of the corporation shall be a President, a Secretary, and a Chief Financial Officer. The corporation may also have, at the discretion of the Board, such other officers as the business of the corporation may require, each of whom shall hold office for such period, have such authority and perform such duties as the Board may from time to time determine.

Section 2. PRESIDENT. The President shall be the general manager and chief executive officer of the corporation and has, subject to the control of the Board, general supervision, direction and control of the business and officers of the corporation. The President shall preside at all meetings of the shareholders and at all meetings of the Board. The President has the general powers and duties of management usually vested in the office of president and general manager of a corporation and has such other powers and duties as may be prescribed by the Board.

Section 3. SECRETARY. The Secretary shall keep or cause to be kept, at the principal executive office or such other place as the Board may order, a book of minutes of all meetings of the shareholders, the Board and its committees, and a share register or a duplicate share register.

The Secretary shall give, or cause to be given, notice of all the meetings of the shareholders and of the Board and any committees thereof required by the Bylaws or by law to be given, shall keep the seal of the corporation in safe custody, and shall have such other powers and perform such other duties as may be prescribed by the Board.

Section 4. CHIEF FINANCIAL OFFICER. The Chief Financial Officer is the chief financial officer of the corporation and shall keep and maintain, or cause to be kept and maintained, adequate and correct accounts of the properties and business transactions of the corporation, and shall send or cause to be sent to the shareholders of the corporation such financial statements and reports as are by law or these Bylaws required to be sent to them. The books of account shall at all times be open to inspection by any director.

The Chief Financial Officer shall deposit all moneys and other valuables in the name and to the credit of the corporation with such depositaries as may be designated by the Board. The Chief Financial Officer shall disburse the funds of the corporation as may be ordered by the Board, shall render to the President and the directors, whenever they request it, an account of all transactions as Treasurer and of the financial condition of the corporation, and shall have such other powers and perform such other duties as may be prescribed by the Board.

ARTICLE V. Other Provisions.

Section 1. ANNUAL REPORT TO SHAREHOLDERS. The annual report to shareholders referred to in Section 1501 of the California General Corporation Law is expressly waived, but nothing herein shall be interpreted as prohibiting the Board from issuing annual or other periodic reports to shareholders.

Section 2. CONSTRUCTION AND DEFINITIONS. Unless the context otherwise requires, the general provisions, rules of construction and definitions contained in the General Provisions of the California Corporations Code and in the California General Corporation Law shall govern the construction of these Bylaws.

ARTICLE VI. Amendments.

These Bylaws may be amended or repealed either by approval of the outstanding shares (as defined in Section 152 of the California General Corporation Law) or by the approval of the Board; provided, however, that after the issuance of shares, a bylaw specifying or changing a fixed number of directors or the maximum or minimum number or changing from a fixed to a variable number of directors or vice versa may be adopted only by approval of the outstanding shares, and a bylaw reducing the fixed number or the minimum number of directors to a number less than five shall be subject to the provisions of Section 212(a) of the California General Corporation Law.

CERTIFICATE OF SECRETARY
of
Southern California Water Company
(a California corporation)

I hereby certify that I am the duly elected and acting Secretary of said corporation and that the foregoing Bylaws, comprising 3 pages, constitute the Bylaws of said corporation as duly adopted by unanimous written consent of the Board of Directors on January 25, 1999.

McClellan Harris III,
Secretary

CERTIFICATE OF AMENDMENT
OF
AMENDED AND RESTATED ARTICLES OF INCORPORATION
OF
AMERICAN STATES WATER COMPANY
(A CALIFORNIA CORPORATION)

Floyd E. Wicks and McClellan Harris III certify that:

1. They are the duly elected and acting President and Secretary, respectively of Southern California Water Company (the "Corporation").

2. The Amended and Restated Articles of Incorporation of the Corporation shall be amended by striking in its entirety the first full paragraph of Article IV of the Amended and Restated Articles of Incorporation which now reads:

"This Corporation is authorized to issue three classes of stock to be designated, respectively, "New Preferred Shares", "Preferred Shares", and "Common Shares". The total number of shares which this Corporation is authorized to issue is 30,233,200; 150,000 shares are to be New Preferred Shares with no par value and a stated value of \$100 per share and an aggregate stated value of \$15,000,000; 83,200 shares are to be Preferred Shares with a par value of \$25 per share and an aggregate par value of \$2,080,000; and 30,000,000 shares are to be Common

Shares with no par value and a stated value of \$2.50 per share and an aggregate par value of \$75,000,000."

and substituting therefore the following paragraph to read in full as follows:

"This Corporation is authorized to issue three classes of stock to be designated, respectively, "New Preferred Shares", "Preferred Shares", and "Common Shares". The total number of shares which this Corporation is authorized to issue is 30,231,600; 150,000 shares are to be New Preferred Shares with no par value and a stated value of \$100 per share and an aggregate stated value of \$15,000,000; 81,600 shares are to be Preferred Shares with a par value of \$25 per share and an aggregate par value of \$2,040,000; and 30,000,000 shares are to be Common Shares with no par value and a stated value of \$2.50 per share and an aggregate par value of \$75,000,000."

3. The Restated Articles of Incorporation of the Corporation shall be further amended by striking in its entirety paragraph (ii) of Section 15 of Article IV of the Amended and Restated Articles of Incorporation which now reads:

"(ii) Number of Shares. The authorized number of shares constituting said Preferred Shares, 5% Series, shall be 19,200."

and substituting therefore the following paragraph to read in full as follows:

"(ii) Number of Shares. The authorized number of shares constituting said Preferred Shares, 5% Series, shall be 17,600."

4. The foregoing amendment set forth in paragraph 3 of this Certificate, as well as the portion of the amendment in Article IV, Section 7, paragraph (ii) that relates to the "Preferred Shares," are each amendments that may be adopted by the Board of Directors alone (and which were so adopted) because the amendments are required by Section 510 of the California General Corporation Law to reflect the reacquisition of a portion of the Corporation's Preferred Shares, 5% Series, \$25 par value, in accordance with the sinking fund provisions thereof. Such reacquired Preferred Shares cannot be reissued.

5. The foregoing amendments have been duly approved by the Board of Directors as required by Section 905(b) of the California General Corporation Law.

We further declare, under penalty of perjury under the laws of the State of California, that the matters set forth in this Certificate of Amendment are true and correct.

IN WITNESS WHEREOF, the undersigned have executed this Certificate in San Dimas, California on this 25th day of August, 1998.

FLOYD E. WICKS, President

McCLELLAN HARRIS III, Secretary

August 25, 1998

Office of the Secretary of State
State of California
Attn: Certification Unit
1500 - 11th Street
Sacramento, CA 95814

Ladies and Gentlemen:

RE: American States Water Company
Corporate No. 137226

Please find enclosed herewith for filing two (2) originals of a Certificate of Amendment of Restated Articles of Incorporation of American States Water Company, a California Corporation. One original should be filed with your office and the other is to be date stamped and returned to me in the enclosed self-addressed, prepaid envelope.

In addition, please find the Corporation's check for \$30.00, which represents the filing fee.

Any questions regarding this matter should be directed to the undersigned person at (909) 394-3600, extension 705.

Sincerely,

McClellan Harris III
Vice President - Finance,

Chief Financial Officer,
Treasurer and Secretary

Enclosure(s)

AMENDED AND RESTATED RIGHTS AGREEMENT
BETWEEN
AMERICAN STATES WATER COMPANY
AND
CHASEMELLON SHAREHOLDER SERVICES, L.L.C.,
as RIGHTS AGENT

_____, 1999

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AMENDED AND RESTATED RIGHTS AGREEMENT

AMENDED AND RESTATED RIGHTS AGREEMENT, dated as of January 25, 1999 (the "Agreement") between American States Water Company, a California corporation (the "Company"), and ChaseMellon Shareholder Services, L.L.C., as Rights Agent.

W I T N E S S E T H

WHEREAS, the Board of Directors of the Company has authorized and declared the distribution of one right for (i) each share of Common Shares of the Company ("Common Stock") outstanding at the Close of Business (as hereinafter defined) on September 22, 1998 (the "Rights Record Date"), each right representing the right to purchase one Unit consisting, initially, of one one-thousandth of a share of Junior Participating Preferred Stock, and (ii) each additional share of Common Stock which shall become outstanding between the Rights Record Date and the earliest of the Distribution Date, the Expiration Date (as such terms are hereinafter defined) and the date, if any, on which such rights may be redeemed, all upon the terms and subject to the conditions hereinafter set forth (each such right being hereinafter referred to as a "Right");

NOW, THEREFORE, the parties agree as follows:

SECTION 1. CERTAIN DEFINITIONS.

(a) For purposes of this Agreement, the following terms have the meanings indicated:

"Acquiring Person" shall mean any Person who or which, alone or together with all Affiliates and Associates of such Person, shall be the Beneficial Owner (within the meaning of Section 1(b)) of a Substantial Block of Voting Stock, but shall not include (i) an Exempt Person or (ii) any Person who or which acquires a Substantial Block of Voting Stock in connection with a transaction or series of transactions approved prior to such transaction or transactions by the Board of Directors of the Company; provided that no person shall become an Acquiring Person solely as a result of a reduction in the number of shares of Voting Stock outstanding, unless and until such Person shall thereafter become the Beneficial Owner of additional shares constituting 1% or more of the general voting power of the Company. If the Directors determine in good faith that a Person who would otherwise be an Acquiring Person has become such inadvertently, and such Person divests as promptly as practicable a sufficient number of shares so that such Person would no longer be an Acquiring Person as herein defined, then such Person shall not be deemed

to be an Acquiring Person unless and until such Person shall become the Beneficial Owner of additional shares constituting 1% or more of the general voting power of the Company.

"Affiliate" and "Associate" shall have the respective meanings ascribed to such terms in Rule 12b-2 of the General Rules and Regulations under the Exchange Act, as in effect as of the date hereof.

"Business Day" shall mean any day other than a Saturday, Sunday or day on which banking institutions in the State of California are authorized or obligated by law or executive order to close.

"Close of Business" on any given date shall mean 5:00 p.m., Los Angeles time, on such date; provided, however, that if such date is not a Business Day it shall mean 5:00 p.m., Los Angeles time, on the next succeeding Business Day.

"Common Stock" shall have the meaning assigned to it in the preamble; and "common stock" when used with reference to Persons other than the Company shall mean: (i) in the case of Persons organized in corporate form, the capital stock or equity security with the greatest voting power of such Person or, if such Person is a Subsidiary of another Person, of the Person or Persons which ultimately control such first-mentioned Person; and (ii) in the case of Persons not organized in corporate form, the units of beneficial interest which (A) represent the right to participate generally in the profits and losses of such Person (including without limitation any flow-through tax benefits resulting from an ownership interest in such Person) and (B) are entitled to exercise the greatest voting power of such Person or, in the case of a limited partnership, shall have the power to remove the general partner or partners.

"Distribution Date" shall have the meaning assigned to it in Section 3(a).

"Equivalent Stock" shall have the meaning assigned to it in Section 7(a).

"Exchange Act" shall mean the Securities Exchange Act of 1934, as amended from time to time.

"Exempt Person" shall mean the Company, any Subsidiary of the Company and any employee benefit plan or employee stock plan of the Company or of any Subsidiary of the Company, or any trust or other entity organized, established or holding shares of Common Stock by, for or pursuant to, the terms of any such plan.

"Expiration Date" shall have the meaning assigned to it in Section 7(a).

"Offer Date" shall have the meaning assigned to it in Section 3(a).

"Person" shall mean any individual, firm, corporation, partnership, trust or other entity and shall include any successor by merger (or otherwise) of any of the foregoing.

"Principal Party" shall have the meaning assigned to it in Section 13(b).

"Purchase Price" shall mean the price payable for one Unit upon exercise of a Right.

"Qualified Offer" shall mean a tender or exchange offer for all outstanding Common Stock at a price and on terms determined to be adequate and otherwise in the best interests of the Company and its shareholders (other than the Person or an Affiliate or Associate thereof on whose behalf the offer is made) by at least a majority of the Directors who are not representatives of or affiliated with the Person making such offer or any Affiliate or Associate of such Person.

"Redemption Price" shall have the meaning assigned to it in Section 23(a).

"Right" shall have the meaning assigned to it in the preamble.

"Rights Record Date" shall have the meaning assigned to it in the preamble.

"Subject Shares" shall mean the class or series of shares then issuable on exercise of the Rights.

"Stock Acquisition Date" shall mean the date of the first public announcement by the Company or an Acquiring Person that an Acquiring Person has become such.

"Subsidiary" shall mean, with respect to any Person, a corporation or other entity the securities or other ownership interests of which having ordinary voting power sufficient to elect a majority of the board of directors or other persons performing similar functions are at the time directly or indirectly owned by such Person and any Affiliate of such Person.

"Substantial Block" shall mean a number of shares of Voting Stock having in the aggregate 15 percent or more of the general voting power.

"Trading Day" shall have the meaning assigned to it in Section 11(d).

"Unit" shall mean the shares or other securities issuable upon exercise of one Right, initially one one-thousandth of a share of Junior Participating Preferred Stock of the Company having the rights and preferences set forth in Exhibit C, before any adjustment pursuant to Section 11(a)(ii) or Section 13.

"Voting Stock" shall mean shares of the Company's capital stock the holders of which have general voting power.

(b) For purposes of this Agreement, a Person shall be deemed the "Beneficial Owner" of any securities:

(i) which such Person or any of such Person's Affiliates or Associates beneficially owns, directly or indirectly, for purposes of Section 13(d) of the Exchange Act and Rule 13d-3 promulgated under the Exchange Act, in each case as in effect on the date hereof;

(ii) which such Person or any of such Person's Affiliates or Associates has (A) the right to acquire (whether such right is exercisable immediately or only after the passage of time) pursuant to any agreement, arrangement or understanding (whether or not in writing) or upon the exercise of any conversion, exchange or purchase rights (other than the Rights), warrants or options, or otherwise; provided, however, that a Person shall not be deemed the "Beneficial Owner" of securities tendered pursuant to a tender or exchange offer made by or on behalf of such Person or any of such Person's Affiliates or Associates until such tendered securities are accepted for payment or exchange; or (B) the right to vote or to direct the voting of, pursuant to any agreement, arrangement or understanding (whether or not in writing); or (C) the right to dispose or to direct the disposition of, pursuant to any agreement, arrangement or understanding (whether or not in writing); or

(iii) which are Beneficially Owned, directly or indirectly, by any other Person with which such Person or any of such Person's Affiliates or Associates has any agreement, arrangement or understanding for the purpose of acquiring, holding, voting or disposing of any securities of the Company;

provided, however, that a Person shall not be deemed the Beneficial Owner of, or to Beneficially Own, any security if the agreement, arrangement or understanding to vote such security (1) arises solely from the grant of a revocable proxy or consent given to such Person in connection with a public proxy or consent solicitation made pursuant to, and in accordance with, the applicable rules and regulations under the Exchange Act, and

(2) is not also then reportable on Schedule 13D (or any comparable or successor report) under the Exchange Act; provided, further, that a Person engaged in business as an underwriter of securities shall not be deemed the "Beneficial Owner" of securities acquired through such person's participation in good faith in a firm commitment underwriting until the expiration of the 40-day period immediately following the date of such acquisition.

SECTION 2. APPOINTMENT OF RIGHTS AGENT. The Company hereby appoints the Rights Agent to act as agent for the Company and the Rights Agent hereby accepts such appointment. The Company may from time to time appoint such Co-Rights Agent or Agents as it may deem necessary or desirable and determine the respective duties of the Rights Agent and the Co-Rights Agents.

SECTION 3. ISSUANCE OF RIGHT CERTIFICATES.

(a) Until the Close of Business on the earlier of (i) the tenth Business Day after a Stock Acquisition Date or (ii) the tenth Business Day (or such later date as the Company's Board of Directors shall determine) after the date of the commencement by any Person (other than an Exempt Person) of, or the date of the first public announcement (such commencement date or announcement date being herein referred to as the "Offer Date") of the intent of any Person (other than an Exempt Person) to commence, a tender or exchange offer upon the successful consummation of which such Person, together with its Affiliates and Associates, would be the Beneficial Owner of 15 percent or more of the then outstanding Voting Stock (irrespective of whether any shares are actually purchased pursuant to such offer) (the tenth Business Day after the first to occur of a Stock Acquisition Date or an Offer Date being herein referred to as the "Distribution Date"),

(i) the Rights will automatically attach to, and be evidenced by, the certificates for Common Stock registered in the names of the holders of Common Stock (which certificates for Common Stock shall be deemed also to be Right Certificates) and not by separate Right Certificates, and

(ii) each Right will be transferable only in connection with the transfer of the underlying shares of Common Stock.

As soon as practicable after the Distribution Date, the Rights Agent will mail, by first-class, insured, postage prepaid mail, to each record holder of Common Stock as of the Close of Business on the Distribution Date, as shown by the records of the Company at the Close of Business on the Distribution Date, at the address of such holder shown on such records, a Right Certificate, in substantially the form of Exhibit A hereto, evidencing one Right for each share of Common Stock so held.

(b) As soon as practicable after the Rights Record Date, the Company will send a copy of a Summary of Rights, in substantially the form attached hereto as Exhibit B, by first-class mail, postage prepaid, to each record holder of Common Stock as

of the Close of Business on the Rights Record Date, at the address of such holder shown on the records of the Company.

(c) The Company will cause certificates for Common Stock issued after the Rights Record Date (including replacement certificates for shares of Common Stock outstanding on or prior to the Rights Record Date), but prior to the earliest of (i) the Distribution Date, (ii) the Expiration Date and (iii) the date, if any, on which the Rights may be redeemed, to have impressed on, printed on, written on or otherwise affixed to them the following legend:

This certificate also entitles the holder hereof to certain Rights as set forth in the Rights Agreement between the Company and ChaseMellon Shareholder Services L.L.C., as Rights Agent, as the same shall be amended from time to time (the "Rights Agreement"), the terms of which are hereby incorporated herein by reference and a copy of which is on file at the principal executive offices of the Company. Under certain circumstances, as set forth in the Rights Agreement, such Rights will be evidenced by separate certificates and will no longer be evidenced by this certificate. The Company will mail to the holder of this certificate a copy of the Rights Agreement without charge after receipt of a written request therefor. Under certain circumstances set forth in the Rights Agreement, Rights issued to, or held by, any Person who is, was or becomes an Acquiring Person or any Affiliate or Associate thereof (as such terms are defined in the Rights Agreement) or certain transferees of any thereof, whether currently held by or on behalf of such Person or by any subsequent holder, may be limited as provided in Section 7(f) of the Rights Agreement.

With respect to such certificates containing the foregoing legend, until the Distribution Date, the Rights associated with Common Stock represented by such certificates shall be evidenced by such certificates alone, and the surrender for transfer of any such certificates shall also constitute the transfer of the Rights associated with the Common Stock represented by such certificate.

(d) Until the Distribution Date, the surrender for transfer of any of the certificates for Common Stock outstanding on or after the Rights Record Date, with or without a copy of the Summary of Rights attached thereto and with or without the legend set forth in subsection (c) above, shall also constitute the transfer of the Rights associated with such Common Stock. After the Distribution Date, the Rights will be evidenced solely by the Right Certificates.

SECTION 4. FORM OF RIGHT CERTIFICATES.

(a) The Right Certificates (and the forms of assignment and certification and of election to purchase shares to be printed on the reverse thereof) shall be in substantially the form of Exhibit A hereto and may have such marks of

identification or designation and such legends, summaries or endorsements printed thereon as the Company may deem appropriate and as are not inconsistent with the provisions of this Agreement, or as may be required to comply with any law or with any rule or regulation made pursuant thereto or with any rule or regulation of any stock exchange on which the Rights may from time to time be listed, or to conform to usage.

(b) Any Right Certificate issued pursuant to Section 3(a) or Section 22 that represents Rights Beneficially Owned by: (i) an Acquiring Person or any Associate or Affiliate of any Acquiring Person, (ii) a transferee of an Acquiring Person (or of any such Associate or Affiliate) who becomes a transferee after the Acquiring Person becomes such, or (iii) a transferee of an Acquiring Person (or of any such Associate or Affiliate) who becomes a transferee prior to or concurrently with the Acquiring Person becoming such and receives such Rights pursuant to either (A) a transfer (whether or not for consideration) from the Acquiring Person to holders of equity interests in such Acquiring Person or to any Person with whom such Acquiring Person has any continuing agreement, arrangement or understanding regarding the transferred Rights, or (B) a transfer which the Board of Directors of the Company has determined is part of a plan, arrangement or understanding which has as a primary purpose or effect avoidance of Section 7(f), and any Right Certificate issued pursuant to Section 6 or Section 11 upon transfer, exchange, replacement or adjustment of any other Right Certificate referred to in this sentence, shall contain (to the extent feasible and reasonably identifiable as such) the following legend:

The Rights represented by this Right Certificate are or were beneficially owned by a Person who was or became an Acquiring Person or an Affiliate or Associate of an Acquiring Person (as such terms are defined in the Rights Agreement) or certain transferees thereof. Accordingly, under certain circumstances as provided in the Rights Agreement, this Right Certificate and the Rights represented hereby may be limited as provided in Section 7(f) of such Agreement.

SECTION 5. COUNTERSIGNATURE AND REGISTRATION.

(a) The Right Certificates shall be executed on behalf of the Company by its Chairman of the Board, its President or any of its Vice Presidents, either manually or by facsimile signature, and have affixed thereto the Company's seal or a facsimile thereof which shall be attested by the Secretary or an Assistant Secretary of the Company, either manually or by facsimile signature. The Right Certificates shall be manually countersigned by the Rights Agent and shall not be valid for any purpose unless so countersigned. In case any officer of the Company who shall have signed any of the Right Certificates shall cease to be such officer of the Company before countersignature by the Rights Agent and issuance and delivery by the Company, such Right Certificates, nevertheless, may be countersigned by the Rights Agent, issued and delivered with the same force and effect as though the person who signed such Right Certificates had not ceased to be such officer of the Company; and any Right Certificate may be signed on behalf of the Company by any person who, at the actual date of the execution of such

Right Certificate, shall be a proper officer (as specified above) of the Company to sign such Right Certificate, although at the date of the execution of this Rights Agreement any such person was not such an officer.

(b) Following the Distribution Date, the Rights Agent will keep or cause to be kept books for registration and transfer of the Right Certificates issued hereunder. Such books shall show the names and addresses of the respective holders of the Right Certificates, the number of Rights evidenced on its face by each Right Certificate, the date of each Right Certificate and the number of each Right Certificate.

SECTION 6. TRANSFER, SPLIT UP, COMBINATION AND EXCHANGE OF RIGHT CERTIFICATES; MUTILATED, DESTROYED, LOST OR STOLEN RIGHT CERTIFICATES.

(a) Subject to the provisions of Section 4(b), Section 7(f) and Section 14, at any time after the Close of Business on the Distribution Date, and prior to the Close of Business on the Expiration Date or the day prior to the day, if any, on which the Rights are to be redeemed pursuant to Section 23, any Right Certificate or Certificates may be transferred, split up, combined or exchanged for another Right Certificate or Right Certificates, entitling the registered holder to purchase such number of Units as the Right Certificate or Right Certificates surrendered then entitled such holder to purchase. Any registered holder desiring to transfer, split up, combine or exchange any Right Certificate shall make such request in writing delivered to the Rights Agent, and shall surrender the Right Certificate(s) to be transferred, split up, combined or exchanged, with the form of assignment on the reverse side(s) thereof duly completed and executed, at the stock transfer office of the Rights Agent. Thereupon the Rights Agent shall countersign and deliver to the persons entitled thereto the Right Certificate(s) requested. The Company may require payment of a sum sufficient to cover any tax or governmental charge that may be imposed in connection with any transfer, split up, combination or exchange of Right Certificates. Notwithstanding the foregoing, neither the Rights Agent nor the Company shall be obligated to take any action whatsoever with respect to the transfer of any such surrendered Right Certificate unless and until the registered holder shall have completed and signed the certificate contained in the form of assignment on the reverse side of such Right Certificate and shall have provided such additional evidence of the identity of the Beneficial Owner (or former Beneficial Owner) or Affiliates or Associates thereof as the Company shall reasonably request.

(b) Upon receipt by the Company and the Rights Agent of evidence reasonably satisfactory to them of the loss, theft, destruction or mutilation of a Right Certificate, and, in case of loss, theft or destruction, of indemnity or security reasonably satisfactory to them, and reimbursement to the Company and the Rights Agent of all reasonable expenses incidental thereto, and upon surrender to the Rights Agent and cancellation of the Right Certificate, if mutilated, the Company will execute and deliver a new Right Certificate of like tenor to the Rights Agent for delivery to the registered owner in lieu of the Right Certificate so lost, stolen, destroyed or mutilated.

SECTION 7. EXERCISE OF RIGHTS; PURCHASE PRICE; EXPIRATION DATE
OF RIGHTS.

(a) Subject to Section 7(f), and unless earlier redeemed as provided in Section 23, the registered holder of any Right Certificate may exercise the Rights evidenced thereby in whole or in part at any time after the Distribution Date upon surrender of the Right Certificate, with the form of election to purchase on the reverse side thereof duly completed and executed, to the Rights Agent at the stock transfer office of the Rights Agent, together with payment of the Purchase Price for each Unit as to which the Rights are exercised, at or prior to the Close of Business on the tenth anniversary of the Rights Record Date or such other date to which the Rights may be extended as provided in this Agreement (the latest of such dates being herein referred to as the "Expiration Date"). If at any time after the Distribution Date but prior to the Expiration Date the Company is unable, under its Articles of Incorporation, to issue the number and class of shares required to be issued upon the exercise of all of the outstanding Rights, the Company may issue upon exercise of any of the Rights shares of capital stock or other securities of the Company of equivalent value to the shares so required to be issued ("Equivalent Stock"), as determined by the Board of Directors.

(b) The Purchase Price for each Unit pursuant to the exercise of a Right shall initially be \$120.00, shall be subject to adjustment from time to time as provided in Sections 11 and 13 and shall be payable in lawful money of the United States of America.

(c) Upon receipt of a Right Certificate, with the form of election to purchase duly executed, accompanied by payment of the Purchase Price for the Units to be purchased and an amount equal to any applicable transfer tax in cash, or by certified check, bank draft or money order payable to the order of the Company, the Rights Agent shall thereupon promptly (i) requisition from the Company or any transfer agent of the Company a certificate for the number of shares to be purchased and the Company will comply, and hereby irrevocably authorizes its transfer agent to comply, with all such requests, (ii) requisition from the Company the amount of cash to be paid in lieu of issuance of a fractional share, when appropriate, in accordance with Section 14, and (iii) promptly after receipt of such certificate from any such transfer agent, cause the same to be delivered to or upon the order of the registered holder of such Right Certificate, registered in such name or names as may be designated by such holder, and, when appropriate, after receipt promptly deliver such cash in lieu of a fractional share to or upon the order of the registered holder of such Right Certificate; provided, however, that in the case of the purchase, in connection with the exercise of a Right, of securities other than shares of stock, the Rights Agent shall promptly take the appropriate actions with respect thereto as shall as nearly as practicable correspond to the actions described in the foregoing clauses (i) through (iii).

(d) The Company shall not be required to pay any transfer tax which may be payable in respect of any transfer involved in the transfer or delivery of Right

Certificates, or the issuance or delivery of certificates in a name other than that of the registered holder of the Right Certificate evidencing Rights surrendered for exercise, or to issue or deliver any certificates upon the exercise of any Rights, until any such tax shall have been paid (any such tax being payable by the holder of such Right Certificate at the time of surrender) or until it has been established to the Company's satisfaction that no such tax is due.

(e) In case the registered holder of any Right Certificate shall exercise less than all the Rights evidenced thereby, a new Right Certificate evidencing Rights equivalent to the Rights remaining unexercised shall be issued by the Rights Agent to the registered holder of such Right Certificate or to his duly authorized assigns, subject to the provisions of Section 14.

(f) Notwithstanding any provision of this Agreement to the contrary, upon the occurrence of any of the events described in any of clauses (A), (B), (C) or (D) of Section 11(a)(ii), the adjustment provided for under Section 11(a)(ii) shall not apply with respect to any Rights that are at the time of the occurrence of such event Beneficially Owned by (i) an Acquiring Person or by any Associate or Affiliate of such Acquiring Person (which Acquiring Person or Affiliate or Associate engages in, or realizes the benefit of, one or more of the transactions described in clause (A) or clause (B) of Section 11(a)(ii), realizes the benefits set forth in clause (C) of Section 11(a)(ii) or, alone or together, become the Beneficial Owner(s) of a number of shares of Voting Stock which equals or exceeds the percentage of the general voting power as provided in clause (D) of Section 11(a)(ii), as the case may be), or (ii) a transferee of an Acquiring Person or of any Associate or Affiliate of such Acquiring Person (which Acquiring Person or Associate or Affiliate engages in, or realizes the benefit of, one or more of the transactions described in clause (A) or clause (B) of Section 11(a)(ii), realizes the benefits set forth in clause (C) of Section 11(a)(ii) or, alone or together with such Acquiring Person or any such Associate or Affiliate, become the Beneficial Owner(s) of a number of shares of Voting Stock which equals or exceeds the percentage of the general voting power as provided in clause (D) of Section 11(a)(ii), as the case may be) (A) who becomes a transferee after the Acquiring Person becomes such, or (B) who becomes a transferee prior to or concurrently with the Acquiring Person becoming such and receives such Rights pursuant to either (1) a transfer (whether or not for consideration) from the Acquiring Person to holders of equity interests in such Acquiring Person or to any Person with whom such Acquiring Person has any continuing agreement, arrangement or understanding regarding the transferred Rights or (2) a transfer which the Board of Directors of the Company has determined is part of a plan, arrangement or understanding which has as a primary purpose or effect the avoidance of this Section 7(f). Upon the exercise of such Rights, the holders thereof shall be entitled to receive, upon payment of the Purchase Price, the number of Units issuable upon exercise of such Rights without giving effect to the adjustment provided for under Section 11(a)(ii). The Company shall use all reasonable efforts to insure that the provisions of this Section 7(f) and Section 4(b) are complied with, but shall have no liability to any holder of Right Certificates or other Person as a

result of its making or failing to make any determinations with respect to an Acquiring Person or its Affiliates, Associates or transferees hereunder.

(g) Notwithstanding anything in this Agreement to the contrary, neither the Rights Agent nor the Company shall be obligated to undertake any action with respect to a registered holder upon the occurrence of any purported exercise as set forth in this Section 7 unless such registered holder shall have (i) completed and signed the certificate contained in the form of election to purchase set forth on the reverse side of the Right Certificate surrendered for such exercise, and (ii) provided such additional evidence of the identity of the Beneficial Owner (or former Beneficial Owner) or Affiliates or Associates thereof as the Company shall reasonably request.

SECTION 8. CANCELLATION AND DESTRUCTION OF RIGHT CERTIFICATES.

All Right Certificates surrendered for the purpose of exercise, transfer, split up, combination or exchange shall, if surrendered to the Company or to any of its agents, be delivered to the Rights Agent for cancellation or in cancelled form, or, if surrendered to the Rights Agent, shall be cancelled by it, and no Right Certificates shall be issued in lieu thereof except as expressly permitted by this Agreement. The Company shall deliver to the Rights Agent for cancellation and retirement, and the Rights Agent shall so cancel and retire, any other Right Certificate purchased or acquired by the Company otherwise than upon the exercise thereof. The Rights Agent shall deliver all cancelled Right Certificates to the Company, or shall, at the written request of the Company, destroy such cancelled Right Certificates, and in such case shall deliver a certificate of destruction thereof to the Company.

SECTION 9. RESERVATION AND AVAILABILITY OF SHARES; REGISTRATION.

(a) The Company covenants and agrees that it shall (i) on or prior to the Rights Record Date, take all such action as shall be necessary to cause to be reserved and kept available out of its authorized and unissued capital stock, the number, class and series of shares that will be sufficient to permit the exercise in full of all Rights to be outstanding as of the Rights Record Date, (ii) no later than promptly following the Distribution Date, take all such action as shall be necessary to cause to be reserved and kept available out of its authorized and unissued capital stock, the number of additional shares that will, from time to time, be sufficient to permit the exercise in full of all Rights from time to time outstanding, (iii) take all such action as may be necessary to insure that all shares delivered upon exercise of Rights shall, at the time of delivery of the certificates for such shares (subject to payment of the Purchase Price), be duly and validly authorized and issued and fully paid and nonassessable, and (iv) pay when due and payable any and all federal and state transfer taxes and charges which may be payable in respect of the issuance or delivery of the Right Certificates or of any shares upon the exercise of Rights (except as otherwise provided in Section 7(d)).

(b) The Company agrees to take all such action, from and after the Distribution Date, as may be necessary or appropriate to permit the issuance of shares in

connection with the exercise of the Rights, including any required registration under (i) the Securities Act of 1933, as amended from time to time (the "Securities Act"), and (ii) the securities or "blue sky" laws of the various states. The Company may temporarily suspend, for a period of time not to exceed 90 days, the exercisability of the Rights in order to prepare and file a registration statement or statements for the purpose of effecting any such registration and permit such statement(s) to become effective. At the commencement and termination of any such suspension, the Company shall issue a public announcement and shall provide written notice to the Rights Agent, stating that the exercisability of the Rights has been temporarily suspended, or that such suspension has terminated, as the case may be.

(c) If and so long as the stock issuable upon the exercise of Rights is listed on any national securities exchange, the Company shall use its reasonable efforts to cause all shares reserved for issuance upon exercise of Rights to be listed on such exchange upon official notice of issuance upon such exercise.

SECTION 10. RECORD DATE. Each Person in whose name any stock certificate is issued upon the exercise of Rights shall for all purposes be deemed to have become the holder of record of the shares represented thereby on, and such certificate shall be dated, the date upon which the Right Certificate evidencing such Rights was duly surrendered and payment of the Purchase Price (and any applicable transfer taxes) was made. Prior to the exercise of the Rights evidenced thereby, the holder of a Right Certificate shall not be entitled to any rights of a shareholder of the Company with respect to shares for which the Rights shall be exercisable, including without limitation the right to vote or to receive dividends or other distributions, and such holder shall not be entitled to receive any notice of any proceedings of the Company, except as provided herein.

SECTION 11. ADJUSTMENT OF PURCHASE PRICE, NUMBER OF SHARES OR NUMBER OF Rights. The Purchase Price, the number and kind of shares or other securities covered by each Right and the number of Rights outstanding are subject to adjustment from time to time as provided in this Section 11.

(a) (i) In the event the Company shall at any time after the date of this Agreement (A) declare and pay a dividend on the shares which are subject to the Rights ("Subject Shares") payable in shares of stock of the Company, (B) subdivide or split the Subject Shares, (C) combine or consolidate the Subject Shares into a smaller number of shares or effect a reverse stock split of the Subject Shares or (D) issue any shares of its capital stock in a reclassification of the Subject Shares (including any such reclassification in connection with a consolidation or merger in which the Company is the continuing or surviving corporation), then, and in each such event, except as otherwise provided in this Section 11(a), the number and kind of the Subject Shares or other securities issuable upon the exercise of a Right on such date shall be proportionately adjusted so that the holder of any Right exercised on or after such time shall be

entitled to receive upon the exercise thereof and payment of the Purchase Price, the aggregate number and kind of shares of capital stock or other property, as the case may be, that if such Right had been exercised immediately prior to such date and at a time when such Right was exercisable and the transfer books of the Company were open, such holder would have owned upon such exercise and would have been entitled to receive by virtue of such dividend, subdivision, split, reverse split, combination, consolidation or reclassification. If an event occurs that would require an adjustment under both this Section 11(a)(i) and Section 11(a)(ii) hereof, the adjustment provided for in this Section 11(a)(i) shall be in addition to, and shall be made prior to, any adjustment required pursuant to Section 11(a)(ii) hereof.

(ii) In the event that at any time after the date of this Agreement

(A) any Acquiring Person, or any Associate or Affiliate of any Acquiring Person, directly or indirectly (1) shall merge into the Company or any of its Subsidiaries or otherwise combine with the Company or any of its Subsidiaries and the Company or such Subsidiary shall be the continuing or surviving corporation of such merger or combination and the Common Stock shall remain outstanding and the outstanding shares thereof shall not be changed into or exchanged for stock or other securities of the Company or of any other Person or cash or any other property, or (2) shall sell or otherwise transfer in one or more transactions, assets to the Company or any of its Subsidiaries in exchange for 25 percent or more of the shares of any class of capital stock of the Company or any of its Subsidiaries, and the Common Stock shall remain outstanding and unchanged, or

(B) directly or indirectly, any Acquiring Person, or any Associate or Affiliate of any Acquiring Person, shall (1) in one or more transactions, transfer any assets to the Company or any of its Subsidiaries in exchange (in whole or in part) for shares of any class of capital stock of the Company or any of its Subsidiaries or for securities exercisable for or convertible into shares of any class of capital stock of the Company or any of its Subsidiaries or otherwise obtain from the Company or any of its Subsidiaries, with or without consideration, any additional shares of any class of capital stock of the Company or any of its Subsidiaries or other securities exercisable for or convertible into shares of any class of capital stock of the Company or any of its Subsidiaries (other than as part of a pro rata distribution by the Company or such Subsidiary to all holders of Common Stock), (2) sell, purchase, lease, exchange, mortgage, pledge, transfer or otherwise dispose (in one or more transactions), to, from or with, as the case may be, the Company or any of its Subsidiaries, assets on terms and conditions less favorable to the Company or such Subsidiary

than the Company or such Subsidiary would be able to obtain in arm's-length negotiation with an unaffiliated third party, (3) receive any compensation from the Company or any of the Company's Subsidiaries other than compensation for full-time employment as a regular employee, or fees for serving as director, at rates in accordance with the Company's (or its Subsidiaries') past practices, or (4) receive the benefit, directly or indirectly (except proportionately as a shareholder), of any loans, advances, guarantees, pledges or other financial assistance provided by the Company or any of its Subsidiaries, on terms and conditions less favorable to the Company or such Subsidiary than the Company or such Subsidiary would be able to obtain in arm's-length negotiation with an unaffiliated third party, or

(C) during any such time as there is an Acquiring Person, there shall be any reclassification of securities (including any reverse stock split), or recapitalization of the Company, or any merger or consolidation of the Company with any of its Subsidiaries or any other similar transaction or series of transactions involving the Company or any of its Subsidiaries (whether or not with or into or otherwise involving an Acquiring Person or any Affiliate or Associate of such Acquiring Person) which has the effect, directly or indirectly, of increasing by more than one percent the proportionate share of the outstanding shares of any class of equity securities, or of securities exercisable for or convertible into equity securities, of the Company or any of its Subsidiaries which is directly or indirectly owned by any Acquiring Person or any Associate or Affiliate of any Acquiring Person, or

(D) any Person shall become an Acquiring Person otherwise than pursuant to a Qualified Offer, then, and in each such case, but subject to the provisions of Section 27, proper provision shall be made so that each holder of a Right, except as provided below and in Section 7(f), shall, on and after the later of (I) the date of the occurrence of an event described in clause (A), (B), (C) or (D) of this Section 11(a)(ii), or (II) the date of the expiration of the period within which the Rights may be redeemed pursuant to Section 23 (as the same may have been amended as provided in Section 26), have the right to receive, upon exercise thereof at the then current Purchase Price, such number of shares of Common Stock as shall equal the result obtained by (x) multiplying the then current Purchase Price by the then number of Units for which a Right is then exercisable and dividing that product by (y) 50 percent of the current market price per share of Common Stock (determined in accordance with Section 11(d)) on the date of the occurrence of the relevant event listed above in clause (A), (B), (C) or (D) of this subparagraph (ii); provided, however, that if the transaction that would otherwise give rise to the foregoing adjustment is also subject to the provisions of Section 13, then

only the provisions of Section 13 shall apply and no adjustment shall be made pursuant to this Section 11(a)(ii). The Company shall not consummate any such merger, combination, transfer or transaction referred to in any of such clauses (A), (B) and (C) unless prior thereto there shall be sufficient authorized but unissued Common Stock to permit the exercise in full of the Rights in accordance with the foregoing sentence, unless the Board of Directors has determined to issue Equivalent Stock in accordance with Section 7(a); provided, however, that in no case may the Company consummate any such merger, combination, transfer or transaction if at the time of or immediately after such transaction there are any rights, warrants or other instruments or securities outstanding or agreements in effect which would substantially diminish or otherwise eliminate the benefits intended to be afforded by the Rights.

In the event that the Company issues Equivalent Stock upon the exercise of any Rights pursuant to the immediately preceding paragraph, then, upon any such exercise, proper provision shall be made so that the holder of a Right (except as provided in Section 7(f)) shall have the right to receive, upon such exercise at the then current Purchase Price, such number of shares or other units of Equivalent Stock of the Company as shall equal the result obtained by (x) multiplying the then current Purchase Price by the number of Units for which a Right is then exercisable and dividing that product by (y) 50 percent of the current market price per share or other unit of the Equivalent Stock of the Company (determined on substantially the same basis as is prescribed by Section 11(d) with respect to the valuation of Common Stock) on the date of occurrence of the relevant event listed above in clause (A), (B), (C) or (D) of this subparagraph (ii). In the event that at any time the Company should be prohibited by law, by any provision of its Articles of Incorporation, or by any instrument or agreement to which the Company is a party or by which it is bound, from issuing, or should be unable under its Articles of Incorporation to issue, sufficient Equivalent Stock to permit the exercise of all outstanding Rights in accordance with the foregoing sentence, then, in lieu of issuing such Equivalent Stock upon such exercise, the Company shall pay to each holder of a Right (except as provided in Section 7(f)) upon surrender of the Right as provided herein but without payment of the Purchase Price, an amount in cash for each Right equal to the Purchase Price.

(b) In case the Company shall at any time after the Rights Record Date fix a record date for the issuance of rights or warrants to all holders of Common Stock or Subject Shares entitling them for a period expiring within 45 calendar days after such record date to subscribe for or purchase Common Stock or Subject Shares or securities convertible into Common Stock or Subject Shares at a price per share (or having a conversion price per share, if a security convertible into Common Stock) less than the current market price per share (determined in accordance with Section 11(d)) on such record date, the Purchase Price to be in effect after such record date shall be determined by multiplying the Purchase Price in effect immediately prior to such record date by a fraction, of which the numerator shall be the total number of shares of Common Stock

and Subject Shares outstanding on such record date plus the number of shares of Common Stock which the aggregate offering price of the total number of shares so to be offered (and/or the aggregate initial conversion price of the convertible securities so to be offered) would purchase at such current market price and of which the denominator shall be the total number of shares of Common Stock and Subject Shares outstanding on such record date plus the number of additional shares to be offered for subscription or purchase (or into which the convertible securities to be offered are initially convertible). In case such subscription or purchase price may be paid, in whole or in part, in a form other than cash, the value of such consideration shall be as determined in good faith by the Board of Directors of the Company, whose determination shall be described in a statement filed with the Rights Agent. Shares owned by or held for the account of the Company shall not be deemed outstanding for the purpose of any such computation. Such adjustment shall be made successively whenever such a record date is fixed, and in the event that such rights or warrants are not so issued, the Purchase Price shall be adjusted to be the Purchase Price which would then be in effect if such record date had not been fixed.

(c) In case the Company shall at any time after the Rights Record Date fix a record date for the making of a distribution on the shares of Common Stock or the Subject Shares, whether by way of a dividend, distribution, reclassification of stock, recapitalization, reorganization or partial liquidation of the Company or otherwise (and including any such distribution made in connection with a consolidation or merger in which the Company is the continuing corporation), of subscription rights or warrants (excluding those referred to in Section 11(b)), evidences of indebtedness or other assets (other than (i) regular periodic cash dividends, (ii) a dividend payable in Common Stock or (iii) a distribution which is part of or is made in connection with a transaction to which Section 11(a)(ii) or Section 13 applies), the Purchase Price to be in effect after such record date shall be determined by multiplying the Purchase Price in effect immediately prior to such record date by a fraction, of which the numerator shall be the current market price per share of Common Stock (determined in accordance with Section 11(d)) on such record date, less the fair market value applicable to one share of Common Stock (as determined in good faith by the Board of Directors of the Company, whose determination shall be described in a statement filed with the Rights Agent) of such assets or evidences of indebtedness or of such subscription rights or warrants so to be distributed, and of which the denominator shall be such current market price per share of Common Stock. Such adjustments shall be made successively whenever such a record date is fixed; and in the event that such distribution is not so made, the Purchase Price shall again be adjusted to be the Purchase Price which would then be in effect if such record date had not been fixed.

(d) For the purpose of any computation hereunder, the "current market price" per share of Common Stock on any date shall be deemed to be the average of the daily closing prices per share of such Common Stock for the 30 consecutive Trading Days immediately prior to such date; provided, however, that in the event that the current market price per share of Common Stock is determined during a period following the announcement by the issuer of such Common Stock of a dividend or distribution on such

Common Stock payable in shares of such Common Stock or securities convertible into shares of Common Stock (other than the Rights), and prior to the expiration of 30 Trading Days after the ex-dividend date for such dividend or distribution, then, and in each such case, the current market price shall be appropriately adjusted to reflect the current market price per share of Common Stock in connection with ex-dividend trading. The closing price for each day shall be the last sale price, regular way, or, in case no such sale takes place on such day, the average of the closing bid and asked prices, regular way, in either case as reported in the principal consolidated transaction reporting system with respect to securities listed or admitted to trading on the New York Stock Exchange or, if the shares of Common Stock are not listed or admitted to trading on the New York Stock Exchange, as reported in the principal consolidated transaction reporting system with respect to securities listed on the principal national securities exchange on which the shares of Common Stock are listed or admitted to trading or, if the shares of Common Stock are not listed or admitted to trading on any national securities exchange, the average of the high bid and low asked prices in the over-the-counter market, as reported by the National Association of Securities Dealers, Inc., Automated Quotation System ("NASDAQ"). If on any such date the shares of Common Stock are not quoted by any such organization, the fair market value of such shares on such date as determined in good faith by the Board of Directors of the issuer of such Common Stock shall be used. Any such determination of current market price shall be described in a statement filed with the Rights Agent.

For the purpose of any computation hereunder, the "current market price" of a Unit shall be deemed to be equal to the current market price per share of Common Stock, and the "current market price" of a Subject Share shall be deemed to be equal to the current market price per share of Common Stock divided by the number of Subject Shares which comprise a Unit.

For purposes of this Agreement, the term "Trading Day" shall mean a day on which the principal national securities exchange on which the shares of Common Stock are listed or admitted to trading is open for the transaction of business or, if the shares of Common Stock are not listed or admitted to trading on any national securities exchange, a Business Day.

(e) No adjustment in the Purchase Price shall be required unless such adjustment would require an increase or decrease of at least one percent in such Price; provided, however, that any adjustments which by reason of this Section 11(e) are not required to be made shall be carried forward and taken into account in any subsequent adjustment. All calculations under this Section 11 shall be made to the nearest cent or to the nearest one-hundredth of a share, as the case may be. Notwithstanding the proviso to the first sentence of this Section 11(e), any adjustment required by this Section 11 shall be made no later than the earlier of (i) three years from the date of the transaction which gives rise to such adjustment or (ii) the date of the expiration of the right to exercise any Rights.

(f) In the event that at any time, as a result of an adjustment made pursuant to Section 11(a), the holder of any Right thereafter exercised shall become entitled to receive any shares of capital stock of the Company other than shares of Common Stock, thereafter the number of such other shares so receivable upon exercise of any Right shall be subject to adjustment from time to time in a manner and on terms as nearly equivalent as practicable to the provisions, with respect to such shares, contained in Sections 11(a) through (c), inclusive, and the provisions of Sections 7, 9, 10, 13 and 14 with respect to the shares of Common Stock shall apply on like terms to any such other shares.

(g) All Rights originally issued by the Company subsequent to any adjustment made to the Purchase Price hereunder shall represent the right to purchase, at the adjusted Purchase Price, the number of shares purchasable from time to time hereunder upon exercise of the Rights, all subject to further adjustment as provided herein.

(h) Unless the Company shall have exercised its election as provided in Section 11(i), upon each adjustment of the Purchase Price as a result of the calculations made in Sections 11(b) and (c), each Right outstanding immediately prior to the making of such adjustment shall thereafter evidence the right to purchase, at the adjusted Purchase Price, that number of shares (calculated to the nearest one-hundredth) obtained by (i) multiplying (x) the number of shares covered by a Right immediately prior to such adjustment by (B) the Purchase Price in effect immediately prior to such adjustment of the Purchase Price and (ii) dividing the product so obtained by the Purchase Price in effect immediately after such adjustment of the Purchase Price.

(i) The Company may elect on or after the date of any adjustment of the Purchase Price to adjust the number of Rights, in substitution for any adjustment in the number of shares purchasable upon the exercise of each Right. Each of the Rights outstanding after such adjustment of the number of Rights shall be exercisable for the number of Units for which a Right was exercisable immediately prior to such adjustment. Each Right held of record prior to such adjustment of the number of Rights shall become that number of Rights (calculated to the nearest one-hundredth) obtained by dividing the Purchase Price in effect immediately prior to adjustment of the Purchase Price by the Purchase Price in effect immediately after adjustment of the Purchase Price. The Company shall make a public announcement of its election to adjust the number of Rights, indicating the record date for the adjustment, and, if known at the time, the amount of the adjustment to be made. This record date may be the date on which the Purchase Price is adjusted or any day thereafter, but, if the Right Certificates have been issued, shall be at least 10 days later than the date of the public announcement. If Right Certificates have been issued, upon each adjustment of the number of Rights pursuant to this Section 11(i) the Company shall, as promptly as practicable, cause to be distributed to holders of record of Right Certificates on such record date Right Certificates evidencing, subject to Section 14, the additional Rights to which such holders shall be entitled as a result of such adjustment, or, at the option of the Company, shall cause to be distributed to such holders of record in substitution and replacement for the Right

Certificates held by such holders prior to the date of adjustment, and upon surrender thereof, if required by the Company, new Right Certificates evidencing all the Rights to which such holders shall be entitled after such adjustment. Right Certificates so to be distributed shall be issued, executed and countersigned in the manner provided for herein (and may bear, at the option of the Company, the adjusted Purchase Price) and shall be registered in the names of the holders of record of Right Certificates on the record date specified in the public announcement.

(j) Irrespective of any adjustment or change in the Purchase Price or the number of shares issuable upon the exercise of the Rights, the Right Certificates theretofore and thereafter issued may continue to express the Purchase Price per share and the number of shares which were expressed in the initial Right Certificates issued hereunder.

(k) In any case in which this Section 11 requires that an adjustment in the Purchase Price be made effective as of the record date for a specified event, the Company may elect to defer until the occurrence of such event the issuance to the holder of any Right exercised after such record date the additional shares or securities of the Company, if any, issuable as a consequence of such adjustment; provided, however, that the Company shall deliver to such holder a due bill or other appropriate instrument evidencing such holder's right to receive such additional shares or securities upon the occurrence of such event.

(l) Anything in this Section 11 to the contrary notwithstanding, the Company shall be entitled to make such adjustments in the number of shares which may be acquired upon exercise of the Rights, and such adjustments in the Purchase Price, in addition to those adjustments expressly required by the other subsections of this Section 11, as and to the extent that the Company, in its sole discretion, shall determine to be advisable, in order that, in the event of (i) any reclassification, consolidation or subdivision of the Common Stock, (ii) any reorganization or partial liquidation of the Company or similar transaction, (iii) any issuance wholly for cash of any Common Stock at less than the current market price, (iv) any issuance wholly for cash of Common Stock or securities which by their terms are convertible into or exchangeable for Common Stock, (v) any stock dividends or (vi) any issuance of rights, options or warrants, hereafter made by the Company to holders of its Common Stock as provided herein-above in this Section 11, (A) the holders of the Rights in any such event shall be treated equitably and in accordance with the purpose and intent of this Agreement, and (B) to the extent reasonably possible, such event shall not, in the opinion of counsel for the Company, result in the shareholders of the Company being subject to any United States federal income tax liability by reason thereof.

SECTION 12. CERTIFICATION OF ADJUSTED PURCHASE PRICE OR NUMBER OF SHARES. Whenever an adjustment is made as provided in Section 11 or 13, the Company shall (i) promptly prepare a certificate setting forth such adjustment, and a brief statement of the facts accounting for such adjustment, (ii) promptly file with the Rights Agent and

with each transfer agent for the Common Stock a copy of such certificate, and (iii) mail a brief summary thereof to each holder of a Right Certificate in accordance with Section 25. Notwithstanding the foregoing sentence, the failure of the Company to give such notice shall not affect the validity of, or the force or effect of, the requirement for such adjustment.

SECTION 13. CONSOLIDATION, MERGER OR SALE OR TRANSFER OF ASSETS OR EARNING POWER.

(a) In the event that, at any time after an Acquiring Person has become such,

(i) the Company shall consolidate with, or merge with and into, any other Person and the Company shall not be the continuing or surviving corporation of such consolidation or merger,

(ii) any other Person(s) shall consolidate or merge with and into the Company, the Company shall be the continuing or surviving corporation of such merger and, in connection with such consolidation or merger, all or part of the Common Stock shall be changed into or exchanged for stock or other securities of the Company or of any other Person or cash or any other property, or

(iii) the Company shall sell or otherwise transfer (or one or more of its Subsidiaries shall sell or otherwise transfer), in one or more transactions, assets or earning power aggregating more than 50 percent of the assets or earning power of the Company and its Subsidiaries (taken as a whole) to any other Person, (other than a pro rata distribution by the Company of assets (including securities) of the Company or any of its Subsidiaries to all holders of the Company's Common Stock),

then, on and after the later of (I) the date of the occurrence of an event described in clause (i), (ii) or (iii) of this Section 13(a), or (II) the date of the expiration of the period within which the Rights may be redeemed pursuant to Section 23 (as the same may have been amended as provided in Section 26):

(A) proper provision shall be made so that each holder of a Right shall thereafter have the right to receive, upon the exercise thereof at the then current Purchase Price, such number of shares of common stock of the Principal Party as shall be equal to the result obtained by (x) multiplying the then current Purchase Price by the number of Units for which a Right is then exercisable and dividing that product by (y) 50 percent of the current market price per share of the common stock of the Principal Party (determined in the same manner as the current market price of Common Stock is determined under Section 11(d)) on the date of consummation of such consolidation, merger, sale or transfer;

(B) the Principal Party shall thereafter be liable for, and shall assume, by virtue of such consolidation, merger, sale or transfer, all the obligations and duties of the Company pursuant to this Agreement, and proper provision shall be made for the foregoing, provided that the Principal Party shall, prior to the first occurrence of an event described in clause (i), (ii) or (iii) of this Section 13(a), have caused to be reserved out of its authorized and unissued shares of common stock, for issuance pursuant to this Agreement, the number of shares of common stock that will be sufficient to permit the exercise in full of the Rights after the occurrence of such event;

(C) the term "Company" wherever used in this Agreement shall thereafter be deemed to refer to such Principal Party; and

(D) the Principal Party shall, in addition to the reservation of shares of its common stock as provided in the proviso to clause (B) above, take such steps (including without limitation compliance with the Company's other obligations as set forth in Section 9) in connection with such consummation as may be necessary to assure that the provisions hereof shall thereafter be applicable, as nearly as reasonably may be, in relation to the shares of its Common Stock thereafter deliverable upon the exercise of the Rights; provided, however, that, upon the subsequent occurrence of any merger, consolidation, sale of all or substantially all assets, recapitalization, reclassification of shares, reorganization or other extraordinary transaction in respect of such Principal Party, each holder of a Right shall thereupon be entitled to receive, upon exercise of a Right and payment of the Purchase Price, such cash, shares, rights, warrants and other property which such holder would have been entitled to receive had such holder, at the time of such transaction, owned the shares of common stock of the Principal Party purchasable upon the exercise of a Right, and such Principal Party shall take such steps (including, but not limited to, reservation of shares of stock) as may be necessary to permit the subsequent exercise of the Rights in accordance with the terms hereof for such cash, shares, rights, warrants and other property.

(b) For purposes of this Agreement, "Principal Party" shall mean

(i) in the case of any transaction described in clause (i) or (ii) of Section 13(a), (A) the Person that is the issuer of the securities into which shares of Common Stock are converted in such merger or consolidation, or, if there is more than one such issuer, the issuer of the common stock of which has the greatest market value, or (B) if no securities are so issued, (x) the Person that is the other party to the merger or consolidation and that survives said merger or consolidation, or, if there is more than one such Person, the Person the common

stock of which has the greatest market value or (y) if the Person that is the other party to the merger or consolidation does not survive the merger or consolidation, the Person that does so survive (including the Company if it survives); and

(ii) in the case of any transaction described in clause (iii) of Section 13(a), the Person that is the party receiving the greatest portion of the assets or earning power transferred pursuant to such transaction or transactions, or, if each Person that is a party to such transaction or transactions receives the same portion of the assets or earning power so transferred or if the Person receiving the greatest portion of the assets or earning power cannot be determined, whichever of such Persons is the issuer of common stock having the greatest market value of shares outstanding;

provided, however, that in any such case, (1) if the common stock of such Person is not at such time and has not been continuously over the preceding 12-month period registered under Section 12 of the Exchange Act, and such Person is a direct or indirect Subsidiary of another corporation the common stock of which is and has been so registered, "Principal Party" shall refer to such other corporation; (2) if the common stock of such Person is not and has not been so registered and such Person is not a direct or indirect Subsidiary of another corporation the common stock of which is and has been so registered, "Principal Party" shall refer to the corporation which ultimately controls such Person; (3) in case such Person is a Subsidiary, directly or indirectly, of more than one corporation, the common stocks of all of which are and have been so registered, "Principal Party" shall refer to whichever of such corporations is the issuer of common stock having the greatest market value of shares held by the public; and (4) if the common stock of such Person is not and has not been so registered and such Person is owned, directly or indirectly, by a joint venture formed by two or more Persons that are not owned, directly or indirectly, by the same Person, the rules set forth in clauses (1), (2) and (3) above shall apply to each of the chains of ownership having an interest in such joint venture as if such Person were a "Subsidiary" of both or all of such joint venturers and the Principal Party in each such chain shall bear the obligations set forth in this Section 13 in the same ratio as its direct or indirect interests in such Person bear to the total of such interests.

(c) The Company shall not consummate any such consolidation, merger, sale or transfer unless prior thereto the Company and the Principal Party shall have executed and delivered to the Rights Agent a supplemental agreement making valid provision for the results described in clause (A) of Section 13(a) and confirming that the Principal Party will perform its obligations under this Section 13(a); provided, however, that in no case may the Company consummate any such consolidation, merger, sale or transfer if (i) at the time of or immediately after such transaction there are any rights, warrants or other instruments or securities outstanding or agreements in effect which would substantially diminish or otherwise eliminate the benefits intended to be afforded by the Rights or (ii) prior to, simultaneously with or immediately after such transaction, the shareholders of the Person which constitutes, or would constitute, the Principal Party

for purposes of this Section 13 shall have received a distribution of Rights previously owned by such Person or any of its Affiliates and Associates.

(d) The provisions of this Section 13 shall similarly apply to successive mergers or consolidations or sales or other transfers. This Section 13 shall not be applicable to a transaction described in Subparagraphs (i), (ii) or (iii) of Subsection (a) of this Section if (i) such transaction is consummated with a Person or Persons who acquired Common Stock pursuant to a Qualified Offer (or a wholly owned subsidiary of any such Person or Persons), (ii) the price per share of Common Stock offered in such transaction or distributable to shareholders upon conclusion of such transaction is not less than the price per share of Common Stock paid to all holders of Common Stock whose shares were purchased pursuant to such Qualified Offer and (iii) the form of consideration being offered to the remaining holders of Common Stock pursuant to such transaction or distributable to shareholders upon conclusion of such transaction is the same as the form of consideration paid pursuant to such Qualified Offer. Upon conclusion of any transaction described in the foregoing sentence, all Rights shall expire.

SECTION 14. FRACTIONAL RIGHTS AND FRACTIONAL SHARES.

(a) The Company shall not be required to issue fractions of Rights or to distribute Right Certificates which evidence fractional Rights. If the Company shall elect not to issue such fractional Rights, in lieu of such fractional Rights, there shall be paid to the registered holders of the Right Certificates with regard to which such Fractional Rights would otherwise be issuable an amount in cash equal to the same fraction of the current market value of a whole Right. For the purposes of this Section 14(a), the current market value of a whole Right shall be the closing price of the Rights for the Trading Day immediately prior to the date on which such fractional Rights would have been otherwise issuable. The closing price for any day shall be the last sale price, regular way, or, in case no such sale takes place on such day, the average of the closing bid and asked prices, regular way, in either case as reported in the principal consolidated transaction reporting system with respect to securities listed or admitted to trading on the New York Stock Exchange or, if the Rights are not listed or admitted to trading on the New York Stock Exchange, as reported in the principal consolidated transaction reporting system with respect to securities listed on the principal national securities exchange on which the Rights are listed or admitted to trading or, if the Rights are not listed or admitted to trading on any national securities exchange, the average of the high bid and low asked prices in the over-the-counter market, as reported by NASDAQ. If on any such date the Rights are not quoted by any such organization, the fair value of the Rights on such date as determined in good faith by the Board of Directors of the Company shall be used. Any such determination of current market value shall be described in a statement filed with the Rights Agent.

(b) The Company shall not be required to issue fractions of shares upon exercise of a Right or to distribute certificates which evidence fractional shares. In lieu of fractional shares, the Company shall pay to the registered holders of Right

Certificates at the time such Right Certificates are exercised as herein provided an amount in cash equal to the same fraction of the current market value of a share of Common Stock. For purposes of this Section 14, the current market value of a share of Common Stock shall be the closing price of a share of Common Stock (as determined pursuant to the second sentence of Section 11(d)) for the Trading Day immediately prior to the date of such exercise.

(c) The holder of a Right by the acceptance thereof expressly waives his right to receive any fractional Rights or any fractional shares upon exercise of a Right.

SECTION 15. RIGHTS OF ACTION. All rights of action in respect of this Agreement are vested in the respective registered holders of the Right Certificates (and prior to the Distribution Date, the registered holders of the Common Stock), and any registered holder of any Right Certificate (or, prior to the Distribution Date, any registered holder of the Common Stock), without the consent of the Rights Agent or of the holder of any other Right Certificate (or, prior to the Distribution Date, any other registered holder of the Common Stock), may, on his own behalf and for his own benefit, enforce, and may institute and maintain, any suit, action or proceeding against the Company to enforce, or otherwise act in respect of, his right to exercise the Rights evidenced by such Right Certificate in the manner provided in such Right Certificate and in this Agreement. Without limiting the foregoing or any remedies available to the holders of Rights, it is specifically acknowledged that the holders of Rights would not have an adequate remedy at law for any breach of this Agreement and will be entitled to specific performance of the obligations under, and injunctive relief against actual or threatened violations of the obligations of any Person subject to, this Agreement.

SECTION 16. AGREEMENT OF RIGHT HOLDERS. Every holder of a Right by accepting the same, consents and agrees with the Company and the Rights Agent and with every other holder of a Right that:

(a) prior to the Distribution Date, the Rights will be transferable only in connection with the transfer of Common Stock;

(b) on and after the Distribution Date, the Right Certificates will be transferable only on the registry books of the Rights Agent and then if surrendered at the stock transfer office of the Rights Agent, duly endorsed or accompanied by a proper instrument of transfer; and

(c) the Company and the Rights Agent may deem and treat the person in whose name the Right Certificate (or, prior to the Distribution Date, the associated Common Stock certificate) is registered as the absolute owner thereof and of the Rights evidenced thereby (notwithstanding any notations of ownership or writing on the Right Certificates or the associated Common Stock certificate made by anyone other than the Company or the Rights Agent) for all purposes whatsoever, and neither the Company nor the Rights Agent shall be affected by any notice to the contrary.

SECTION 17. RIGHT CERTIFICATE HOLDER NOT DEEMED A SHAREHOLDER. No holder, as such, of any Right Certificate shall be entitled to vote, receive dividends or be deemed for any purpose the holder of Common Stock or any other securities of the Company which may at any time be issuable on the exercise of the Rights represented thereby, nor shall anything contained herein or in any Right Certificate be construed to confer upon the holder of any Right Certificate, as such, any of the rights of a shareholder of the Company or any right to vote for the election of directors or upon any matter submitted to shareholders at any meeting thereof, or to give or withhold consent to any corporate action, or to receive notice of meetings or other actions affecting shareholders (except as provided in Section 24), or to receive dividends or subscription rights, or otherwise, until the Right or Rights evidenced by such Right Certificate shall have been exercised in accordance with the provisions hereof.

SECTION 18. CONCERNING THE RIGHTS AGENT.

(a) The Company agrees to pay to the Rights Agent reasonable compensation for all services rendered by it hereunder and, from time to time, on demand of the Rights Agent, its reasonable expenses and reasonable legal fees and other disbursements incurred in the administration and execution of this Agreement and the exercise and performance of its duties hereunder. The Company also agrees to indemnify the Rights Agent for, and to hold it harmless against, any loss, liability, or expense incurred, without negligence, bad faith or willful misconduct on the part of the Rights Agent, for anything done or omitted by the Rights Agent in connection with the acceptance and administration of this Agreement, including the costs and expenses of defending against any claim of liability in the premises. In no case will the Rights Agent be liable for special, indirect, incidental or consequential loss or damages of any kind whatsoever (including but not limited to lost profits) even if the Rights Agent has been advised of the possibility of damages.

(b) The Rights Agent shall be protected and shall incur no liability for or in respect of any action taken, suffered or omitted by it in connection with its administration of this Agreement in reliance upon any Right Certificate or Certificate for Common Stock or for other securities of the Company, instrument of assignment or transfer, power of attorney, endorsement, affidavit, letter, notice, direction, consent, certificate, statement, or other paper or document believed by it, acting with reasonable care, to be genuine and to be signed, executed and, where necessary, verified or acknowledged, by the proper person or persons.

If and for so long as the Rights are listed on the New York Stock Exchange or the American Stock Exchange, the Rights Agent, if its principal offices are located outside New York City, shall maintain in the New York City area facilities for the servicing of the Rights in the area of Manhattan located south of Chambers Street. Such facilities may consist of either an office or agency where transactions in the Rights are serviced directly or a "drop" where Common Stock certificates, Right Certificates, and other instruments relating to transactions in Rights may be received for redelivery to an

office or agency outside New York City, all in accordance with the applicable rules of the stock exchange on which the Rights are listed.

SECTION 19. MERGER OR CONSOLIDATION OR CHANGE OF NAME OF RIGHTS AGENT.

(a) Any corporation into which the Rights Agent or any successor Rights Agent may be merged or with which it may be consolidated, or any corporation resulting from any merger or consolidation to which the Rights Agent or any successor Rights Agent shall be a party, or any corporation succeeding to the stock transfer business of the Rights Agent or any successor Rights Agent, shall be the successor to the Rights Agent under this Agreement without the execution or filing of any paper or any further act on the part of any of the parties hereto, provided that such corporation would be eligible for appointment as a successor Rights Agent under the provisions of Section 21. In case at the time such successor Rights Agent shall succeed to the agency created by this Agreement any of the Right Certificates shall have been countersigned but not delivered, any such successor Rights Agent may adopt the countersignature of the predecessor Rights Agent and deliver such Right Certificates so countersigned, and in case at that time any of the Right Certificates shall not have been countersigned, any successor Rights Agent may countersign such Right Certificates either in the name of the predecessor Rights Agent or in the name of the successor Rights Agent and in all such cases such Right Certificates shall have the full force provided in the Right Certificates and in this Agreement.

(b) In case at any time the name of the Rights Agent shall be changed and at such time any of the Right Certificates shall have been countersigned but not delivered, the Rights Agent may adopt the countersignature under its prior name and deliver Right Certificates so countersigned, and in case at that time any of the Right Certificates shall not have been countersigned, the Rights Agent may countersign such Right Certificates either in its prior name or in its changed name, and in all such cases such Right Certificates shall have the full force provided in the Right Certificates and in this Agreement.

SECTION 20. DUTIES OF RIGHTS AGENT. The Rights Agent undertakes the duties and obligations imposed by this Agreement upon the following terms and conditions, by all of which the Company and the holders of Right Certificates, by their acceptance thereof, shall be bound:

(a) The Rights Agent may consult with legal counsel (who may be legal counsel for the Company), and the opinion of such counsel shall be full and complete authorization and protection to the Rights Agent as to any action taken or omitted by it in good faith and in accordance with such opinion.

(b) Whenever in the performance of its duties under this Agreement the Rights Agent shall deem it necessary or desirable that any fact or matter be proved or established by the Company prior to taking or suffering any action hereunder, such fact or

matter (unless other evidence in respect thereof be herein specifically prescribed) may be deemed to be conclusively proved and established by a certificate signed by the President, any Vice President, or the Secretary of the Company and delivered to the Rights Agent, and such certificate shall be full authorization to the Rights Agent for any action taken or suffered in good faith by it under the provisions of this Agreement in reliance upon such certificate.

(c) The Rights Agent shall be liable hereunder only for its own negligence, bad faith or willful misconduct.

(d) The Rights Agent shall not be liable for or by reason of any of the statements of fact or recitals contained in this Agreement or in the Right Certificates (except its countersignature thereof) or be required to verify the same, but all such statements and recitals are and shall be deemed to have been made by the Company only.

(e) The Rights Agent shall not be under any responsibility in respect of the validity of this Agreement or the execution and delivery hereof (except the due execution hereof by the Rights Agent) or in respect of the validity or execution of any Right Certificate (except its countersignature thereof), nor shall it be responsible for any breach by the Company of any covenant or condition contained in this Agreement or in any Right Certificate, nor shall it be responsible for any adjustment required under the provisions of Section 11 or 13 or responsible for the manner, method or amount of any such adjustment or the ascertaining of the existence of facts that would require any such adjustment (except with respect to the exercise of Rights evidenced by Right Certificates after actual notice of any such adjustment), nor shall it by any act hereunder be deemed to make any representation or warranty as to the authorization or reservation of any shares of stock to be issued pursuant to this Agreement or any Right Certificate or as to whether any shares of stock will, when issued, be validly authorized and issued, fully paid and nonassessable.

(f) The Company agrees that it will perform, execute, acknowledge and deliver or cause to be performed, executed, acknowledged and delivered all such further and other acts, instruments and assurances as may reasonably be required by the Rights Agent for the carrying out or performance by the Rights Agent of the provisions of this Agreement.

(g) The Rights Agent is hereby authorized and directed to accept instructions with respect to the performance of its duties hereunder from the President, any Vice President or the Secretary of the Company, and to apply to such officers for advice or instructions in connection with its duties, and it shall not be liable for any action taken or suffered to be taken by it in good faith in accordance with instructions of any such officer.

(h) The Rights Agent and any shareholder, director, officer or employee of the Rights Agent may buy, sell or deal in any of the Rights or other securities of the Company or become pecuniarily interested in any transaction in which

the Company may be interested, or contract with or lend money to the Company or otherwise act as fully and freely as though it were not Rights Agent under this Agreement. Nothing herein shall preclude the Rights Agent from acting in any other capacity for the Company or for any other legal entity.

(i) The Rights Agent may execute and exercise any of the rights or powers hereby vested in it or perform any duty hereunder either itself or by or through its attorneys or agents, and the Rights Agent shall not be answerable or accountable for any act, default, neglect or misconduct of any such attorneys or agents or for any loss to the Company resulting from any such act, default, neglect or misconduct, provided reasonable care was exercised in the selection and continued employment thereof.

(j) If, with respect to any Right Certificate surrendered to the Rights Agent for exercise or transfer, the certificate attached to the form of assignment or form of election to purchase, as the case may be, has either not been completed or indicates an affirmative response to clause 1 and/or 2 thereof, the Rights Agent shall not take any further action with respect to such requested exercise or transfer without first obtaining the Company's approval.

SECTION 21. CHANGE OF RIGHTS AGENT. Unless the Company and the Rights Agent agree to a shorter time period, the Rights Agent or any successor Rights Agent may resign and be discharged from its duties under this Agreement upon 15 days' notice in writing mailed to the Company and to each transfer agent of Common Stock by registered or certified mail, and to the holders of the Right Certificates by first-class mail. Unless the Company and the Rights Agent agree to a shorter time period, the Company may remove the Rights Agent or any successor Rights Agent upon 15 days' notice in writing, mailed to the Rights Agent or successor Rights Agent, as the case may be, and to each transfer agent of Common Stock by registered or certified mail, and to the holders of the Right Certificates by first-class mail. If the Rights Agent shall resign or be removed or shall otherwise become incapable of acting, the Company shall appoint a successor to the Rights Agent. If the Company shall fail to make such appointment within a period of 15 days after such removal or after it has been notified in writing of such resignation or incapacity by the resigning or incapacitated Rights Agent or by the holder of a Right Certificate (who shall, with such notice, submit his Right Certificate for inspection by the Company), then the registered holder of any Right Certificate may apply to any court of competent jurisdiction for the appointment of a new Rights Agent. Any successor Rights Agent, whether appointed by the Company or by such a court, shall be either (a) a corporation organized and doing business under the laws of the United States or of the State of California (or of any other state of the United States so long as such corporation is authorized to do business as a banking institution in the State of California) in good standing, having a stock transfer office in the State of California, which is authorized under such laws to exercise stock transfer powers and is subject to supervision or examination by federal or state authority and which has at the time of its appointment as Rights Agent a combined capital and surplus of at least \$100,000,000, or (b) an affiliate of such a corporation. After appointment, the successor Rights Agent shall be vested

with the same powers, rights, duties and responsibilities as if it had been originally named as Rights Agent without further act or deed, but the predecessor Rights Agent shall deliver and transfer to the successor Rights Agent any property at the time held by it hereunder, and execute and deliver any further assurance, conveyance, act or deed necessary for the purpose. Not later than the effective date of any such appointment, the Company shall file notice thereof in writing with the predecessor Rights Agent and each transfer agent of Common Stock and mail a notice thereof in writing to the registered holders of the Right Certificates. Failure to give any notice provided for in this Section 21, however, or any defect therein, shall not affect the legality or validity of the resignation or removal of the Rights Agent or the appointment of the successor Rights Agent, as the case may be.

SECTION 22. ISSUANCE OF NEW RIGHT CERTIFICATES. Notwithstanding any of the provisions of this Agreement or of the Rights to the contrary, the Company may, at its option, issue new Right Certificates evidencing Rights in such form as may be approved by its Board of Directors to reflect any adjustment or change in the Expiration Date, the Purchase Price per share or the number or kind or class of shares of stock or other securities or property purchasable under the Right Certificates made in accordance with the provisions of this Agreement.

SECTION 23. REDEMPTION.

(a) The Board of Directors of the Company may, at its option and as provided herein, and notwithstanding the provisions of Sections 11 and 13 of this Agreement, elect to redeem all but not less than all of the then outstanding Rights at a redemption price of \$.01 per Right, appropriately adjusted to reflect any stock split, stock dividend, reclassification or similar transaction occurring after the date hereof (such redemption price being herein referred to as the "Redemption Price") at any time up to the Close of Business on a Stock Acquisition Date.

(b) Immediately upon the action of the Board of Directors of the Company electing to redeem the Rights, the Company shall make a public announcement thereof, and from and after the date of such announcement, without any further action and without any further notice, the right to exercise the Rights will terminate and the only right thereafter of the holders of Rights shall be to receive the Redemption Price. As soon as practicable after the election of the Board of Directors to redeem the Rights, the Company shall give notice of such redemption to the holders of the then outstanding Rights by mailing such notice to all such holders at their last addresses as they appear upon the registry books of the Rights Agent. Any notice which is mailed in the manner herein provided shall be deemed given, whether or not the holder receives the notice. Each such notice of redemption will state the method by which the payment of the Redemption Price will be made.

SECTION 24. NOTICE OF PROPOSED ACTIONS. In case the Company, after the Rights become exercisable, shall propose (i) to pay any dividend payable in stock of any

class to the holders of its Common Stock or the Subject Shares or to make any other distribution to the holders of its Common Stock or Subject Shares (other than a regular periodic cash dividend), or (ii) to offer to the holders of its Common Stock or Subject Shares rights or warrants to subscribe for or to purchase any additional shares of Common Stock or shares of stock of any class or any other securities, rights or options, or (iii) to effect any reclassification of its Common Stock or Subject Shares (other than a reclassification involving only the subdivision of outstanding shares of Common Stock) or any recapitalization or reorganization of the Company, or (iv) to effect any consolidation or merger into or with, or to effect any sale or other transfer (or to permit one or more of its Subsidiaries to effect any sale or other transfer), in one or more transactions, of more than 50 percent of the assets or earning power of the Company and its Subsidiaries (taken as a whole) to, any other Person, or (v) to effect the liquidation, dissolution or winding up of the Company, then, in each such case, the Company shall give to each holder of a Right, in accordance with Section 25, a notice of such proposed action, which shall specify the record date for the purposes of such dividend, distribution of rights or warrants, or the date on which such reclassification, recapitalization, reorganization, consolidation, merger, sale, transfer, liquidation, dissolution or winding up is to take place and the date of participation therein by the holders of Common Stock and/or Subject Shares, if any such date is to be fixed, and such notice shall be so given in the case of any action covered by clause (i) or (ii) above at least twenty days prior to the record date for determining holders of the Common Stock and/or Subject Shares for purposes of such action, and in the case of any such other action, at least twenty days prior to the date of the taking of such proposed action or the date of participation therein by the holders of Common Stock and/or Subject Shares, whichever shall be the earlier. The failure to give notice required by this Section 24 or any defect thereon shall not affect the legality or validity of the action taken by the Company or the vote upon any such action.

SECTION 25. NOTICES. Notices or demands authorized by this Agreement to be given or made by the Rights Agent or by the holder of any Right Certificate to or on the Company shall be sufficiently given or made if sent by first-class mail, postage prepaid, addressed (until another address is filed in writing with the Rights Agent) as follows:

American States Water Company
630 East Foothill Boulevard
San Dimas, California 91773
Attention: McClellan Harris III

Subject to the provisions of Section 21, any notice or demand authorized by this Agreement to be given or made by the Company or by the holder of any Right Certificate to or on the Rights Agent shall be sufficiently given or made if sent by first-class mail, postage prepaid, addressed (until another address is filed in writing with the Company) as follows:

ChaseMellon Shareholder Services
400 South Hope Street, Fourth Floor
Los Angeles, California 90071
Attention: Ray Torres

Notices or demands authorized by this Agreement to be given or made by the Company or the Rights Agent to or on the holder of any Right Certificate shall be sufficiently given or made if sent by first-class mail, postage prepaid, addressed to such holder at the address of such holder as shown on the registry books of the Company.

SECTION 26. SUPPLEMENTS AND AMENDMENTS. Prior to the Distribution Date and subject to the penultimate sentence of this Section 26, the Company and the Rights Agent shall, if the Company so directs, supplement or amend any provision of this Agreement without the approval of any holders of certificates representing shares of Common Stock. From and after the Distribution Date and subject to the penultimate sentence of this Section 26, the Company and the Rights Agent shall, if the Company so directs, supplement or amend this Agreement without the approval of any holders of Right Certificates in order (i) to cure any ambiguity, (ii) to correct or supplement any provision contained herein which may be defective or inconsistent with any other provisions herein, (iii) to shorten or lengthen any time period hereunder, or (iv) to change or supplement the provisions hereof in any manner which the Company may deem necessary or desirable and which shall not adversely affect the interests of the holders of Right Certificates; provided, however, this Agreement may not be supplemented or amended to lengthen, pursuant to clause (iii) of this sentence, (A) a time period relating to when the Rights may be redeemed at such time as the Rights are not then redeemable, or (B) any other time period, unless such lengthening is for the purpose of protecting, enhancing or clarifying the rights of, and/or the benefits to, the holders of Rights. Upon the delivery of a certificate from an appropriate officer of the Company which states that the proposed supplement or amendment is in compliance with the terms of this Section 26, the Rights Agent shall execute such supplement or amendment. Notwithstanding anything contained in this Agreement to the contrary: (1) no supplement or amendment shall be made which changes the Redemption Price, the Purchase Price or the number of shares or Units for which a Right is exercisable; and (2) the duration of the Rights may not be shortened without the written consent of the registered holders thereof (other than by a redemption of the Rights pursuant to Section 23). Prior to the Distribution Date, the interests of the holders of Rights shall be deemed coincident with the interests of the holders of Common Stock.

SECTION 27. EXCHANGE.

(a) The Board of Directors of the Company may, at its option, at any time after any Person becomes an Acquiring Person, exchange all or part of the then outstanding and exercisable Rights (which shall not include Rights that have become subject to the provisions of Section 7(f) hereof) for Common Stock at an exchange ratio

of one share of Common Stock per Right, appropriately adjusted to reflect any stock split, stock dividend or similar transaction occurring after the date hereof (such exchange ratio being hereinafter referred to as the "Exchange Ratio").

(b) Immediately upon the action of the Board of Directors of the Company ordering the exchange of any Rights pursuant to subsection (a) of this Section and without any further action and without any notice, the right to exercise such Rights shall terminate and the only right thereafter of a holder of such Rights shall be to receive that number of shares of Common Stock equal to the number of such Rights held by such holder multiplied by the Exchange Ratio. The Company shall promptly give public notice of any such exchange; provided, however, that the failure to give, or any defect in, such notice shall not affect the validity of such exchange. The Company promptly shall mail a notice of any such exchange to all of the holders of such Rights at their last addresses as they appear upon the registry books of the Rights Agent. Any notice which is mailed in the manner herein provided shall be deemed given, whether or not the holder receives the notice. Each such notice of exchange will state the method by which the exchange of the Common Stock for Rights will be effected and, in the event of any partial exchange, the number of Rights which will be exchanged. Any partial exchange shall be effected pro rata based on the number of Rights (other than Rights which have become subject to the provisions of Section 7(f) hereof) held by each holder of Rights.

(c) In the event that there shall not be sufficient authorized Common Stock to permit an exchange of Rights as contemplated in accordance with this Section, the Company shall take all such action as may be necessary to authorize additional Common Stock or Equivalent Stock for issuance upon exchange of the Rights.

SECTION 28. SUCCESSORS. All the covenants and provisions of this Agreement by or for the benefit of the Company or the Rights Agent shall bind and inure to the benefit of their respective successors and assigns hereunder.

SECTION 29. DETERMINATION AND ACTIONS TAKEN BY THE BOARD OF DIRECTORS. For all purposes of this Agreement, any calculation of the number of shares of Common Stock (or other applicable securities hereunder) outstanding at any particular time, including for purposes of determining the particular percentage of such outstanding shares of Common Stock (or other securities) of which any Person is the Beneficial Owner, shall be made in accordance with the last sentence of Rule 13d-3(d)(1)(i) (as in effect on the date of this Agreement) of the General Rules and Regulations under the Exchange Act. The Board of Directors of the Company shall have the exclusive power and authority to administer this Agreement and to exercise all rights and powers specifically granted to such Board or to the Company, or as may be necessary or advisable in the administration of this Agreement, including without limitation the right and power to (i) interpret the provisions of this Agreement, and (ii) make all determinations deemed necessary or advisable for the administration of this Agreement (including a determination to redeem or not redeem the Rights or to amend the Agreement). All such actions, calculations, interpretations and determinations (including,

for purposes of clause (B) below, all omissions with respect to the foregoing) which are done or made by the Board in good faith, shall (A) be final, conclusive and binding on the Company, the Rights Agent, the holders of the Rights and all other parties, and (B) not subject the Board to any liability to the holders of the Rights.

SECTION 30. BENEFITS OF THIS AGREEMENT. Nothing in this Agreement shall be construed to give to any Person other than the Company, the Rights Agent and the registered holders of the Right Certificates (and, prior to the Distribution Date, the holders of Common Stock) any legal or equitable right, remedy or claim under this Agreement. This Agreement shall be for the sole and exclusive benefit of the Company, the Rights Agent and the registered holders of the Right Certificates (and, prior to the Distribution Date, the holders of Common Stock).

SECTION 31. GOVERNING LAW. This Agreement and each Right Certificate issued hereunder shall be deemed to be a contract made under the laws of the State of California and for all purposes shall be governed by and construed in accordance with the laws of such State applicable to contracts to be made and performed entirely within such State. The rights and obligations of the Rights Agent under this Agreement shall be governed by and construed in accordance with the laws in effect in such state.

SECTION 32. COUNTERPARTS. This Agreement may be executed in any number of counterparts and each of such counterparts shall for all purposes be deemed to be an original, and all such counterparts shall together constitute but one and the same instrument.

SECTION 33. SECTION HEADINGS. Descriptive headings of the several Sections of this Agreement are inserted for convenience only and shall not control or affect the meaning or construction of any of the provisions hereof.

SECTION 34. SEVERABILITY. If any term, provision, covenant or restriction of this Agreement is held by a court of competent jurisdiction or other authority to be invalid, illegal, or unenforceable, (i) such invalid, illegal or unenforceable term, provision, covenant or restriction shall nevertheless be valid, legal and enforceable to the extent, if any, provided by such court or authority, and (ii) the remainder of the terms, provisions, covenants and restrictions of this Agreement shall remain in full force and effect and shall in no way be affected, impaired or invalidated.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be duly executed as of the day and year first above written.

AMERICAN STATES WATER COMPANY:

By: _____
Name:
Title:

By: _____
Name:
Title:

THE RIGHTS AGENT:

By: _____
Name:
Title:

Exhibit A

[Form of Right Certificate]

Certificate No. R-

_____ Rights

NOT EXERCISABLE AFTER PUBLIC ANNOUNCEMENT OF REDEMPTION IS MADE. THE RIGHTS ARE SUBJECT TO REDEMPTION, AT THE OPTION OF THE COMPANY, AT \$.01 PER RIGHT ON THE TERMS SET FORTH IN THE AGREEMENT. IN THE EVENT THAT THE RIGHTS REPRESENTED BY THIS CERTIFICATE ARE ISSUED TO A PERSON WHO IS AN ACQUIRING PERSON OR AN ASSOCIATE OR AFFILIATE THEREOF (AS SUCH TERMS ARE DEFINED IN THE RIGHTS AGREEMENT) OR CERTAIN TRANSFEREES THEREOF, THIS RIGHT CERTIFICATE AND THE RIGHTS REPRESENTED HEREBY MAY BE SUBJECT TO CERTAIN LIMITATIONS IN THE CIRCUMSTANCES SPECIFIED IN SECTION 7 OF THE RIGHTS AGREEMENT.

RIGHT CERTIFICATE

This certifies that _____, or registered assigns, is the registered owner of the number of Rights set forth above, each of which entitles the owner thereof, subject to the terms, provisions and conditions of the Amended and Restated Rights Agreement, dated as of _____, 1999 (the "Rights Agreement"), between American States Water Company, (the "Company"), and ChaseMellon Shareholder Services, L.L.C. (the "Rights Agent"), to purchase from the Company, unless the Rights have been previously redeemed, at any time after the Distribution Date (as such term is defined in the Rights Agreement) and prior to the Expiration Date (as such term is defined in the Rights Agreement), or the date, if any, on which the Rights evidenced by this Certificate may be redeemed, at the stock transfer office of the Rights Agent, or its successors as Rights Agent, one one-thousandth of a fully paid and nonassessable share of Junior Participating Preferred Stock, at a purchase price of \$120 (the "Purchase Price"), upon presentation and surrender of this Right Certificate with the Form of Election to Purchase duly completed and executed. The number of Rights evidenced by this Right Certificate as set forth above (and the number of shares which may be purchased upon exercise thereof), and the Purchase Price set forth above, are the number and Purchase Price as of the date of the Rights Agreement based on the shares of

Common Stock (as such term is defined in the Rights Agreement) of the Company as constituted at such date.

Upon the occurrence of an event described in clause (A), (B), (C) or (D) of Section 11(a)(ii) of the Rights Agreement, the holder of any Rights that are, or were, beneficially owned by an Acquiring Person or an Associate or Affiliate thereof (as such terms are defined in the Rights Agreement) or certain transferees thereof which engaged in, or realized the benefit of, an event or transaction or transactions described in clause (A), (B), (C) or (D) of such Section 11(a)(ii), shall not be entitled to the benefit of the adjustment described in such Section 11(a)(ii).

As provided in the Rights Agreement, the Purchase Price and the number and class of shares which may be purchased upon the exercise of the Rights evidenced by this Right Certificate are subject to modification and adjustment upon the happening of certain events.

This Right Certificate is subject to all of the terms, provisions and conditions of the Rights Agreement, which terms, provisions and conditions are hereby incorporated herein by reference and made a part hereof and to which Rights Agreement reference is hereby made for a full description of the rights, limitations of rights, obligations, duties and immunities hereunder of the Rights Agent, the Company and the holders of the Right Certificates, which limitations of rights include the temporary suspension of the exercisability of such Rights under specific circumstances set forth in the Rights Agreement. Copies of the Rights Agreement are on file at the above-mentioned office of the Rights Agent and at the principal office of the Company.

This Right Certificate, with or without other Right Certificates, upon surrender at the stock transfer office of the Rights Agent set forth above, may be exchanged for another Right Certificate or Right Certificates of like tenor and date evidencing Rights entitling the holder to purchase such number of shares as the Rights evidenced by the Right Certificate or Right Certificates surrendered shall have entitled such holder to purchase. If this Right Certificate shall be exercised in part, the holder shall be entitled to receive upon surrender hereof another Right Certificate or Right Certificates for the number of whole Rights not exercised.

Subject to the provisions of the Rights Agreement, the Rights evidenced by this Certificate may be redeemed by the Company at its option at a redemption price of \$.01 per Right.

No fractional shares will be issued upon the exercise of any Rights evidenced hereby, but in lieu thereof a cash payment may be made, as provided in the Rights Agreement.

No holder of this Right Certificate shall be entitled to vote or receive dividends or be deemed for any purpose the holder of shares or of any other securities of the Company which may at any time be issuable on the exercise hereof, nor shall anything

contained in the Rights Agreement or herein be construed to confer upon the holder hereof, as such, any of the rights of a shareholder of the Company or any right to vote for the election of directors or upon any matter submitted to shareholders at any meeting thereof, or to give or withhold consent to any corporate action, or to receive notice of meetings or other actions affecting shareholders (except as provided in the Rights Agreement), or to receive dividends or subscription rights, or otherwise, until the Right or Rights evidenced by this Right Certificate shall have been exercised as provided in the Rights Agreement.

This Right Certificate shall not be valid or obligatory for any purpose until it shall have been countersigned by the Rights Agent.

WITNESS the facsimile signatures of the proper officers of the Company. Dated as of _____, _____.

By: _____
Title:

Secretary

Countersigned:

By: _____
Authorized Signature

[Form of Reverse Side of Right Certificate]

FORM OF ASSIGNMENT

(To be executed by the registered holder if such holder desires to transfer the Right Certificate.)

FOR VALUE RECEIVED _____ hereby sells, assigns and transfers unto _____ (Please print name and address of transferee) this Right Certificate, together with all right, title and interest therein, and does hereby irrevocably constitute and appoint _____ Attorney to transfer the within Right Certificate on the books of the within-named Corporation, with full power of substitution.

Dated: _____, _____
Signature

Signature Guaranteed:

CERTIFICATE

The undersigned hereby certifies (after due inquiry and to the best knowledge of the undersigned) by checking the appropriate boxes that:

(1) this Right Certificate [] is [] is not being sold, assigned and transferred by or on behalf of a Person who is or was an Acquiring Person or an Affiliate or Associate of an Acquiring Person (as such terms are defined in the Rights Agreement);

(2) the undersigned [] did [] did not acquire the Rights evidenced by this Right Certificate from any Person who is, was or subsequently became an Acquiring Person or an Affiliate or Associate of an Acquiring Person.

Date: _____, _____
Signature

Signature Guaranteed:

NOTICE

The signature to the foregoing Assignment and Certificate must correspond to the name as written upon the face of this Right Certificate in every particular, without alteration or enlargement or any change whatsoever.

FORM OF ELECTION TO PURCHASE
(To be executed if holder desires to
exercise the Right Certificate.)

To the Company and the Rights Agent:

The undersigned hereby irrevocably elects to exercise
_____ Rights represented by this Right Certificate and to purchase
the shares issuable upon the exercise of such Rights and requests that
certificates for such shares be issued in the name of:

Please insert social security or other identifying number _____

Please print name and address: _____

If such number of Rights shall not be all the Rights evidenced by this Right
Certificate, a new Right Certificate for the balance remaining of such Rights
shall be registered in the name of and delivered to:

Please insert social security or other identifying number: _____

Please print name and address: _____

Dated: _____, _____

Signature: _____
(Signature must conform in all respects
to name of holder as specified on the
face of this Right Certificate)

Signature Guaranteed:

CERTIFICATE

The undersigned hereby certifies (after due inquiry and to the
best knowledge of the undersigned) by checking the appropriate boxes that:

LOAN AGREEMENT

Between

CALIFORNIA POLLUTION CONTROL FINANCING AUTHORITY

And

SOUTHERN CALIFORNIA WATER COMPANY

Dated as of December 1, 1996

relating to

\$8,000,000
California Pollution Control Financing Authority
Water Distribution Facilities Revenue Bonds
(Southern California Water Company Project)
1996 Series A

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THIS LOAN AGREEMENT, dated as of December 1, 1996, by and between the CALIFORNIA POLLUTION CONTROL FINANCING AUTHORITY, a public instrumentality and political subdivision of the State of California (the "Authority"), and SOUTHERN CALIFORNIA WATER COMPANY, a corporation organized and existing under the laws of the State of California (the "Borrower"),

WITNESSETH

WHEREAS, the Authority is a public instrumentality and political subdivision of the State of California, organized and existing under the California Pollution Control Financing Authority Act, being Division 27 of the California Health and Safety Code, as amended and supplemented (the "Act"); and

WHEREAS, the Act authorizes the Authority to issue its revenue bonds for the purpose of paying all or any part of the costs of a "project" as defined in the Act; and

WHEREAS, the Borrower has requested that the Authority issue bonds to finance certain water distribution facilities located throughout the State of California, as more particularly described in Exhibit A hereto (the "Project"), which qualify as a "project" under the Act; and

WHEREAS, the Authority after due investigation and deliberation has adopted its resolution approving said request and authorizing the making of a loan to the Borrower for the payment of the Cost of the Project (as defined in the Indenture); and

WHEREAS, the Authority proposes to issue its California Pollution Control Financing Authority Water Distribution Facilities Revenue Bonds (Southern California Water Company Project) 1996 Series A (the "Bonds"), in the aggregate principal amount of \$8,000,000 upon the terms and conditions set forth herein; and

WHEREAS, the Authority will enter into an Indenture of Trust dated as of December 1, 1996 (the "Indenture"), with Chemical Trust Company of California, as trustee thereunder pursuant to which the Bonds will be issued;

WHEREAS, payment of the Bonds is secured by the Municipal Bond Insurance Policy specified in the Indenture;

NOW, THEREFORE, in consideration of the premises and the respective representations and covenants herein contained, the parties hereto agree as follows:

ARTICLE I

DEFINITIONS

SECTION 1.1. DEFINITION OF TERMS. Unless the context otherwise requires, the terms used in this Agreement shall have the meanings specified in Section 1.01 of the Indenture, as originally executed or as they may from time to time be supplemented or amended as provided therein.

SECTION 1.2. NUMBER AND GENDER. The singular form of any word used herein, including the terms defined in Section 1.01 of the Indenture, shall include the plural, and vice versa. The use herein of a word of any gender shall include all genders.

SECTION 1.3. ARTICLES, SECTIONS, ETC. Unless otherwise specified, references to Articles, Sections and other subdivisions of this Agreement are to the designated Articles, Sections and other subdivisions of this Agreement as originally executed. The words "hereof," "herein," "hereunder" and words of similar import refer to this Agreement as a whole. The headings or titles of the several articles and sections, and the table of contents appended to copies hereof, shall be solely for convenience of reference and shall not affect the meaning, construction or effect of the provisions hereof.

ARTICLE II

REPRESENTATIONS

SECTION 2.1. REPRESENTATIONS OF THE AUTHORITY. The Authority makes the following representations as the basis for its undertakings herein contained:

(a) The Authority is a public instrumentality and political subdivision of the State. Under the provisions of the Act, the Authority has the power to enter into the transactions contemplated by this Agreement and to carry out its obligations hereunder. By proper action, the Authority has been duly authorized to execute, deliver and duly perform this Agreement.

(b) To pay the Cost of the Project, the Authority will issue the Bonds, which will mature, bear interest and be subject to redemption as provided in the Indenture.

(c) The Bonds will be issued under and secured by the Indenture, pursuant to which the Authority's interest in this Agreement (except certain rights of the Authority to payment for expenses and indemnification) will be pledged to the Trustee as security for payment of the principal of, premium, if any, and interest on the Bonds.

(d) The Authority has not pledged and will not pledge its interest in this Agreement for any purpose other than to secure the Bonds under the Indenture.

(e) The Authority is not in default under any of the provisions of the laws of the State of California which default would affect its existence or its powers referred to in subsection (a) of this Section 2.1.

(f) The Authority has found and determined and hereby finds and determines that all requirements of the Act with respect to the issuance of the Bonds and the execution of this Agreement have been complied with and that paying the Cost of the Project by issuing the Bonds and entering into this Agreement will be in furtherance of the purposes of the Act.

(g) On October 30, 1995, the Authority adopted its resolution approving the issuance of the Bonds, and a public hearing with respect to the Bonds and the Project was held in accordance with the provisions of the Code. The meetings of the Authority on such date were held in accordance with the applicable provisions of Article 9 of Chapter 1 of Division 3 of Title 2 of the California Government Code, as amended.

(h) The Authority has taken proper action to allocate to the Bonds a share of the State of California ceiling on private activity bonds for the 1995 calendar which is available to the Authority pursuant to Section 146 of the Code, in an amount at least equal to the \$8,000,000 aggregate principal amount of the Bonds. Issuance of the Bonds will not violate any provisions of Section 146 of the Code.

(i) No member, officer or other official of the Authority has any interest whatsoever in the Borrower or in the transactions contemplated by this Agreement.

SECTION 2.2. REPRESENTATIONS OF THE BORROWER. The Borrower makes the following representations as the basis for its undertakings herein contained:

(a) The Borrower is a corporation duly formed under the laws of the State, is in good standing in said State and has the corporate power to enter into and has duly authorized, by proper corporate action, the execution and delivery of this Agreement, the contract of purchase executed by it in connection with the sale of the Bonds (the "Contract of Purchase"), and all other documents contemplated hereby to be executed by the Borrower.

(b) This Agreement and the Contract of Purchase have been duly authorized, executed and delivered by the Borrower and constitute legal, valid and binding obligations of the Borrower, enforceable in accordance with its terms, except as limited by bankruptcy, insolvency, reorganization, moratorium or other similar laws or judicial decisions affecting the rights of creditors generally and by judicial discretion in the exercise of equitable remedies.

(c) Neither the execution and delivery of this Agreement and the Contract of Purchase, the consummation of the transactions contemplated hereby and thereby, nor the fulfillment of or compliance with the terms and conditions hereof and thereof, conflict with or result in a breach of any of the terms, conditions or provisions of the Borrower's articles of incorporation or bylaws or of any corporate actions or of any agreement or instrument to which the Borrower is now a party or by which it is bound, or constitute a default (with due notice or the passage of time or both) under any of the foregoing, or result in the creation or imposition of any prohibited lien, charge or encumbrance

whatsoever upon any of the property or assets of the Borrower under the terms of any instrument or agreement to which the Borrower is now a party or by which it is bound.

(d) The Borrower has not been served with and, to the knowledge of the Borrower there is no action, suit, proceeding, inquiry or investigation by or before any court, governmental agency or public board or body pending or threatened against the Borrower which (i) affects or seeks to prohibit, restrain or enjoin the issuance, sale or delivery of the Bonds or the loaning of the proceeds of the Bonds to the Borrower or the execution and delivery of this Agreement and the Contract of Purchase or the Indenture, (ii) affects or questions the validity or enforceability of the this Agreement and the Contract of Purchase, the Bonds or the Indenture, (iii) questions the exclusion of interest on the Bonds from gross income for federal income tax purposes, (iv) questions the power or authority of the Borrower to carry out the transactions contemplated by, or to perform its obligations under, this Agreement, the Contract of Purchase, the Bonds or the Indenture, or the powers of the Borrower to own, acquire, equip or operate the Project, or (v) which, if adversely determined, would materially impair its right to carry on business substantially as now conducted or as now contemplated to be conducted, or would materially adversely affect its financial condition.

(e) The Borrower is not in default under any document, instrument or commitment to which the Borrower is a party or to which it or any of its property is subject which default would or could affect the ability of the Borrower to carry out its obligations under this Agreement and the Contract of Purchase.

(f) Any certificate signed by the Borrower or an Authorized Borrower Representative and delivered pursuant to this Agreement or the Contract of Purchase or the Indenture shall be deemed a representation and warranty by the Borrower to the Authority and the Trustee as to the statements made therein.

(g) The estimated Cost of the Project is as set forth in Exhibit A hereto and has been determined in accordance with sound engineering principles and generally accepted accounting principles.

(h) The Project consists of those facilities described in Exhibit A hereto and the Borrower shall make no changes to the Project or to the operation thereof which would adversely affect the qualification of the Project under the Act or impair the Tax-exempt status of the Bonds. In particular, the Borrower has complied and shall comply with all requirements set forth in the Tax Certificate which is hereby incorporated by reference herein. The Borrower intends to utilize the Project as water distribution facilities until the principal of, the premium, if any, and the interest on the Bonds shall have been paid.

(i) The Project consists of water mains and related water distribution facilities as described in the Tax Certificate.

(j) The economic useful life of the Project is as set forth in the Tax Certificate.

(k) To the best knowledge of the Borrower, no member, officer or other official of the Authority has any interest whatsoever in the Borrower or in the transactions contemplated by this Agreement.

(l) The Borrower has and will have title to the Project sufficient to carry out the purposes of this Agreement.

(m) At the time of submission of an application to the Authority for financial assistance in connection with the Project and on the date on which the Authority took action on such application, permanent financing for the Project had not otherwise been obtained or arranged.

(n) All certificates, approvals, permits and authorizations with respect to the construction of the Project of agencies of applicable local governments, the State of California and the federal government, which are required to be obtained as of the date of this Agreement, have been obtained, and the Borrower has no reason to believe that any other such certificates, approvals, permits or authorizations with respect to the construction of the Project will not be obtained in due course.

(o) No event has occurred and no condition exists which would constitute an Event of Default or which, with the passing of time or with the giving of notice or both, would become such an Event of Default.

ARTICLE III

CONSTRUCTION OF THE PROJECT; ISSUANCE OF THE BONDS

SECTION 3.1. AGREEMENT TO CONSTRUCT THE PROJECT. The Borrower agrees that it will acquire, construct and install, or complete or cause the completion of the acquisition, construction and installation of the Project, and will acquire, construct and install or cause the acquisition, construction and installation of all other facilities and real and personal property deemed necessary for the operation of the Project, substantially in accordance with the plans and specifications prepared therefor by the Borrower and approved by the Authority, including any and all supplements, amendments and additions or deletions thereto or therefrom, it being understood that the approval of the Authority shall not be required for changes in such plans and specifications which do not materially alter the purpose and description of the Project as set forth in Exhibit A hereto.

In the event that the Borrower desires to amend or supplement the Project, and such amendment or supplement materially alters the purpose and description of the Project as described in Exhibit A hereto, and the Authority approves of such amendment or supplement, which approval will not be unreasonably withheld, the Authority will enter into, and will instruct the Trustee to consent to, such amendment or supplement upon receipt of:

(i) a certificate of the Authorized Borrower Representative describing in detail the proposed changes and stating that they will not have the effect of disqualifying the Project as a facility that may be financed pursuant to the Act;

(ii) a copy of the proposed form of amended or supplemented Exhibit A hereto; and

(iii) an opinion of Bond Counsel that such proposed changes will not affect the Tax-exempt status of interest on the Bonds.

SECTION 3.2. AGREEMENT TO ISSUE BONDS; APPLICATION OF BOND PROCEEDS. To provide funds to finance the Cost of the Project, the Authority agrees that it will issue under the Indenture, sell and cause to be delivered to the purchasers thereof, the Bonds, bearing interest and maturing as provided in the Indenture, subject to the Borrower's final approval of the interest rates. The Authority will thereupon deposit the proceeds received from the sale of the Bonds as provided in the Indenture.

SECTION 3.3. DISBURSEMENTS FROM THE CONSTRUCTION FUND. (a) The Borrower will authorize and direct the Trustee, upon compliance with Section 3.03 of the Indenture, to disburse the moneys in the Construction Fund to or on behalf of the Borrower only for the following purposes, subject to the provisions of Section 3.5 hereof.

(i) Payment to the Borrower of such amounts, if any, as shall be necessary to reimburse the Borrower in full for all advances and payments made by it, at any time prior to or after the delivery of the Bonds, in connection with (A) the preparation of plans and specifications for the Project (including any preliminary study or planning of the Project or any aspect thereof) and ~) subject to any limitation imposed by subsection ~) hereof, the acquisition, construction and installation of the Project.

(ii) Payment for labor, services, materials and supplies used by or furnished to the Borrower to improve the site and to acquire and construct the Project, as provided in the plans, specifications and work orders therefor; payment of the costs of acquiring, constructing and installing utility services or other related facilities; payment of the costs of acquiring all real and personal property deemed necessary to construct the Project; and payment of the miscellaneous expenses incidental to any of the foregoing items.

(iii) Payment of the fees, if any, of architects, engineers, legal counsel and supervisors expended in connection with the acquisition and construction of the Project.

(iv) Payment of taxes, including property taxes, assessments and other charges, if any, payable during the period of construction with respect to the Project, or reimbursement thereof, if paid by the Borrower.

(v) Payment of expenses incurred in seeking to enforce any remedy against any contractor or subcontractor in respect of any default under a contract relating to the acquisition, construction or installation of the Project.

(vi) Interest paid during the Construction Period and properly allocable to the Project, to the extent of the portion of the Project which has not been completed as of the date of accrual of any such interest costs and other interest paid in respect of the Bonds.

(vii) Payment of any other Cost of the Project permitted by the Tax Certificate but not including any Costs of Issuance).

(b) All moneys remaining in the Construction Fund after the Completion Date and after payment or provision for payment of all other items provided for in the preceding subsection (a) of this Section, shall be used in accordance with Section 3.03 of the Indenture.

Each of the payments referred to in this Section 3.3 shall be made upon receipt by the Trustee of a written requisition in the form prescribed by Section 3.03 of the Indenture, signed by the Authorized Borrower Representative.

SECTION 3.4. ESTABLISHMENT OF COMPLETION DATE; OBLIGATION OF BORROWER TO COMPLETE. As soon as the Project is completed, the Authorized Borrower Representative, on behalf of the Borrower, shall evidence the Completion Date by providing a certificate to the Trustee and the Authority stating the Cost of the Project and further stating that (i) construction of the Project has been completed substantially in accordance with the plans, specifications and work orders therefor, as such may be amended or supplemented from time to time as provided for herein, and all labor, services, materials and supplies used in construction have been paid for, and (ii) all other facilities necessary in connection with the Project have been acquired, constructed and installed in accordance with the plans and specifications and work orders therefor and all costs and expenses incurred in connection therewith have been paid. Notwithstanding the foregoing, such certificate may state that it is given without prejudice to any rights of the Borrower against third parties for the payment of any amount not then due and payable which exist at the date of such certificate or which may subsequently exist.

At the time such certificate is delivered to the Trustee, moneys remaining in the Construction Fund (other than moneys relating to provisional payments permitted by Section 3.3), including any earnings resulting from the investment of such moneys, shall be used as provided in Section 3.03 of the Indenture.

In the event the moneys in the Construction Fund available for payment of the Cost of the Project should be insufficient to pay the costs thereof in full, the Borrower agrees to pay directly, or to deposit in the Construction Fund moneys sufficient to pay, any costs of completing the Project in excess of the moneys available for such purpose in the Construction Fund. The Authority makes no express or implied warranty that the moneys deposited in the Construction Fund and available for payment of the Cost of the Project, under the provisions of this Agreement, will be sufficient to pay all the amounts which may be incurred for the Project. The Borrower agrees that if, after exhaustion of the moneys in the Construction Fund, the Borrower should pay, or deposit moneys in the Construction Fund for the payment of, any portion of the Cost of the Project pursuant to the provisions of this Section, it shall not be entitled to any reimbursement therefor from the Authority, from the Trustee or from the holders of any of the Bonds, nor shall it be entitled to any diminution of the amounts payable under Section 4.2 hereof.

SECTION 3.5. INVESTMENT OF MONEYS IN FUNDS. Any moneys in any fund held by the Trustee shall, at the written request of the Authorized Borrower Representative, be invested or

reinvested by the Trustee as provided in the Indenture. Such investments shall be held by the Trustee and shall be deemed at all times a part of the fund from which such investments were made, and the interest accruing thereon, and any profit or loss realized therefrom, except as otherwise provided in the Indenture shall be credited or charged to such fund.

SECTION 3.6. SPECIAL TAX CERTIFICATIONS. The Borrower confirms the representations set forth in, and covenants that it will comply with the requirements and conditions of, the Tax Certificate, incorporated in its entirety herein by reference. The Borrower covenants and agrees that it will not use or permit the use by any person of any of the funds provided by the Authority hereunder or any other of its funds, directly or indirectly, or direct the Trustee to invest any funds held by it under the Indenture or this Agreement, in such manner as would, or enter into, or allow any "related person" (as defined in Section 144(a)(3) of the Code) to enter into, any arrangement, formal or informal, that would, cause any Bond to be an "arbitrage bond" within the meaning of Section 148(a) of said Code. The Borrower acknowledges having read Sections 5.07 and 6.06 of the Indenture and agrees to perform all duties imposed upon it by such Sections 5.07 and 6.06 of the Indenture and by the Tax Certificate. Insofar as said Sections 5.07 and 6.06 of the Indenture and the Tax Certificate impose duties and responsibilities on the Borrower, they are specifically incorporated herein by reference, except to the extent that they may be amended or modified upon the Opinion of Bond Counsel that any such amendment or modification will not adversely affect the Tax-exempt status of the Bonds.

ARTICLE IV

LOAN OF PROCEEDS; REPAYMENT PROVISIONS

SECTION 4.1. LOAN OF BOND PROCEEDS. The Authority covenants and agrees, upon the terms and conditions in this Agreement, to make a loan to the Borrower for the purpose of financing the Cost of the Project. Pursuant to said covenant and agreement, the Authority will issue the Bonds upon the terms and conditions contained in this Agreement and the Indenture and will cause the Bond proceeds to be applied as provided in Article III of the Indenture. Such proceeds shall be disbursed in accordance with the Indenture and Section 3.3 hereof.

SECTION 4.2. REPAYMENT AND PAYMENT OF OTHER AMOUNTS PAYABLE. To secure and provide for the repayment of the loan made hereunder, the Borrower hereby agrees to make the payments required by this Section as Repayment Installments on such loan.

(a) The Borrower covenants and agrees to pay to the Trustee as a Repayment Installment on the loan to the Borrower from Bond proceeds pursuant to Section 4.1 hereof, on each date provided in or pursuant to the Indenture for the payment of principal (whether at maturity or upon redemption or acceleration) of, premium, if any, and/or interest on the Bonds, until the principal of, premium, if any, and interest on the Bonds shall have been fully paid or provision for the payment thereof shall have been made in accordance with the Indenture, in immediately available funds, for deposit in the Bond Fund, a sum equal to the amount payable on such interest or principal payment or redemption or acceleration date as principal of (whether at maturity or upon redemption or acceleration), premium, if any, and interest on the Bonds as provided in the Indenture.

Each payment made pursuant to this Section 4.2(a) shall at all times be sufficient to pay the total amount of interest and principal (whether at maturity or upon redemption or acceleration) and premium, if any, payable on the Bonds on the date of payment of principal or interest, as the case may be; provided that any amount held by the Trustee in the Bond Fund on any due date for a Repayment Installment hereunder shall be credited against the installment due on such date to the extent available for such purpose; and provided further that, subject to the provisions of this paragraph, if at any time the Borrower determines that amounts held by the Trustee in the Bond Fund are sufficient to pay all of the principal of and interest and premium, if any, on the Bonds as such payments become due, the Borrower shall be relieved of any obligation to make any further payments under the provisions of this Section. Notwithstanding the foregoing, if on any date the amount held by the Trustee in the Bond Fund is insufficient to make any required payments of principal of (whether at maturity or upon redemption or acceleration) and interest and premium, if any, on the Bonds as such payments become due, the Borrower shall forthwith pay such deficiency as a Repayment Installment hereunder.

In addition, the Borrower agrees to provide for the issuance of, and cause to be delivered to the Trustee on the Issue Date, the Bond Insurance Policy to secure the payment of principal of and interest on the Bonds as set forth in the Indenture. If at any time after the Bonds are issued, the Borrower does not intend or will be unable to make a Repayment Installment due hereunder, it shall notify the Bond Insurer of its failure or inability to make such payment not less than two (2) days prior to the date on which such payment is due.

(b) The Borrower also agrees to pay to the Trustee until the principal of, premium, if any, and interest on the Bonds shall have been fully paid or provision for the payment thereof shall have been made as required by the Indenture, in accordance with the letter proposal of the Trustee presented and agreed to by the Borrower prior to the issuance of the Bonds, (i) the annual fee of the Trustee for its ordinary services rendered as trustee, and its ordinary expenses incurred under the Indenture, as and when the same become due, (ii) the reasonable fees, charges and expenses of the Trustee, as registrar, as provided in the Indenture, as and when the same become due, (iii) the reasonable fees, charges and expenses of the Trustee, as paying agent, for the necessary extraordinary services rendered by it and extraordinary expenses incurred by it under the Indenture, as and when the same become due, (iv) the cost of printing any Bonds required to be furnished by the Authority, expenses of collection, just and reasonable compensation to the Trustee for its services and the services of counsel, agents and employees by it properly engaged and employed, and all other expenses and liabilities reasonably incurred in connection with the Bonds and the Project, and (v) any amounts required to be deposited in the Rebate Fund to comply with the provisions of Section 3.6 hereof and Sections 5.07 and 6.06 of the Indenture. The Trustee shall submit written invoices to the Borrower regarding all of the foregoing fees and expenses of the Trustee.

(c) The Borrower also agrees to pay, (i) at the time of Bond closing, all expenses required to be paid by the Borrower under the terms of the Contract of Purchase, including the premium and all costs related to the Bond Insurance Policy, and the Authority's administrative fee in the amount of one-half of one percent of the original principal amount of the Bonds (less any amounts previously paid by the Borrower to the Authority); (ii) on or after the date of Bond closing, on the request of the Authority, the Authority's Small Business Assistance Fund fee pursuant to Section 44548(a) of the

California Health and Safety Code, in the amount calculated by the Authority; and (-) all reasonable expenses of the Authority related to the Project which are not otherwise required to be paid by the Borrower under the terms of this Agreement; provided that the Authority shall have obtained the prior written approval of the Authorized Borrower Representative for any expenditures other than those provided for herein or in the Contract of Purchase.

(d) In the event the Borrower should fail to make any of the payments required by subsections (a) through (c) of this Section, such payments shall continue as obligations of the Borrower until such amounts shall have been fully paid. The Borrower agrees to pay overdue payments under subsection (a) above, together with interest thereon until paid, to the extent permitted by law, at the rate of interest per annum borne by the Bonds or, if less, at the maximum rate permitted by law. Interest on overdue payments required under subsection (a) above shall be paid to Bondholders as provided in the Indenture.

SECTION 4.3. UNCONDITIONAL OBLIGATION. The obligations of the Borrower to make the payments required by Section 4.2 hereof and to perform and observe the other agreements on its part contained herein shall be absolute and unconditional, irrespective of any defense or any rights of set-off, recoupment or counterclaim it might otherwise have against the Authority, and during the term of this Agreement, the Borrower shall pay absolutely net the payments to be made on account of the loan as prescribed in Section 4.2 and all other payments required hereunder, free of any deductions and without abatement, diminution or set-off. Until such time as the principal of, premium, if any, and interest on the Bonds shall have been fully paid, or provision for the payment thereof shall have been made as required by the Indenture, the Borrower (i) will not suspend or discontinue any payments provided for in Section 4.2 hereof; (ii) will perform and observe all of its other covenants contained in this Agreement; and (iii) except as provided in Article VII hereof, will not terminate this Agreement for any cause, including, without limitation, failure to complete the Project, the occurrence of any act or circumstances that may constitute failure of consideration, destruction of or damage to the Project, commercial frustration of purpose, any change in the tax or other laws of the United States of America or of the State of California or any political subdivision or either of these, or any failure of the Authority or the Trustee to perform and observe any covenant, whether express or implied, or any duty, liability or obligation arising out of or connected with this Agreement or the Indenture, except to the extent permitted by this Agreement.

SECTION 4.4. ASSIGNMENT OF AUTHORITY'S RIGHTS. As security for the payment of the Bonds, the Authority will assign to the Trustee the Authority's rights under this Agreement, including the right to receive payments hereunder (except the right of the Authority to receive certain payments, if any, with respect to expenses and indemnification under Sections 4.2- and (c), 6.3, 8.2 and 8.3 hereof), and the Authority hereby directs the Borrower to make the payments required hereunder (except such payments for expenses and indemnification) directly to the Trustee. The Borrower hereby assents to such assignment and agrees to make payments directly to the Trustee without defense or set-off by reason of any dispute between the Borrower and the Authority or the Trustee.

SECTION 4.5. AMOUNTS REMAINING IN FUNDS. It is agreed by the parties hereto that after payment in full of (i) the Bonds, or after provision for such payment shall have been made as provided in the Indenture, (ii) the fees, charges and expenses of the Trustee, paying agents and the

Authority in accordance with the Indenture and (ill) all other amounts required to be paid under this Agreement and the Indenture including, without limitation, amounts required to be paid from the Rebate Fund, any amounts remaining in any fund held by the Trustee under the Indenture shall belong to the Borrower and be paid to the Borrower by the Trustee.

ARTICLE V

SPECIAL COVENANTS AND AGREEMENTS

SECTION 5.1. POWER TO ESTABLISH CHARGES AND COLLECT AMOUNTS. The Borrower has, and shall maintain as long as any Bonds are Outstanding, the lawful power to establish charges and cause to be collected amounts with respect to the Project.

SECTION 5.2. RIGHT OF ACCESS TO THE PROJECT. The Borrower agrees that during the term of this Agreement the Authority, the Trustee and the duly authorized agents of either of them shall have the right at all reasonable times during normal business hours, upon reasonable notice to the Borrower, to enter upon the site of the Project to examine and inspect the Project; provided, however, that this right is subject to federal and State laws and regulations applicable to the site of the Project and may be exercised only for the purpose of carrying out the duties of the Authority and the Trustee, respectively, hereunder and under the Indenture. The rights of access hereby reserved to the Authority and the Trustee may be exercised only after such agent shall have executed release of liability and secrecy agreements if requested by the Borrower in the form then currently used by the Borrower, and nothing contained in this Section or in any other provision of this Agreement shall be construed to entitle the Authority or the Trustee to any information or inspection involving the confidential know-how of the Borrower.

SECTION 5.3. THE BORROWER'S MAINTENANCE OF ITS EXISTENCE; ASSIGNMENTS.

(a) To the extent permitted or required by law and its articles of incorporation, the Borrower agrees that during the term of this Agreement it will maintain its existence as a corporation, will continue to maintain its status as a corporation in good standing in the State, will not dissolve or otherwise dispose of all or substantially all of its assets and will not combine or consolidate with or merge into another person or permit one or more persons to consolidate with or merge into it; provided, however, that if the Borrower has obtained the prior written consent of the Authority, which consent shall not be unreasonably withheld, the Borrower may so combine, consolidate with, or merge into another person legally existing under the laws of one of the states of the United States, or permit one or more persons to consolidate with or merge into it, or sell or otherwise transfer to another person all or substantially all of its assets as an entity and thereafter dissolve. The consent of the Authority shall be given within 30 days after written evidence acceptable to the Authority is provided by the Borrower to demonstrate that (i) the surviving, resulting or transferee person, as the case may be, assumes and agrees in writing to pay and perform all of the obligations of the Borrower hereunder, (ii) the surviving, resulting or transferee person, as the case may be, qualifies to do business in the State, (iii) the resulting or transferee person shall have a net worth (as determined in accordance with generally accepted accounting principles) immediately after such consolidation, merger, sale or transfer greater than or equal to 95 % of the net worth of the Borrower at the end of the fiscal quarter immediately preceding the effective date of

such consolidation, merger, sale or transfer, and (iv) the credit rating on the Bonds, as determined by the bond rating service then rating the Bonds, shall remain at the same rating level, or a higher rating level, as the rating level of the Bonds immediately prior to the effective date of such consolidation, merger, sale or transfer. If the Authority does not act within 30 days after such written evidence is received, such consent shall be deemed to be given.

Within 10 business days of the consummation of the merger (other than a merger involving the Borrower and any wholly-owned subsidiary of the Borrower) or other transaction, the Borrower shall provide the Authority with counterpart copies of the merger instruments, or other documents constituting the transaction, including (A) copies of the instruments of assumption referred to in (i) above, and (B) evidence of qualification as referred to in (ii) above. The Borrower shall also at such time provide the Authority with an opinion of counsel satisfactory to the Authority that the Borrower has complied with all of the provisions of this Section 5.3(a). In the case of a merger involving the Borrower and any wholly-owned subsidiary of the Borrower, the Borrower shall send the Authority a notice of such merger within 10 business days after its completion, together with an opinion of counsel as described in the preceding sentence. The Borrower shall provide the Authority with at least 30 days' written notice prior to the consummation of any merger or other transaction described in (iii) above. At such time the Borrower shall provide the Authority with drafts of the documents of assumption and the legal opinion referred to above, and with copies of pro forma financial statements showing expected compliance with the requirements of (iii) above. The Borrower agrees to provide such other information as the Authority may reasonably request in order to assure compliance with this Section 5.3(a).

Notwithstanding any other provisions of this Section 5.3(a), the Borrower need not comply with any of the provisions of Section 5.3(a) above if, at the time of such merger, combination, sale of assets, dissolution or reorganization, the Bonds will be defeased as provided in Article X of the Indenture.

(b) The rights and obligations of the Borrower under this Agreement may be assigned by the Borrower to any person in whole or in part, subject, however, to each of the following conditions:

(i) No assignment other than pursuant to subsection (a) of this Section shall relieve the Borrower from primary liability for any of its obligations hereunder, and in the event of any assignment not pursuant to subsection (a) of this Section the Borrower shall continue to remain primarily liable for the payments specified in Section 4.2 hereof and for performance and observance of the other agreements on its part herein provided to be performed and observed by it.

(ii) Any assignment from the Borrower shall retain for the Borrower such rights and interests as will permit it to perform its obligations under this Agreement, and any assignee from the Borrower shall assume in writing the obligations of the Borrower hereunder to the extent of the interest assigned.

(iii) The Borrower shall give the Authority thirty-days notice of any assignment, (other than pursuant to subsection (a) above) and shall, within thirty days after delivery of any assignment, furnish or cause to be furnished to the Authority and the Trustee a true and

complete copy of each such assignment together with an instrument of assumption, and an Opinion of Counsel satisfactory to the Authority that the Borrower has complied with the provisions of this Section 5.3(b).

SECTION 5.4. RECORDS AND FINANCIAL STATEMENTS OF BORROWER. The Borrower shall deliver to the Trustee and, to the extent requested in writing, to the Authority, the following:

(a) As soon as available, but in no event more than one-hundred and twenty (120) days after the end of each fiscal year, copies of the Borrower's statements of operation for such fiscal year, financial statements of cash flows for such fiscal year, all prepared in accordance with generally accepted accounting principles applicable to the Borrower, and setting forth in each case in comparative form the figures for the previous fiscal year. All financial statements shall be certified by independent certified public accountants of national standing, showing the financial condition of the Borrower at the close of such fiscal year and the results of Project operations during such fiscal year;

(b) Simultaneously with the delivery of each set of financial statements referred to in clause (a) above, a certificate of an Authorized Borrower Representative stating whether there exists on the date of such certificate any circumstance known to the Borrower that, with the passage of time or the giving of notice constitutes or would constitute an Event of Default and, if any circumstance known to the Borrower that, with the passage of time or the giving of notice constitutes or would constitute an Event of Default exists, setting forth the details thereof and the action which the Borrower is taking or proposes to take with respect thereto (this certificate shall always be delivered to the Authority);

(c) Simultaneously with the delivery of each set of financial statements referred to in clause (a) above, a statement (for so long as such statements are routinely provided by the independent public accountant certifying the financial statements in Section 5.4(a) to its clients) of the firm of independent public accountants which reported on such statements advising that nothing has come to their attention to cause them to believe that there existed on the date of such statements any Event of Default; provided, that failure to obtain and deliver such a certificate shall not be a default under Article VI;

(d) Forthwith upon the occurrence of any circumstance known to the Borrower that, with the passage of time or the giving of notice, constitutes or would constitute an Event of Default, a certificate of an Authorized Borrower Representative setting forth the details thereof and the action which the Borrower is taking or proposes with respect thereto; provided that a cure of any occurrence for which notice pursuant to this clause should be given will cure any failure of the notice provisions of this clause;

(e) From time to time, such additional information regarding the financial position or business operations of the Borrower, as the Trustee or the Authority may reasonably request; and

(f) At the same time as the financial statements are delivered pursuant to clause (a) above, a certificate of an Authorized Borrower Representative stating that all routine and major maintenance to the Project has been performed.

SECTION 5.5. MAINTENANCE AND REPAIR; TAXES; UTILITY AND OTHER CHARGES; INSURANCE. The Borrower agrees to maintain, to the extent permitted or required by applicable law and regulation, the Project, or cause the Project to be so maintained, during the term of this Agreement (i) in as reasonably safe condition as its operations shall permit and (ii) in good repair and in good operating condition, ordinary wear and tear excepted, making from time to time all necessary repairs thereto and renewals and replacements thereof.

The Borrower agrees to pay or cause to be paid during the term of this Agreement all taxes, governmental charges of any kind lawfully assessed or levied upon the Project or any part thereof, including any taxes levied against the Project which, if not paid, will become a charge on the receipts from the Project prior to or on a parity with the charge thereon and the pledge or assignment thereof to be created therefrom or under this Agreement, all utility and other charges incurred in the operation, maintenance, use, occupancy and upkeep of the Project and all assessments and charges lawfully made by any governmental body for public improvements that may be secured by a lien on the Project, provided that with respect to special assessments or other governmental charges that may lawfully be paid in installments over a period of years, the Borrower shall be obligated to pay only such installments as are required to be paid during the term of this Agreement. The Borrower may, at the Borrower's expense and in the Borrower's name, in good faith, contest any such taxes, assessments and other charges and, in the event of any such contest, may permit the taxes, assessments or other charges so contested to remain unpaid during that period of such contest and any appeal therefrom unless by such nonpayment the Project or any part thereof will be subject to loss or forfeiture.

The Borrower agrees that it will keep, or cause to be kept (i) the Project insured against such risks and in such amounts and for such occurrences as similar properties are usually insured by companies similarly situated against loss or damage of the kinds usually insured against by companies similarly situated, either by means of policies issued by reputable insurance companies or, at Borrower's election, partially or wholly by means of an adequate self-insurance program, and (ii) insurance against all direct or contingent loss or liability for personal injury, death or property damage occasioned by the operation of the Project, which insurance may be a part of the policy or policies of insurance customarily maintained by the Borrower in connection with its general property and liability insurance upon all of the plants and properties operated by it (including such deductibles as may be provided in said policies).

SECTION 5.6. TAX-EXEMPT STATUS OF BONDS. It is the intention of the parties hereto that interest on the Bonds shall be and remain Tax-exempt and to that end the covenants and agreements of the Authority and the Borrower in this Section are for the benefit of the Trustee and each and every holder of the Bonds.

The Borrower represents and warrants that substantially all of the proceeds of the Bonds will be used with respect to the Project as more specifically set forth in the Tax Certificate.

The Authority covenants and agrees that it has not taken and will not take any action which results in interest paid on the Bonds not being Tax-exempt to the holders of the Bonds, and the Borrower covenants and agrees that it has not taken or permitted to be taken and will not take or permit to be taken any action which will cause the interest on the Bonds not to be Tax-exempt to the holders thereof; provided that neither the Borrower nor the Authority shall have violated these covenants if the interest on any of the Bonds becomes taxable to a person solely because such person is a "substantial user" of the Project or a "related person" within the meaning of Section 147(a) of the Code; and provided further that none of the covenants and agreements herein contained shall require either the Borrower or the Authority to enter an appearance or intervene in any administrative, legislative or judicial proceeding in connection with any changes in applicable laws, rules or regulations or in connection with any decisions of any court or administrative agency or other governmental body affecting the taxation of interest on the Bonds.

SECTION 5.7. NOTICE AND CERTIFICATES TO TRUSTEE. The Borrower hereby agrees to provide the Trustee with the following:

(a) On or before the fifth business day following June 30 and December 31 of each year (commencing June 30, 1997) in which any of the Bonds are outstanding a certificate of an officer of the Borrower that: (i) all payments required under this Agreement have been made and (ii) any applicable third party credit support will continue in full force during the succeeding twelve months, or explaining why not;

(b) Within one hundred twenty (120) days of the end of the fiscal year of the Borrower, (i) a certificate of an officer of the Borrower to the effect that to the best of such officer's knowledge, there exists no event of default or potential default (which exists or which has previously occurred) and (ii) the audited annual report of the Borrower;

(c) Upon knowledge of an Event of Default under this Agreement or the Indenture, notice of such Event of Default, such notice to include a description of the nature of such event and what steps are being taken to remedy such Event of Default; and

(d) At the time of filing the certificates referred to in (a) above, a written disclosure of any significant change known to the Borrower that occurs which would adversely impact the Trustee's ability to perform its duties under the Indenture, or of any conflicts which may result because of other business dealings between the Trustee and the Borrower.

SECTION 5.8. CONTINUING DISCLOSURE. The Borrower hereby covenants and agrees that it will comply with and carry out all of the provisions of the Continuing Disclosure Agreement. Notwithstanding any other provision of this Loan Agreement, failure of the Borrower to comply with the Continuing Disclosure Agreement shall not be considered an Event of Default hereunder; however, the Trustee shall at the request of any Participating Underwriter (as defined in the Continuing Disclosure Agreement) or the Holders of at least 25 % aggregate principal amount in Outstanding Bonds (upon receipt of satisfactory indemnification), or any Bondholder or Beneficial Owner may take such actions as may be necessary and appropriate, including seeking specific performance by court order, to cause the Borrower to comply with its obligations under this Section. For purposes of this Section, "Beneficial Owner" means any person which has the power, directly or

indirectly, to vote or consent with respect to, or to dispose of ownership of, any Bonds (including persons holding Bonds through nominees, depositories or other intermediaries).

SECTION 5.9. QUALIFICATION IN CALIFORNIA. The Borrower agrees that throughout the term of this Agreement it, or any successor or assignee as permitted by Section 5.3, will be qualified to do business in the State.

ARTICLE VI

EVENTS OF DEFAULT AND REMEDIES

SECTION 6.1. EVENTS OF DEFAULT. Any one of the following which occurs and continues shall constitute an Event of Default:

(a) failure by the Borrower to pay any amounts required to be paid under Section 4.2(a) hereof which failure causes an Event of Default under the Indenture;

(b) failure of the Borrower to observe and perform any covenant, condition or agreement on its part required to be observed or performed by this Agreement, other than making the payments referred to in (a) above, which continues for a period of 30 days after written notice, which notice shall specify such failure and request that it be remedied, given to the Borrower by the Authority or the Trustee, unless the Authority and the Trustee shall agree in writing to an extension of such time; provided, however, that if the failure stated in the notice cannot be corrected within such period, the Authority and the Trustee will not unreasonably withhold their consent to an extension of such time if corrective action is instituted within such period and diligently pursued until the default is corrected; or

(c) an Act of Bankruptcy of the Borrower.

The provisions of subsection (b) of this Section are subject to the limitation that the Borrower shall not be deemed in default if and so long as the Borrower is unable to carry out its agreements hereunder by reason of strikes, lockouts or other industrial disturbances; acts of public enemies; orders of any kind of the government of the United States or of the State of California or any of their departments, agencies or officials, or any civil or military authority; insurrections; riots; epidemics; landslides; lightning; earthquake; fire; hurricanes; storms; floods; washouts; droughts; arrests; restraint of government and people; civil disturbances; explosions; breakage or accident to machinery, transmission pipes or canals; partial or entire failure of utilities; or any other cause or event not reasonably within the control of the Borrower; it being agreed that the settlement of strikes, lockouts and other industrial disturbances shall be entirely within the discretion of the Borrower, and the Borrower shall not be required to make settlement of strikes, lockouts and other industrial disturbances by acceding to the demands of the opposing party or parties when such course is, in the judgment of the Borrower, unfavorable to the Borrower. This limitation shall not apply to any default under subsections (a) or (c) of this Section.

SECTION 6.2. REMEDIES ON DEFAULT. Whenever any Event of Default shall have occurred and shall continue:

(a) The Trustee, by written notice to the Borrower, shall declare the unpaid balance of the loan payable under Section 4.2(a) of this Agreement to be due and payable immediately, if concurrently with or prior to such notice the unpaid principal amount of the Bonds shall have been declared to be due and payable. Upon any such declaration such amount shall become and shall be immediately due and payable as set forth in Section 7.01 of the Indenture.

(b) The Trustee may have access to and may inspect, examine and make copies of the books and records and accounts, data and federal income tax and other tax returns of the Borrower.

(c) The Authority or the Trustee may take whatever action at law or in equity as may be necessary or desirable to collect the payments and other amounts then due and thereafter to become due or to enforce performance and observance of any obligation, agreement or covenant of the Borrower under this Agreement. Nothing in Section 4.4 of this Agreement shall be deemed to limit the rights of the Authority under this Section 6.2(c); provided that, the Authority will not exercise any remedies, with respect to any of the Authority's rights assigned to the Trustee pursuant to Section 4.4 of this Agreement unless, in the Authority's reasonable judgment and after written request to the Trustee, the Trustee has failed to enforce such rights.

In case the Trustee or the Authority shall have proceeded to enforce its rights under this Agreement and such proceedings shall have been discontinued or abandoned for any reason or shall have been determined adversely to the Trustee or the Authority, then, and in every such case, the Borrower, the Trustee and the Authority shall be restored respectively to their several positions and rights hereunder, and all rights, remedies and powers of the Borrower, the Trustee and the Authority shall continue as though no such action had been taken.

The Borrower covenants that, in case an Event of Default shall occur with respect to the payment of any Repayment Installment payable under Section 4.2(a) hereof, then, upon demand of the Trustee, the Borrower will pay to the Trustee the whole amount that then shall have become due and payable under said Section, with interest, to the extent permitted by law, on the amount then overdue at the rate of interest per annum borne by the Bonds until such amount has been paid.

In case the Borrower shall fall forthwith to pay such amounts upon such demand, the Trustee shall be entitled and empowered to institute any action or proceeding at law or in equity for the collection of the sums so due and unpaid, and may prosecute any such action or proceeding to judgment or final decree, and may enforce any such judgment or final decree against the Borrower and collect in the manner provided by law the moneys adjudged or decreed to be payable.

In case proceedings shall be pending for the bankruptcy or for the reorganization of the Borrower under the federal bankruptcy laws or any other applicable law, or in case a receiver or trustee shall have been appointed for the property of the Borrower or in the case of any other similar judicial proceedings relative to the Borrower, or the creditors or property of the Borrower, then the Trustee shall be entitled and empowered, by intervention in such proceedings or otherwise, to file and prove a claim or claims for the whole amount owing and unpaid pursuant to this Agreement and,

in case of any judicial proceedings, to file such proofs of claim and other papers or documents as may be necessary or advisable in order to have the claims of the Trustee allowed in such judicial proceedings relative to the Borrower, its creditors or its property, and to collect and receive any moneys or other property payable or deliverable on any such claims, and to distribute such amounts as provided in the Indenture after the deduction of its charges and expenses. Any receiver, assignee or trustee in bankruptcy or reorganization is hereby authorized to make such payments to the Trustee, and to pay to the Trustee any amount due it for compensation and expenses, including expenses and fees of counsel incurred by it up to the date of such distribution.

SECTION 6.3. AGREEMENT TO PAY ATTORNEYS' FEES AND EXPENSES. In the event the Borrower should default under any of the provisions of this Agreement and the Authority or the Trustee should employ attorneys or incur other expenses for the collection of the payments due under this Agreement or the enforcement of performance or observance of any obligation or agreement on the part of the Borrower herein contained, the Borrower agrees to pay to the Authority or the Trustee the reasonable fees of such attorneys and such other expenses so incurred by the Authority or the Trustee.

SECTION 6.4. NO REMEDY EXCLUSIVE. No remedy herein conferred upon or reserved to the Authority or the Trustee is intended to be exclusive of any other available remedy or remedies, but each and every such remedy shall be cumulative and shall be in addition to every other remedy given under this Agreement or now or hereafter existing at law or in equity or by statute. No delay or omission to exercise any right or power accruing upon any default shall impair any such right or power or shall be construed to be a waiver thereof, but any such right and power may be exercised from time to time and as often as may be deemed expedient. In order to entitle the Authority or the Trustee to exercise any remedy reserved to it in this Article, it shall not be necessary to give any notice, other than such notice as may be herein expressly required. Such rights and remedies as are given the Authority hereunder shall also extend to the Trustee, and the Trustee and the holders of the Bonds shall be deemed third party beneficiaries of all covenants and agreements herein contained.

SECTION 6.5. NO ADDITIONAL WAIVER IMPLIED BY ONE WAIVER. In the event any agreement or covenant contained in this Agreement should be breached by the Borrower and thereafter waived by the Authority or the Trustee, such waiver shall be limited to the particular breach so waived and shall not be deemed to waive any other breach hereunder.

ARTICLE VII

PREPAYMENT

SECTION 7.1. REDEMPTION OF BONDS WITH PREPAYMENT MONEYS. By virtue of the assignment of the rights of the Authority under this Agreement to the Trustee as is provided in Section 4.4 hereof, the Borrower agrees to and shall pay directly to the Trustee any amount permitted or required to be paid by it under this Article VII. The Trustee shall use the moneys so paid to it by the Borrower to redeem the Bonds on the date set for such redemption pursuant to Section 7.5 hereof.

SECTION 7.2. OPTIONS TO PREPAY INSTALLMENTS. The Borrower shall have the option to prepay the amounts payable under Section 4.2 hereof with respect to the Bonds, in whole or in part, by paying to the Trustee, for deposit in the Bond Fund, the amount set forth in Section 7.4 hereof, under circumstances set forth in Section 4.01(a) of the Indenture. The Borrower shall notify the Trustee and the Authority in writing of its election to prepay the amounts payable hereunder and direct the Trustee to cause the Bonds to be redeemed on a date specified, which shall be at least 45 days after the date of such notice.

SECTION 7.3. MANDATORY PREPAYMENT. The Borrower shall have and hereby accepts the obligation to prepay Repayment Installments with respect to the Bonds to the extent mandatory redemption of the Bonds is required pursuant to Section 4.01(1,) of the Indenture and upon the occurrence of any of the following events:

(i) all or substantially all of the properties of the Borrower shall be sold or taken through the exercise of the right of eminent domain or the right to purchase by any municipal or governmental body or agency; or

(ii) a Determination of Taxability.

In the case of any of the events stated in this Section 7.3, the Borrower must satisfy its obligation by prepaying within 180 days after such event, such prepayment date to be specified in writing by the Borrower to the Trustee and the Authority at least 45 days in advance.

The amount payable by the Borrower in the event of a prepayment required by this Section shall be determined as set forth in Section 7.4 and shall be deposited in the Bond Fund.

SECTION 7.4. AMOUNT OF PREPAYMENT. In the case of a prepayment of the entire amount due hereunder with respect to the Bonds pursuant to Section 7.2 or 7.3 hereof, the amount to be paid shall be a sum sufficient, together with other funds and the yield on any securities deposited with the Trustee and available without reinvestment for such purpose, to pay (1) the principal of all Bonds outstanding on the redemption date specified in the notice of redemption, plus interest accrued and to accrue to the payment or redemption date of the Bonds, plus premium, if any, required pursuant to the Indenture, (2) all reasonable and necessary fees and expenses of the Authority, the Trustee and any paying agent accrued and to accrue through final payment of the Bonds and (3) all other liabilities of the Borrower accrued and to accrue with respect to the Bonds under this Agreement.

In the case of partial prepayment of the Repayment Installments, the amount payable shall be a sum sufficient, together with other funds deposited with the Trustee and available without reinvestment for such purpose, to pay the principal amount of and premium, if any, and accrued interest on the Bonds to be redeemed, as provided in the Indenture, and to pay the expenses of redemption of the Bonds.

SECTION 7.5. NOTICE OF PREPAYMENT. To exercise an option granted in or to perform an obligation required by this Article VII, the Borrower shall give written notice at least fifteen (15) days prior to the last day by which the Trustee is permitted to give notice of redemption pursuant to

Section 4.03 of the Indenture to the Authority and the Trustee specifying the date upon which any prepayment will be made. If the Borrower fails to give such notice of a prepayment required by this Section 7.5, such notice may be given by the Authority, by the Trustee or by any holder or holders of 10% or more in aggregate principal amount of the Bonds outstanding. The Authority and the Trustee, at the request of the Borrower or any such Bondholder, shall forthwith take all steps necessary under the applicable provisions of the Indenture (except that neither the Authority nor the Trustee shall be required to make payment of any money required for such redemption) to effect redemption of all or part of the then outstanding Bonds, on the earliest practicable date thereafter on which such redemption may be made under applicable provisions of the indenture.

ARTICLE VIII

NON-LIABILITY OF AUTHORITY; EXPENSES; INDEMNIFICATION

SECTION 8.1. NON-LIABILITY OF AUTHORITY. The Authority shall not be obligated to pay the principal of, or premium, if any, or interest on the Bonds, except from Revenues. The Borrower hereby acknowledges that the Authority's sole source of moneys to repay the Bonds will be provided by the payments made by the Borrower pursuant to this Agreement, together with other Revenues, including investment income on certain funds and accounts held by the Trustee under the Indenture, and hereby agrees that if the payments to be made hereunder shall ever prove insufficient to pay all principal of, and premium, if any, and interest on the Bonds as the same shall become due (whether by maturity, redemption, acceleration or otherwise), then upon written notice from the Trustee, the Borrower shall pay such amounts as are required from time to time to prevent any deficiency or default in the payment of such principal, premium, if any, or interest, including, but not limited to, any deficiency caused by acts, omissions, nonfeasance or malfeasance on the part of the Trustee, the Borrower, the Authority or any third party.

SECTION 8.2. EXPENSES. The Borrower covenants and agrees to pay and to indemnify the Authority and the Trustee against all costs and charges, including reasonable fees and disbursements of attorneys, accountants, consultants and other experts, incurred in good faith in connection with this Agreement, the Bonds or the Indenture.

SECTION 8.3. INDEMNIFICATION. The Borrower releases the Authority and the Trustee from, and covenants and agrees that neither the Authority nor the Trustee shall be liable for, and covenants and agrees, to the extent permitted by law, to indemnify and hold harmless the Authority and the Trustee and their directors, officers, employees and agents from and against, any and all losses, claims, damages, liabilities or expenses, of every conceivable kind, character and nature whatsoever arising out of, resulting from or in any way connected with (1) the Project, or the conditions, occupancy, use, possession, conduct or management of, or work done in or about, or from the planning, design, acquisition, installation or construction of the Project or any part thereof; (2) the issuance of any Bonds or any certifications, covenants or representations made in connection therewith and the carrying out of any of the transactions contemplated by the Bonds and this Agreement; (3) the Trustee's acceptance or administration of the trusts under the Indenture, or the exercise or performance of any of its powers or duties under the Indenture; or (4) any untrue statement or alleged untrue statement of any material fact or omission or alleged omission to state a

material fact necessary to make the statements made, in light of the circumstances under which they were made, not misleading, in any continuing disclosure documents, official statement or other offering circular utilized by the Authority or any underwriter or placement agent in connection with the sale of any Bonds; provided that such indemnity shall not be required for damages that result from negligence or willful misconduct on the part of the party seeking such indemnity. The indemnity required by this Section shall be only to the extent that any loss sustained by the Authority or the Trustee exceeds the net proceeds the Authority or the Trustee receives from any insurance carried with respect to the loss sustained. The Borrower further covenants and agrees, to the extent permitted by law, to pay or to reimburse the Authority and the Trustee and their officers, employees and agents for any and all costs, reasonable attorneys fees, liabilities or expenses incurred in connection with investigating, defending against or otherwise in connection with any such losses, claims, damages, liabilities, expenses or actions, except to the extent that the same arise out of the negligence or willful misconduct of the party claiming such payment or reimbursement. The provisions of this Section shall survive the retirement of the Bonds or the removal or resignation of the Trustee.

ARTICLE IX

MISCELLANEOUS

SECTION 9.1. NOTICES. All notices, certificates or other communications shall be deemed sufficiently given on the second day following the day on which the same have been mailed by certified mail, postage prepaid, addressed to the Authority, the Borrower or the Trustee as the case may be, as follows:

To the Authority: California Pollution Control Financing Authority
915 Capitol Mall, Suite 466
Sacramento, California 95814
Attention: Executive Director

To the Borrower: Southern California Water Company
630 East Foothill Boulevard
San Dimas, CA 91773
Attention: Treasurer

To the Trustee: Chemical Trust Company of California
101 California Street, Suite 2725
San Francisco, CA 94111
Attention: Corporate Trust Department

A duplicate copy of each notice, certificate or other communication given hereunder by either the Authority or the Borrower to the other shall also be given to the Trustee and the Bond Insurer. The Authority, the Borrower and the Trustee may, by notice given hereunder, designate any different addresses to which subsequent notices, certificates or other communications shall be sent.

SECTION 9.2. SEVERABILITY. If any provision of this Agreement shall be held or deemed to be, or shall in fact be, illegal, inoperative or unenforceable, the same shall not affect any other provision or provisions herein contained or render the same invalid, inoperative, or unenforceable to any extent whatever.

SECTION 9.3. EXECUTION OF COUNTERPARTS. This Agreement may be simultaneously executed in several counterparts, each of which shall be an original and all of which shall constitute but one and the same instrument; provided, however, that for purposes of perfecting a security interest in this Agreement to the Trustee under Article 9 of the California Uniform Commercial Code, only the counterpart delivered, pledged and assigned to the Trustee shall be deemed the original.

SECTION 9.4. AMENDMENTS, CHANGES AND MODIFICATIONS. Except as otherwise provided in this Agreement or the Indenture, subsequent to the initial issuance of Bonds and prior to their payment in full, or provision for such payment having been made as provided in the Indenture, this Agreement may not be effectively amended, changed, modified, altered or terminated by the Authority and the Borrower without the written consent of the Trustee and the Bond Insurer.

Notice of any such amendment to this Agreement or the Indenture shall be promptly delivered to any rating agency then maintaining a rating on the Bonds.

SECTION 9.5. GOVERNING LAW. This Agreement shall be governed exclusively by and construed in accordance with the applicable laws of the State. This Agreement shall also be enforceable in the State and any action arising out of this Agreement shall be filed and maintained in the Sacramento County Superior Court, Sacramento, California; provided that the Authority may waive the requirement of venue. The parties agree that the terms and conditions of this Agreement supersede those of all previous agreements between the parties with respect to the subject matter hereto, and that this Agreement, together with the documents referred to in this Agreement, contains the entire agreement between the parties hereto. In the event of a dispute between the parties under this Agreement, the losing party in such dispute shall pay all costs and expenses incurred by the prevailing party in connection therewith, including but not limited to attorneys fees.

SECTION 9.6. AUTHORIZED BORROWER REPRESENTATIVE. Whenever under the provisions of this Agreement the approval of the Borrower is required or the Borrower is required to take some action at the request of the Authority, such approval or such request shall be given on behalf of the Borrower by the Authorized Borrower Representative, and the Authority and the Trustee shall be authorized to act on any such approval or request and neither party hereto shall have any complaint against the other or against the Trustee as a result of any such action taken.

SECTION 9.7. TERM OF THE AGREEMENT. This Agreement shall be in full force and effect from the date hereof and shall continue in effect as long as any of the Bonds are outstanding or the Trustee holds any moneys under the Indenture, whichever is later provided, however, that the rights of the Trustee and the Authority under Sections 8.2 and 8.3 hereof shall survive the termination of this Agreement, the retirement of the Bonds and the removal or resignation of the

Trustee. All representations and certifications by the Borrower as to all matters affecting the Tax-exempt status of the Bonds shall survive the termination of this Agreement.

SECTION 9.8. BINDING EFFECT. This Agreement shall inure to the benefit of and shall be binding upon the Authority, the Borrower and their respective successors and assigns; subject, however, to the limitations contained in Section 5.3 hereof.

IN WITNESS WHEREOF, the California Pollution Control Financing Authority has caused this Agreement to be executed in its name and its seal to be hereunto affixed and attested by its duly authorized officers, and Southern California Water Company has caused this Agreement to be executed in its name and its seal to be hereunto affixed by its duly authorized officers, all as of the date first above written.

CALIFORNIA POLLUTION CONTROL
FINANCING AUTHORITY
By Matt Fong, Chairman

By: _____

[SEAL]

Attest:

Executive Director

SOUTHERN CALIFORNIA WATER
COMPANY

By: _____
Vice President and Treasurer

[SEAL]

Attest:

Secretary

IN WITNESS WHEREOF, the California Pollution Control Financing Authority has caused this Agreement to be executed in its name and its seal to be hereunto affixed and attested by its duly authorized officers, and Southern California Water Company has caused this Agreement to be executed in its name and its seal to be hereunto affixed by its duly authorized officers, all as of the date first above written.

CALIFORNIA POLLUTION CONTROL
FINANCING AUTHORITY
By Matt Fong, Chairman

By: _____

[SEAL]

Attest:

Executive Director

SOUTHERN CALIFORNIA WATER
COMPANY

By: _____
Vice President and Treasurer

[SEAL]

Attest:

Secretary

EXHIBIT A

DESCRIPTION OF THE PROJECT

The Project includes the acquisition, construction and installation of water mains facilities and appurtenances thereto, situated at the following locations throughout the State and acquired at the following respective costs:

Location

- - - - -

- (a) in Bell, Los Angeles County, California; facilities located at:
 1,200 feet of water mains on Atlantic, from Florence to Brompton,
 3,100 feet of water mains on Gage, from Wilcox to Atlantic,
 3,800 feet of water mains on Gage, from Atlantic to California,
- (b) in Culver City, Los Angeles County, California; facilities located at:
 810 feet of water mains on Jefferson, from Dobson to Sepulveda,
 850 feet of water mains on Berryman, from McDonald to Port,
 864 feet of water mains on Berryman, from McDonald to Port,
- (c) in Walnut Park, Los Angeles County, California; facilities located at:
 1,075 feet of water mains on Hickory, from Firestone to 83rd Street,
- (d) in South Gate, Los Angeles County, California; facilities located at:
 900 feet of water mains on Harding, from alley to Center,
- (e) in Artesia, Los Angeles County, California; facilities located at:
 300 feet of water mains in the alley east of Gridley, south of Ashworth
- TOTAL \$8,000,000

Strength
Growth
Strategy

AMERICAN STATES WATER COMPANY
1998 Annual Report

COVER

AWR offers long-term, income-oriented investors an attractive total return potential.

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INSIDE FRONT COVER

CORPORATE PROFILE

American States Water Company (NYSE:AWR) is a holding company for Southern California Water Company (SCW) and American States Utility Services, Inc. (ASUS).

SCW is a public utility company engaged principally in the delivery of water service. SCW operates 41 separate water systems within 75 communities in 10 counties in the State of California and provides water service to over 1 million people, or 1 out of every 30 Californians. In addition, SCW provides electric service to approximately 21,000 customers.

SCW focuses on customers by providing water and electric services at affordable rates approved by the California Public Utilities Commission (CPUC). Providing over one-half of the water it sells from its own wells, SCW complies with state environmental regulations and the federal Safe Drinking Water Act.

SCW has no mortgage debt and its unsecured debt rating of "A+" allows ample access to finance its capital expansion programs.

ASUS engages in non-regulated business activities through long-term leases or operation and maintenance contracts with municipally owned water and wastewater systems. ASUS meets the needs and challenges facing municipalities throughout the country, by offering cost effective alternatives to higher water rates and diminishing water supplies.

AWR offers long-term, income-oriented investors an attractive total return potential. AWR has paid dividends on its common shares every year since 1931 and has increased dividends paid out annually since 1953. AWR has a corporate rating of "A" and has no outstanding mortgage debt.

AWR's philosophy is to continue to implement long-term strategies through its subsidiaries, to increase shareholder value by earning the authorized rate of return for its utility operations, and to increase overall earnings through selective non-regulated activities.

1929:
The Company's predecessor, American States Public Service Company of California incorporated; serving 42,000 customers

[3 GRAPHS P. 2]

1930:
First Shareholder
Meeting of American States
Public Service Company
of California

1936:
Official name change
to Southern California
Water Company
and the corporate merging of
Bear Valley Utility
Company into Southern
California Water Company

SELECTED FINANCIAL DATA

(dollars in thousand, except per share
amounts)

| | 1998 | 1997 | 1996 | 1995 | 1994 |
|---|-----------|-----------|-----------|-----------|-----------|
| | ---- | ---- | ---- | ---- | ---- |
| Income Statement Information | | | | | |
| Total Operating Revenues | \$148,060 | \$153,755 | \$151,529 | \$129,813 | \$122,675 |
| Total Operating Expenses | 122,999 | 130,297 | 128,100 | 108,425 | 103,745 |
| Operating Income | 25,061 | 23,458 | 23,429 | 21,388 | 18,930 |
| Other Income | 769 | 758 | 531 | 336 | 236 |
| Interest Charges | 11,207 | 10,157 | 10,500 | 9,559 | 7,828 |
| Net Income | 14,623 | 14,059 | 13,460 | 12,165 | 11,338 |
| Preferred Dividends | 90 | 92 | 94 | 96 | 98 |
| Earnings Available for Common Shareholders | 14,533 | 13,967 | 13,366 | 12,069 | 11,240 |
| Basic Earnings per Common Share | \$ 1.62 | \$ 1.56 | \$ 1.69 | \$ 1.54 | \$ 1.43 |
| Dividends Declared per Common Share | \$ 1.26 | \$ 1.25 | \$ 1.23 | \$ 1.21 | \$ 1.20 |
| Balance Sheet Information | | | | | |
| Total Assets | \$484,671 | \$457,074 | \$430,922 | \$406,255 | \$383,627 |
| Net Utility Plant | 414,753 | 383,623 | 357,776 | 334,968 | 317,879 |
| Common Shareholders' Equity | 154,299 | 151,053 | 146,766 | 121,576 | 118,962 |
| Long-Term Debt | 120,809 | 115,286 | 107,190 | 107,455 | 92,891 |
| Preferred Shares | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 |
| Preferred Shares-Subject to Mandatory Redemption | 400 | 440 | 480 | 520 | 560 |
| Total Capitalization | \$277,108 | \$268,379 | \$256,036 | \$231,151 | \$214,013 |
| Book Value per Common Share | \$ 17.23 | \$ 16.86 | \$ 16.52 | \$ 15.50 | \$ 15.16 |
| Average Shares Outstanding | 8,957 | 7,891 | 7,845 | 7,842 | 8,958 |
| Other Information | | | | | |
| Ratio of Earnings to Fixed Charges | 3.21% | 3.35% | 3.26% | 3.19% | 3.58% |
| Ratio of Earnings to Total Fixed Charges | 3.17% | 3.30% | 3.21% | 3.14% | 3.50% |
| Return on Average Common Equity | 9.6% | 9.5% | 10.7% | 10.3% | 9.7% |

LETTER TO SHAREHOLDERS

1998 was an eventful year in the history of your Company. On July 1, 1998, American States Water Company was formed as the result of approvals received from shareholders and the California Public Utilities Commission (CPUC). On that date, shares of American States Water Company initiated trading on the New York Stock Exchange under the symbol "AWR".

As part of this restructuring, Southern California Water Company became a wholly-owned subsidiary and a new subsidiary, American States Utility Services, Inc. was formed to engage in selective non-regulated operations. We believe the Company is organizationally, operationally and financially poised to meet future challenges in the water utility industry.

FINANCIAL RESULTS

We are pleased to report that for the year ended December 31, 1998, total earnings available for common shareholders were \$14.5 million, or \$1.62 per common share, as compared to total earnings recorded last year of \$14.0 million, or \$1.56 per common share.

The abnormally wet winter weather experienced during the first half of 1998 significantly impacted water sales volumes at the Company's SCW subsidiary and, accordingly, revenues from water and electric operations were \$148.1 million, down by 3.7% from the \$153.8 million recorded in 1997. However, offsetting this decline in revenues, total operating expenses for 1998 decreased by 5.6% to \$123.0 million, primarily reflecting reduced supply costs due to the increase in total water supplied from Company-owned pumped sources.

The Company's stock market performance continued to reward management's efforts. Based on performance measures set forth by the Securities and Exchange Commission, a \$10,000 investment in the common shares of American States Water Company on December 31, 1993, assuming all dividends were reinvested in additional common shares, would have increased in value to approximately \$16,800, a 68% increase in five years.(1)

REGULATORY MATTERS

The Company's subsidiary, SCW received an order from the CPUC increasing rates covering approximately 65% of its water customers. The new rates were effective January 1, 1999 and are based on a 10% return on common equity. In February 1999, SCW filed for rate increases in four additional water customer service areas. When approved, new rates will likely be effective on January 1, 2000.

(1) Past performance is no guarantee of future results. Share values and returns fluctuate and gain or loss may occur when shares are sold.

1936:
First Public Offering of Southern California Water Company

1939-1947:
The War Years, Southern California Water Company prepares for any eventuality by partnering with various utilities for mutual aid in the event of enemy attack

1960:
State Water Project authorized by voters, project bringing a second source of imported water supply to Southern California

WATER QUALITY AND WATER SUPPLY ISSUES

The Company's SCW subsidiary made its compliance filing with the CPUC, pursuant to its Order Instituting Investigation into water quality. A final order in that proceeding is anticipated during 1999. The CPUC maintains that it has primary jurisdiction over water quality matters of the utilities it regulates and has notified the courts of same in the lawsuits faced by the Company.

The California Department of Water Resources (DWR) recently released a report detailing the explosive growth in population anticipated for California and the state's current ability to meet water needs. DWR's plans for meeting these needs include a combination of reduced water usage and the development of additional water supplies. SCW currently meets the water needs of its customers through its own wells and through purchased water. The increased availability of water supplies coupled with enhanced conservation measures will play an important role in the Company's future.

IN CLOSING

At the start of this letter, we discussed the formation of American States Water Company and as you read this Annual Report you will note significant milestones in the 70 year history of your Company. However, one thing has not changed over the years - dedication to meeting our mission of providing safe and reliable water and electric service to our customers and providing growth and return on the investment made by our shareholders. American States Water Company is positioned as a leader for the future, founded on the heritage of the past.

Sincerely,

/s/ Floyd E. Wicks
Floyd E. Wicks
President and Chief Executive Officer

/s/W.V. Caveney
William V. Caveney
Chairman of the Board

[PHOTO P. 5]

"with total assets in excess of \$484,000,000, AWR operates the second largest private water utility in the state of California."

[TABLE P. 6]

[GRAPH P. 7]

STRENGTH

Effective July 1, 1998, American States Water Company (AWR) became the parent company of Southern California Water Company (SCW). The American States name is an integral part of the strength and history of your Company. In 1929, American States Water Services Company of California commenced operations with the acquisition of 34 water systems, an electric utility and a telephone service provider at an original cost of \$5.7 million. In 1936 the name was changed to Southern California Water Company. AWR today, with total assets in excess of \$484 million, operates the second largest private water utility in the state of California, providing water service to over one million people, or 1 out of every 30 Californians.

AWR's historical and continuing objective to improve shareholder value is indicative of its strength. Since 1953, AWR has paid shareholders annual increases in dividends. The Company continues to implement strategies and pursue opportunities to grow earnings and dividends through rate base additions, acquisitions and the provision of services through leases and/or contracts. Because of this, AWR offers long-term, income oriented investors an attractive total return potential.

With a credit rating of "A/A2" from Standard & Poor's and Moody's Investor Services, respectively, AWR is prepared to move into the future by investing in the needs of both the regulated and non-regulated water industry. SCW also continues to maintain its healthy "A+/A2" ratings from Standard & Poor's and Moody's Investor Services, respectively, which provides the financial strength necessary to meet operating and capital expenses.

On August 3, 1998, the Board of Directors adopted a Shareholder Rights Plan. The Plan was designed to address the issue of unilateral actions by hostile acquirers, who would attempt to deprive the Board and shareholders of the ability to determine the company's destiny and receive fair value.

AWR continues to aggressively pursue growth opportunities related to the acquisition and/or operation of municipally-owned water and wastewater systems. A new subsidiary, American States Utility Services, Inc., offers the financial strength and technically trained personnel necessary to secure and provide maintenance and operations under lease, purchase, or specific service contracts.

1994:
SCW organized into regions; Northridge earthquake (6.8 on the Richter Scale);
City of Simi Valley and the CPUC recognize SCW for restoring service to 90% of
its affected customers within 18 hours

GROWTH

1998 was an eventful year for AWR, with new contracts secured with the Cities of Tustin, Bell Gardens, Goleta and Calipatria for various types of utility services. On the regulated side, rates in three of SCW's districts were increased in January 1998 with rates increased in six other districts in January 1999. Working towards stability of rates for customers, SCW filed an application to combine tariff schedules among several of its districts into rates applicable on a regional basis. Long-term rate stability is crucial to each district as costs of operation and infrastructure replacement continue to increase. During 1998, the CPUC approved the Direct Access Implementation Plan of SCW's Bear Valley Electric service area and also excluded any requirement to freeze rates or reduce rates.

One of SCW's many strengths lies in its customer service. In addition to the improved on-line access to the Customer Service Center, further strides were made for Bear Valley electric customers when ATM, credit card and bank by phone payment options were introduced in 1998.

One of the most challenging areas of providing water service continues to be quality assurance. In 1998, SCW completed a comprehensive review of 25 years of water quality records in its response to the CPUC-initiated Order Instituting Investigation (OII) to determine if existing standards and policies regarding drinking water quality adequately protect the public health and if those standards and policies are being uniformly complied with by water utilities. The OII notes the constitutional and statutory jurisdiction of the CPUC and the Department of Health Services (DOHS) to establish and enforce adherence to water quality standards for water delivered by utilities to their customers.

Continuing the Company's efforts in staff development, AWR's corporate university achieved certification by the International Association for Continuing Education and Training in 1998. The Employee Development University is a unique training opportunity for employees and continues to deliver value to its students and ultimately the Company.

[5 PHOTOS P. 9]

commitment
purity
dependable
community
confidence

[GRAPH P. 10]

1996:
Employee
Development University
established

1998:
Creation of
American States Water
Company and American States Utility
Services Company

1999:
First Annual
Meeting of Shareholders of
American States Water Company

STRATEGY

The water utility industry has historically attracted individual investors, rather than institutional owners or sell-side analysts who follow companies and make recommendations to investors on selected companies. This trend is changing as the general turmoil within the regulated utility industry has left water utilities uniquely possessing many of the characteristics which originally attracted portfolio managers and analysts to the regulated industries: relative safety of principal and income generation through dividends. Even within the water utility industry, however, a number of events are changing the landscape. Increased regulatory oversight, water quality and supply concerns, mergers and acquisitions, and financial pressures are interacting to change the manner in which water service is priced and provided.

AWR is well positioned to face these challenges and turn them into opportunities. With good management, a proven earnings record, appropriate valuation and growth potential, AWR ranks high on the key investment criteria used by analysts and portfolio managers to evaluate a company. As one of the largest investor-owned, publicly-traded companies in the U.S. water industry, AWR is financially and technically positioned to meet the significant and ongoing regulatory demands for high quality water service. Through the resources and management of its subsidiaries, AWR can further capitalize on growth opportunities in both the public/private market and the acquisition of other water utility companies.

Management is committed to focus on AWR's four long-term growth strategies: provide safe, reliable water and electric service to customers; earn the return on equity authorized by the CPUC; increase earnings through selected non-regulated, water related activities; acquire utility assets through purchase or merger. Management believes that equal emphasis on all four strategies will best serve the long-term interests of shareholders.

[GRAPH P. 11]

progress o partnering
opportunity

[GRAPH P. 11]

We all honor Bill for
his many years of service
and wish him a very
fulfilled future.

WILLIAM V. CAVENEY - A TRIBUTE

The 1999 Annual Meeting of Shareholders marks an end to a long and distinguished career of a vital force in the Company's 69 year history. When William V. Caveney, Chairman of the Board, retires on April 27, 1999, a 30 year chapter of dedication to the shareholders and employees of the Company draws to a close. His career will be remembered as one of conservative and loyal leadership by a modest and friendly man.

Bill Caveney joined Southern California Water Company in 1968 as manager of the Rate and Valuation Department. His prior 15 years of experience with the staff of the California Public Utilities Commission regulating energy, communications and water utilities assisted him well in leading the department.

Twelve years later his stewardship heightened when, in 1980, he was elected President of Southern California Water Company. This occurred at a time when the water industry was touting the benefits of the Peripheral Canal and the future of importing water to Southern California seemed uncertain. Regardless of the politics or uncertainties, this Company, under Bill's leadership, was poised for a significant period of growth in new water and electric services. Two years later Bill was elected to the position of Chief Executive Officer and, in 1990, was also elected Chairman of the Board.

Bill's unwavering dedication to the success of your Company has been etched in many ways. His guidance, counsel, evenhanded management and, humor will be missed. We all honor Bill for his many years of contributions and wish him a very fulfilled future.

[PHOTO P. 12]

MANAGEMENT'S DISCUSSION AND ANALYSIS

In April 1998, shareholders of Southern California Water Company (SCW) voted to approve formation of a holding company. The formation process was completed on July 1, 1998 at which time American States Water Company (AWR) became the parent company. As a result, SCW became one of AWR's two operating subsidiaries. SCW will continue as a public utility engaged principally in the purchase, distribution and sale of water and also the distributor of electricity in several mountain communities. SCW is regulated by the California Public Utilities Commission (CPUC) as to its water and electric business including properties, rates, services, facilities and other matters. The other subsidiary, American States Utility Services, Inc. (ASUS) is a new company which will perform non-regulated, water related services and operations. AWR and ASUS are not regulated by the CPUC. Unless specifically noted, the following discussion and analysis provides information on AWR's (the Company) consolidated operations and assets.

FORWARD-LOOKING INFORMATION

Certain matters discussed in this report (including the documents incorporated herein by reference) are forward-looking statements intended to qualify for the "safe harbor" from liability established by the Private Securities Litigation Reform Act of 1995. These forward-looking statements can generally be identified as such because the context of the statement will include words such as the Company "believes," "anticipates," "expects" or words of similar import. Similarly, statements that describe the Company's future plans, objectives, estimates or goals are also forward-looking statements. Such statements address future events and conditions concerning capital expenditures, earnings, litigation, rates, water quality and other regulatory matters, adequacy of water supplies, liquidity and capital resources, opportunities related to operations of municipally-owned water systems and accounting matters. Actual results in each case could differ materially from those currently anticipated in such statements, by reason of factors such as utility restructuring, including ongoing local, state and federal activities; future economic conditions, including changes in customer demand; future climatic conditions; legislative, regulatory and other circumstances affecting anticipated revenues and costs; and abilities of other companies to remain or become year 2000 ready.

RESULTS OF OPERATIONS

YEARS ENDED DECEMBER 31, 1998 AND 1997

Basic earnings per common share in 1998 increased by 3.8 % to \$1.62 per share as compared to \$1.56 per share for the comparable period last year. Although wet weather significantly impacted revenues in 1998, lower supply costs and modest increases in other operating expenses partially offset the decline in revenues.

Water operating revenues decreased by 4.3% in 1998 to \$134.9 million from the \$141.0 million reported in 1997. Water sales volumes in 1998 were 9.9% lower than last year due to extremely wet weather during the first half of the year. The decrease in sales was partially offset by rate increases effective during 1998.

Electric operating revenues of \$13.2 million were 3.4% higher in 1998 as compared to last year due to the impact of a general rate increase effective January 1998 as well as a 2.0% increase in kilowatt-hour sales.

Purchased water costs decreased in 1998 to \$30.8 million as compared to \$38.3 million in 1997 due to a 20.8% decrease in volumes purchased and refunds received from the Company's wholesale water supplier during 1998 of approximately \$1.4 million. Refunds of \$20.0 million were received in 1997.

Costs of power purchased for pumping decreased by 7.2% to \$7.0 million in 1998 chiefly as the result of the reduced energy costs from the Company's suppliers.

Costs of power purchased for resale in 1998 decreased by 3.4% to \$5.0 million from the \$5.2 million recorded in 1997 due to reduced costs from the Company's energy providers which partially offset the effects of increased kilowatt-hour sales volumes recorded during the year.

Groundwater production assessments increased 10.5% to \$7.6 million in 1998 from \$6.8 million in 1997 due to the increased amounts of pumped water in the Company's resource mix as well as additional assessments associated with increased pumping in the Company's Metropolitan and Orange County customer service areas.

A positive entry for the provision for supply cost balancing accounts reflects recovery of previously under-collected supply costs. Conversely, a negative entry for the provision for supply cost balancing accounts reflects an under-collection of previously incurred supply costs. In 1998, recovery of previously under-collected supply costs was lower in 1998 than 1997 due to the expiration in

January 1998 of a surcharge designed to recover those costs. It is anticipated that the new rates, effective January 1999, will increase collection of these under-collected costs. The balancing account mechanism insulates earnings from changes in the unit cost of supply costs which are outside of the immediate control of the Company. However, the balancing account is not designed to insulate earnings against changes in supply mix, as occurred during the first eight months of 1997.

Other operating expenses increased by 10.6% from the \$13.1 million recorded in 1997 due to employee time charged to this category. Reversals in 1997 of costs associated with recovery of water quality expenditures through the CPUC's memorandum account mechanism also contributed to the increase. There were no such reversals of equal magnitude in 1998.

Administrative and general expenses decreased slightly by 0.7% to \$22.0 million in 1998 from the \$22.1 million recorded in 1997. The decrease is due to stability in costs associated with health insurance, post-retirement medical benefits, pension and 401(k) plan costs and to a reduction of time charge by employees to this category.

In 1998, maintenance expense remained at approximately the \$7.3 million level recorded in 1997 due principally to the wet weather conditions during the first part of the year that hampered planned maintenance activity.

Depreciation expense in 1998 increased by 14.5% to \$12.5 million reflecting the effects of recording approximately \$38 million in net plant additions during 1997, depreciation on which began in 1998. In addition, amortization of start-up and organizational costs associated with the formation of AWR is reflected in 1998 and there were no similar amortization costs in 1997.

Taxes on income increased by approximately 3.1% to \$10.1 million in 1998 as compared to the \$9.8 million last year due to a 5.7% increase in operating income partially offset by a lower effective tax rate.

Property and other taxes decreased by 2.5% in 1998 to \$6.1 million due primarily to reduced franchise tax payments directly attributable to reduced revenues.

Other income increased by 1.5% in 1998 due principally to the flow-through of tax benefits related to refinancing of long-term debt which was partially offset by an increase in reserves against costs associated with the Company's non-regulated joint venture.

Interest expense increased by 10.3% to \$11.2 million primarily due to increased short-term bank borrowing and the issuance of \$15 million in long-term debt in March 1998.

YEARS ENDED DECEMBER 31, 1997 AND 1996

Basic earnings per common share in 1997 decreased by 7.7% to \$1.56 per share as compared to \$1.69 per share for the comparable period last year, directly attributable to significantly increased supply costs during the first eight months of 1997.

Water operating revenues increased by 0.7% in 1997 to \$141.0 million from the \$140.0 million reported in 1996. Although water sales volumes were 2.7% higher in 1997, in 1996 SCW began recovery of previously incurred supply costs, in accordance with rules of the CPUC. In 1997, recovery of these costs was completed in several customer service areas and rates were accordingly reduced, partially offsetting rate increases effective during 1997 in other customer service areas.

Electric operating revenues of \$12.8 million were 10.7% higher in 1997 as compared to last year due to the impact of a general rate increase effective January 1997 as well as a 3.6% increase in kilowatt-hour sales.

Purchased water costs remained relatively the same at \$38.3 million in 1997 as compared to \$38.4 million in 1996, despite a 6.4% increase in volumes purchased, due to refunds received from SCW's wholesale water supplier during 1997 of approximately \$2.0 million, which reduced recorded purchased water costs. There were no such refunds received during 1996.

Costs of power purchased for pumping decreased by 2.0% to \$7.6 million in 1997, chiefly as the result of the reduced amounts of water produced from pumped sources in SCW's resource mix. During 1997, SCW had several wells out of service due to water quality issues which significantly affected its ability to fully utilize its groundwater resources.

Costs of power purchased for resale in 1997 decreased by 10.9% to \$5.2 million from the \$5.8 million recorded in 1996 due to reduced costs from SCW's energy provider which partially offset the effects of increased kilowatt-hour sales volumes recorded during the year.

Groundwater production assessments increased 15.2% to \$6.8 million in 1997 from \$5.9 million in 1996 due to additional assessments associated with increased pumping in SCW's San Gabriel Valley and San Dimas customer service areas.

A positive entry for the provision for supply cost balancing accounts reflects recovery of previously under-collected supply costs. Conversely, a negative entry for the provision for supply cost balancing accounts reflects an under-collection of previously incurred supply costs. The positive entry for 1997 is a result of approval by the CPUC of rate increases sufficient to recover previously under-collected purchased supply costs, as well as refunds received during 1997 from wholesale suppliers. The balancing account mechanism insulates earnings from changes in the unit costs of supply costs which are outside of the immediate control of SCW. However, the balancing account is not designed to insulate earnings against changes in supply mix, as occurred during the first eight months of 1997.

Administrative and general expenses increased by 7.7% to \$22.1 million in 1997 from the \$20.5 million recorded in 1996. This increase reflects higher labor costs. In addition, during 1997 SCW incurred costs for consulting on water quality litigation for which there was no corresponding amount in 1996.

In 1997, maintenance expense decreased by 5.7% to \$7.3 million from \$7.7 million recorded in 1996 due principally to increased emphasis being placed on SCW's meter replacement and capital improvement program which partially offset increased maintenance on SCW's water supply sources.

Depreciation expense in 1997 increased by 8.4% to \$11.0 million reflecting the effects of recording approximately \$31.0 million in net plant additions during 1996, depreciation on which began in 1997.

Taxes on income decreased by approximately 4.4% to \$9.8 million in 1997 as compared to the \$10.3 million in 1996 as a result of lower pre-tax income. Other taxes increased by 3.0% in 1997 to \$6.3 million due primarily to increased property taxes resulting from higher valuation assessments in 1997.

Other income increased by 42.7% in 1997 due principally to an increase in billings to the City of Folsom for the lease of a portion of SCW's water rights in the American River.

Interest expense decreased by 3.3% to \$10.2 million primarily due to reduced short-term bank borrowing and the lower borrowing rates experienced during 1997.

LIQUIDITY AND CAPITAL RESOURCES

AWR funds its operating expenses, dividends on its outstanding Common and Preferred Shares and makes its mandatory sinking fund payments principally through dividends from SCW. AWR has filed a Registration Statement with the Securities and Exchange Commission (SEC) for issuance, from time to time, of up to \$60 million in Common Shares, Preferred Shares and/or debt securities. The proceeds will be used primarily for investment in its subsidiaries.

SCW funds the majority of its operating expenses, interest payments on its debt and dividends on its outstanding Common Shares through internal sources. SCW continues to rely on external sources, including short-term bank borrowing, contributions-in-aid-of-construction, advances for construction and install-and-convey advances, to fund the majority of its construction expenditures.

Because of the seasonal nature of its water and electric operations, SCW utilizes its short-term borrowing capacity to finance current operating expenses. The aggregate short-term borrowing capacity available to SCW under its three bank lines of credit was \$47 million as of December 31, 1998 of which a total of \$38 million was outstanding. SCW routinely employs short-term bank borrowing as an interim financing source prior to executing either a long-term debt or equity issue. SCW issued long-term debt totaling \$15.0 million in March 1998. The funds were used initially to repay short-term bank borrowings, after which construction expenditures were funded.

SCW has filed a Registration Statement with the SEC for issuance, from time to time, of up to \$60 million in long-term debt with the net proceeds being used to repay short-term bank borrowings and fund construction needs. In January 1999, SCW issued \$40 million of long-term debt pursuant to this Registration Statement, all of which was used to reduce bank borrowing.

The Company has no derivative financial instruments, financial instruments with significant off-balance sheet risks or financial instruments with concentrations of credit risk.

CONSTRUCTION PROGRAM

SCW's construction program is designed to ensure its customers high quality service. A program for water pipeline replacement is on-going throughout the 22 customer service areas, based on priority of leaks detected, fire protection enhancements and reflection of the underlying replacement schedule. In addition, general upgrades in SCW's water supply facilities are anticipated to be on-going. SCW's Board of Directors has approved anticipated net capital expenditures of \$42.1 million in 1999. Neither AWR nor ASUS have material capital requirements.

REGULATORY MATTERS

SCW is subject to regulation by the CPUC, which has broad powers with respect to service and facilities, rates, classifications of accounts, valuation of properties, the purchase, disposition and mortgaging of properties necessary or useful in rendering public utility service, the issuance of securities, the granting of certificates of convenience and necessity as to the extension of services and facilities and various other matters. AWR and ASUS are not regulated by the CPUC.

The 22 customer service areas of SCW are grouped into 16 water districts and one electric district for ratemaking purposes. Water rates vary among the 16 ratemaking districts due to differences in operating conditions and costs. SCW monitors operations on a regional basis in each of these districts so that applications for rate changes may be filed, when warranted. Under the CPUC's practices, rates may be increased by three methods: general rate case increases (GRC's), offsets for certain expense increases and advice letter filings related to certain plant additions. GRC's are typically for three-year periods, which include step increases for the second and third year. Rates are based on forecasted expenses and capital costs. GRC's have a typical regulatory lag of one year. Offset rate increases typically have a two to four month regulatory lag.

New water rates were implemented in three of SCW's customer service areas in January 1, 1998 to recover costs associated with capital projects in those areas. Step increases in rates were effective in April 1998 in Barstow and in May 1998 in Santa Maria. Increased rates for six additional water ratemaking districts and recovery of costs associated with SCW's general office functions were effective January 1, 1999.

Applications to increase water rates were filed for four water ratemaking districts in February 1999. The new rates, if authorized in total or in part by the CPUC, would be effective January 1, 2000.

SCW has filed an application with the CPUC to combine tariff schedules into regional rates over a six year phase-in plan for the customer service areas that make up SCW's Region III. A final decision from the CPUC is anticipated by the fourth quarter of 1999.

Hearings were held before the CPUC in November 1998 on SCW's filing seeking recovery through rates of \$1.8 million in costs associated with its participation in the coastal aqueduct extension of the State Water Project. SCW is continuing to pursue alternative forms of recovery of its investment in the Project, which will require CPUC approval. A final order from the CPUC is anticipated in 1999. See Note 8 to the Notes to Financial Statements.

In March 1998, the CPUC issued an Order Instituting Investigation (OII) to regulated water utilities in the state of California, including SCW. The purpose of the OII is to determine whether existing standards and policies regarding drinking water quality adequately protect the public health and whether those standards and policies are being uniformly complied with by those water utilities. The OII delineates the constitutional and statutory jurisdiction of the CPUC and the DOHS in establishing and enforcing adherence to water quality standards. The CPUC's jurisdiction provides for the establishment of rates which permit water utilities to furnish safe water meeting the established water quality standards at prices

which are both affordable and allow the utility to earn a reasonable return on its investment. SCW has provided its response to a series of questions dealing with the adequacy of current drinking water standards, compliance by water utilities with such standards, appropriate remedies for failure to comply with safe drinking water standards and whether increased enforcement and additional drinking water standards are necessary. SCW anticipates a final decision by the CPUC on this matter in 1999. See Note 8 to the Notes to Financial Statements. See Note 8 to the Notes to Financial Statements.

ENVIRONMENTAL MATTERS

The 1996 amendments to the Safe Drinking Water Act (SDWA) revised the 1986 amendments to the SDWA with a new process for selecting and regulating contaminants. The Environmental Protection Agency (EPA) can only regulate contaminants that may have adverse health effects, are known or likely to occur at levels of public health concern, and if regulated the regulation would provide "a meaningful opportunity for health risk reduction." The EPA has published a list of contaminants for possible regulation and must update that list every five years. In addition, every five years, the EPA must select at least five contaminants on that list and determine whether to regulate them. The new law allows the EPA to bypass the selection process and adopt interim regulations for contaminants in order to address urgent health threats. Current regulations, however, remain in place and are not subject to the new standard-setting provisions. The California Department of Health Services, acting on behalf of the EPA, administers the EPA's program in California.

The 1996 SDWA amendments allow the EPA, for the first time, to base primary drinking water regulations on risk assessment and cost/benefit considerations and on minimizing overall risk. The EPA must base regulations on the best available, peer-reviewed science and data from best available methods. For proposed regulations that involve the setting of maximum contaminant levels (MCL's), the EPA must use, and seek public comment on, an analysis of quantifiable and non-quantifiable risk-reduction benefits and cost for each such MCL.

SCW currently tests its wells and water systems for more than 90 contaminants, currently covering all contaminants listed in the SDWA, except for those from which SCW has received an exemption. Water from wells found to contain levels of contaminants above or near the established MCL's is treated before it is delivered to customers.

Since the SDWA became effective, SCW has experienced increased operating costs for testing to determine the levels, if any, of the constituents in SCW's sources of supply and additional expense to lower the level of any such contaminants in order to meet the MCL standards. Such costs and the costs of controlling any other contaminants may cause SCW to experience additional capital costs as well as increased operating costs. The ratemaking process provides SCW with the opportunity to recover prudently incurred capital and operating costs associated with water quality.

There have been no environmental matters that have materially affected or are currently materially affecting the Company's Bear Valley Electric customer service area. The construction of a proposed 115kv line to serve the Bear Valley Electric customer service area is subject to an Environmental Impact Statement (EIS). Delays in approval of the EIS could impact SCW's ability to meet electric load growth in the future until the project is completed.

WATER SUPPLY

During 1998, the Company supplied a total of 179,927 acre feet of water. Of this amount, approximately 61% came from pumped sources and 39% was purchased from others, principally the Metropolitan Water District of Southern California (MWD). The remaining amount was supplied by the Bureau of Reclamation (the "Bureau") under a no-cost contract. During 1997, the Company produced 199,146 acre feet of water, 54% of which came from pumped sources, 45% was purchased and the remainder was supplied by the Bureau.

The MWD is a water district organized under the laws of the State of California for the purpose of delivering imported water to areas within its jurisdiction. The Company has 52 connections for the water distribution facilities of MWD and other municipal water agencies. MWD imports water from two principal sources: the Colorado River and the State Water Project (SWP). Available water supplies from the Colorado River and the SWP have historically been sufficient to meet most of MWD's requirements and MWD's supplies from these

sources are anticipated to remain adequate through 1999. However, MWD has taken a number of steps to secure additional storage capacity and increase available water supplies, including effecting transfers of water rights from other sources.

The 1997-1998 water year, which ended September 1998, was labeled a "wet one" by the California Department of Water Resources. The outlook for water supply in 1999 remains favorable. In those customer services areas of SCW which pump groundwater, overall groundwater conditions remain at adequate levels. However, certain of SCW's groundwater supplies have been affected to varying degrees by various forms of contamination which, in some cases, has caused increased reliance on purchased water in its resource mix.

WATER-RELATED OPPORTUNITIES

SCW anticipates terminating its Golden State Water Company joint venture in 1999. In its place, American States Utility Services Inc. was formed to pursue opportunities such as long-term leases, and operation and maintenance contracts of government or municipally owned water and wastewater systems.

YEAR 2000 READINESS

The Company has been actively assessing its Year 2000 (Y2K) readiness since early 1997 and has inventoried its significant computer hardware and software programs. All major upgrades to these systems have been completed and were operational at year-end 1998. In addition to work being done on internal systems, the Company has sought compliance certification from external vendors and service providers. The Company has initiated due diligence with those external vendors upon which the Company is significantly dependent, such as energy and telecommunication companies and wholesale water suppliers. In the event that such suppliers might be adversely affected by Y2K, the Company has prepared a contingency plan, which is anticipated to be completed by the second quarter of 1999. See Note 13 of the Notes to Financial Statements for more information.

To date, there have been no significant costs associated with Y2K readiness that have not been approved by the CPUC for recovery through rates. The Company believes that future costs associated with Y2K, which are prudently incurred, will be allowed for recovery through rates.

ACCOUNTING STANDARDS

In February 1997, the Financial Accounting Standards Board (FASB) issued SFAS No. 130, "Reporting Comprehensive Income," which establishes standards for the reporting and displaying of comprehensive income and its components, such as minimum pension liability, in a full set of general-purpose financial statements. Adoption of this statement, effective for fiscal years beginning after December 15, 1997, did not have a significant impact on the Company's financial statements.

In June 1997, the FASB issued SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," which establishes standards for the method of reporting information about operating segments in annual financial statements and in interim reports issued to shareholders. Adoption of this statement, effective for fiscal years beginning after December 15, 1997, did not have a significant impact on disclosure of segment related information.

In February 1998, the FASB issued SFAS No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits," which amends SFAS No. 87 and SFAS No. 109 and revises employers' disclosure concerning pension and other postretirement benefits plans. Adoption of this statement, effective for fiscal years beginning after December 15, 1997, did not have a significant impact the Company's financial statements.

In June 1998, the FASB issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," which establishes a new model for accounting for derivative and hedging activities, and supersedes and amends a number of existing standards. Adoption of this statement, effective for fiscal years beginning after June 15, 1999, will not have a significant impact on financial position or results of operation.

Balance Sheets

| (dollars in thousands) | For the years ended December 31, | |
|---|----------------------------------|------------|
| | 1998 | 1997 |
| | ----- | ----- |
| Assets | | |
| Utility Plant, at cost | | |
| Water | \$ 482,989 | \$ 446,605 |
| Electric | 35,171 | 34,137 |
| | ----- | ----- |
| | 518,160 | 480,742 |
| Less - Accumulated depreciation | (138,423) | (125,020) |
| | ----- | ----- |
| | 379,737 | 355,722 |
| Construction work in progress | 35,016 | 27,901 |
| | ----- | ----- |
| Net utility plant | 414,753 | 383,623 |
| | ----- | ----- |
| Other Property and Investments | 1,077 | 1,355 |
| | ----- | ----- |
| Current Assets | | |
| Cash and cash equivalents | 620 | 4,186 |
| Accounts receivable-Customers, less reserves of \$403 in 1998; \$466 in 1997 | 7,626 | 8,544 |
| Other | 5,301 | 3,614 |
| Unbilled revenue | 9,303 | 9,106 |
| Materials and supplies, at average cost | 994 | 1,299 |
| Supply cost balancing accounts | 4,300 | 4,286 |
| Prepayments | 5,988 | 7,676 |
| Accumulated deferred income taxes - net | 5,156 | 5,783 |
| | ----- | ----- |
| Total current assets | 39,288 | 44,494 |
| | ----- | ----- |
| Deferred Charges | | |
| Regulatory tax-related assets | 21,506 | 22,337 |
| Other | 8,047 | 5,265 |
| | ----- | ----- |
| Total deferred charges | 29,553 | 27,602 |
| | ----- | ----- |
| Total Assets | \$ 484,671 | \$ 457,074 |
| | ===== | ===== |
| Capitalization and Liabilities | | |
| Capitalization | | |
| Common shareholders' equity | \$ 154,299 | \$ 151,053 |
| Preferred shares | 1,600 | 1,600 |
| Preferred shares - mandatory redemption | 400 | 440 |
| Long-term debt | 120,809 | 115,286 |
| | ----- | ----- |
| Total capitalization | 277,108 | 268,379 |
| | ----- | ----- |
| Current Liabilities | | |
| Notes payable to banks | 38,000 | 26,000 |
| Long-term debt and preferred shares - current | 260 | 231 |
| Accounts payable | 10,218 | 11,770 |
| Taxes payable | 5,900 | 9,115 |
| Accrued interest | 1,405 | 1,868 |
| Other | 7,985 | 7,196 |
| | ----- | ----- |
| Total current liabilities | 63,768 | 56,180 |
| | ----- | ----- |
| Other Credits | | |
| Advances for construction | 54,743 | 55,574 |
| Contributions in aid of construction | 36,530 | 28,467 |
| Accumulated deferred income taxes - net | 46,902 | 42,984 |
| Unamortized investment tax credits | 3,155 | 3,246 |
| Regulatory tax-related liability | 1,906 | 1,950 |
| Other | 559 | 294 |
| | ----- | ----- |
| Total other credits | 143,795 | 132,515 |
| | ----- | ----- |
| Total Capitalization and Liabilities | \$ 484,671 | \$ 457,074 |
| | ===== | ===== |

The accompanying notes are an integral part of these financial statements

Statements Of Capitalization

| (dollars in thousands) | For the years ended December 31, | |
|---|----------------------------------|------------|
| | 1998 | 1997 |
| | ----- | ----- |
| Common Shareholders' Equity: | | |
| Common shares, \$2.50 stated value-- | | |
| Authorized 30,000,000 shares | | |
| Outstanding 8,957,671 in 1998 and 1997 | \$ 22,394 | \$ 22,394 |
| Additional paid-in capital | 74,937 | 74,937 |
| Earnings reinvested in the business | 56,968 | 53,722 |
| | ----- | ----- |
| | 154,299 | 151,053 |
| | ----- | ----- |
| Preferred Shares: \$25 par value | | |
| Authorized 64,000 shares | | |
| Outstanding 32,000 shares, 4% Series | 800 | 800 |
| Outstanding 32,000 shares, 4 1/4 % Series | 800 | 800 |
| | ----- | ----- |
| | 1,600 | 1,600 |
| | ----- | ----- |
| Preferred Shares Subject to Mandatory Redemption | | |
| Requirements: \$25 par value | | |
| Authorized and outstanding 17,600 shares in 1998 and | 440 | 480 |
| 19,200 shares in 1997, 5% Series | | |
| Less: Preferred shares to be redeemed within one year | (40) | (40) |
| | ----- | ----- |
| | 400 | 440 |
| | ----- | ----- |
| Long-Term Debt | | |
| 5.82% notes due 2003 | 12,500 | 12,500 |
| 10.10% notes due 2009 | -- | 10,000 |
| 6.64% notes due 2013 | 1,100 | 1,100 |
| 6.80% notes due 2013 | 2,000 | 2,000 |
| 8.50% fixed rate obligation due 2013 | 1,882 | 1,947 |
| Variable rate obligation due 2014 | 6,000 | 6,000 |
| Variable rate obligation due 2018 | 630 | -- |
| 6.87% notes due 2023 | 5,000 | 5,000 |
| 7.00% notes due 2023 | 10,000 | 10,000 |
| 7.55% notes due 2025 | 8,000 | 8,000 |
| 7.65% notes due 2025 | 22,000 | 22,000 |
| 5.50% notes due 2026 | 8,000 | 8,000 |
| 6.81% notes due 2028 | 15,000 | -- |
| 9.56% notes due 2031 | 28,000 | 28,000 |
| Other | 917 | 930 |
| | ----- | ----- |
| | 121,029 | 115,477 |
| Less: Current maturities | (220) | (191) |
| | ----- | ----- |
| | 120,809 | 115,286 |
| | ===== | ===== |
| Total Capitalization | \$ 277,108 | \$ 268,379 |
| | ===== | ===== |

The accompanying notes are an integral part of these financial statements

Statements Of Income

| (dollars in thousands, except per share amounts) | For the years ended December 31, | | |
|--|----------------------------------|------------|------------|
| | 1998 | 1997 | 1996 |
| | ----- | ----- | ----- |
| Operating Revenues | | | |
| Water | \$ 134,859 | \$ 140,988 | \$ 139,997 |
| Electric | 13,201 | 12,767 | 11,532 |
| | ----- | ----- | ----- |
| Total operating revenues | 148,060 | 153,755 | 151,529 |
| | ----- | ----- | ----- |
| Operating Expenses | | | |
| Water purchased | 30,833 | 38,318 | 38,355 |
| Power purchased for resale | 5,013 | 5,188 | 5,825 |
| Power purchased for pumping | 7,009 | 7,554 | 7,711 |
| Groundwater production assessment | 7,567 | 6,847 | 5,946 |
| Supply cost balancing accounts | 28 | 2,813 | 2,064 |
| Other operating expenses | 14,459 | 13,074 | 13,421 |
| Administrative and general expenses | 21,987 | 22,138 | 20,549 |
| Depreciation | 12,538 | 10,952 | 10,102 |
| Maintenance | 7,311 | 7,301 | 7,745 |
| Taxes on income | 10,130 | 9,830 | 10,283 |
| Property and other taxes | 6,124 | 6,282 | 6,099 |
| | ----- | ----- | ----- |
| Total operating expenses | 122,999 | 130,297 | 128,100 |
| | ----- | ----- | ----- |
| Operating Income | 25,061 | 23,458 | 23,429 |
| | ----- | ----- | ----- |
| Other Income | | | |
| Total other income - net | 769 | 758 | 531 |
| | ----- | ----- | ----- |
| Income before interest charges | 25,830 | 24,216 | 23,960 |
| | ----- | ----- | ----- |
| Interest Charges | | | |
| Interest on long-term debt | 9,612 | 8,821 | 8,551 |
| Other interest and amortization of debt expense | 1,595 | 1,336 | 1,949 |
| | ----- | ----- | ----- |
| Total interest charges | 11,207 | 10,157 | 10,500 |
| | ----- | ----- | ----- |
| Net Income | 14,623 | 14,059 | 13,460 |
| Dividends on Preferred Shares | (90) | (92) | (94) |
| Earnings Available For Common Shareholders | \$ 14,533 | \$ 13,967 | \$ 13,366 |
| Basic Earnings Per Common Share | \$ 1.62 | \$ 1.56 | \$ 1.69 |
| Weighted Average Number of Common Shares Outstanding | 8,958 | 8,957 | 7,891 |

The accompanying notes are an integral part of these financial statements

Statements Of Changes In Common Shareholders' Equity

| (dollars in thousands) | Common Number of Shares | Shares Amount | Additional Paid-in Capital | Earnings Reinvested in the Business |
|--|-------------------------------|------------------|----------------------------------|--|
| | ----- | ----- | ----- | ----- |
| Balances at December 31, 1995 | 7,845 | \$19,613 | \$54,753 | \$47,210 |
| Add: | | | | |
| Net Income | | | | 13,460 |
| Issuance of Common Shares for public offering | 1,000 | 2,500 | 18,090 | |
| under Dividend Reinvestment and 401(k) | 41 | 102 | 802 | |
| Plans | | | | |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 94 |
| Dividends on Common Shares - \$1.225 per share | | | | 9,670 |
| | ----- | ----- | ----- | ----- |
| Balances at December 31, 1996 | 8,886 | \$22,215 | \$73,645 | \$50,906 |
| Add: | | | | |
| Net Income | | | | 14,059 |
| Issuance of Common Shares for public offering | 72 | 179 | 1,292 | |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 92 |
| Dividends on Common Shares - \$1.245 per share | | | | 11,151 |
| | ----- | ----- | ----- | ----- |
| Balances at December 31, 1997 | 8,958 | \$22,394 | \$74,937 | \$53,722 |
| Add: | | | | |
| Net Income | | | | 14,623 |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 90 |
| Dividends on Common Shares - \$1.26 per share | | | | 11,287 |
| | ----- | ----- | ----- | ----- |
| Balances at December 31, 1998 | 8,958 | \$22,394 | \$74,937 | \$56,968 |
| | ===== | ===== | ===== | ===== |

The accompanying notes are an integral part of these financial statements

Statements Of Cash Flows

| (dollars in thousands) | For the years ended December 31, | | |
|---|----------------------------------|-----------|-----------|
| | 1998 | 1997 | 1996 |
| | ----- | ----- | ----- |
| Cash Flows From Operating Activities: | | | |
| Net income | 14,623 | \$ 14,059 | \$ 13,460 |
| Adjustments for non-cash items: | | | |
| Depreciation and amortization | 12,929 | 11,387 | 10,389 |
| Deferred income taxes and investment tax credits | 5,241 | 826 | 577 |
| Other - net | 2,036 | (1,426) | (1,660) |
| Changes in assets and liabilities: | | | |
| Customer receivables | 918 | (673) | 368 |
| Supply cost balancing accounts | (14) | 1,987 | 1,800 |
| Accounts payable | (1,552) | (1,095) | 6,026 |
| Taxes payable | (3,215) | 3,338 | 215 |
| Other - net | 438 | 341 | 122 |
| | ----- | ----- | ----- |
| Net cash provided | 31,404 | 28,744 | 31,297 |
| | ----- | ----- | ----- |
| Cash Flows from Investing Activities: | | | |
| Construction expenditures | (41,826) | (34,717) | (31,953) |
| | ----- | ----- | ----- |
| Net cash used | (41,826) | (34,717) | (31,953) |
| | ----- | ----- | ----- |
| Cash Flows from Financing Activities: | | | |
| Issuance of Common Shares | -- | 1,472 | 21,494 |
| Issuance of long-term debt and lease obligations | 15,000 | 8,000 | -- |
| Receipt of advances for and contributions in aid of construction | 3,381 | 1,302 | 2,462 |
| Refunds on advances for construction | (2,651) | (2,957) | (2,088) |
| Retirement or repayments of long-term debt and redemption of preferred shares - net | (9,488) | (198) | (15,447) |
| Net change in notes payable to banks | 12,000 | 10,000 | 7,500 |
| Common and preferred dividends paid | (11,386) | (11,243) | (9,825) |
| | ----- | ----- | ----- |
| Net cash provided | 6,856 | 6,376 | 4,096 |
| | ----- | ----- | ----- |
| Net Increase (Decrease) in Cash and Cash Equivalents | (3,566) | 403 | 3,440 |
| Cash and Cash Equivalents, Beginning of Year | 4,186 | 3,783 | 343 |
| | ----- | ----- | ----- |
| Cash and Cash Equivalents, End of Year | 620 | 4,186 | \$ 3,783 |
| | ----- | ----- | ----- |
| Taxes and Interest Paid: | | | |
| Income taxes paid | \$ 5,430 | \$ 6,338 | \$ 10,767 |
| Interest paid | \$ 11,391 | 9,451 | 10,128 |
| | ----- | ----- | ----- |
| Non-Cash Transactions: | | | |
| Property installed by developers and conveyed to Company | \$ 1,797 | \$ 2,082 | \$ 957 |
| | ===== | ===== | ===== |

NOTES TO FINANCIAL STATEMENTS

In April 1998, shareholders of Southern California Water Company (SCW) voted to approve formation of a holding company. The formation process was completed on July 1, 1998 at which time American States Water Company (AWR) became the parent company. As a result of the holding company formation, SCW became one of AWR's two operating subsidiaries. SCW will continue to be a public utility engaged principally in the purchase, production, distribution and sale of water and also the distributor of electricity in several mountain communities. SCW is regulated by the California Public Utilities Commission (CPUC) as to its water and electric business including properties, rates, services, facilities and other matters. The other subsidiary, American States Utility Services, Inc. (ASUS) is a new company which will perform non-regulated, water related services and operations. The consolidated financial statements include the accounts of SCW which comprise virtually all of AWR's assets and revenues.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements include the accounts of American States Water Company and its wholly-owned subsidiaries, Southern California Water Company and American States Utility Services, Inc., collectively referred to as the Company. Inter-company transactions and balances have been eliminated.

The accounting records for SCW are maintained in accordance with the Uniform System of Accounts prescribed by the California Public Utilities Commission. The preparation of these financial statements required the use of certain estimates by management in determining the company's assets, liabilities, revenues and expenses.

Property and Depreciation - The Company capitalizes as utility plant the cost of additions and replacements of retirement units. Such cost includes labor, material and certain indirect charges. Depreciation is computed on the straight-line, remaining-life basis. For the years 1998, 1997 and 1996, the aggregate provisions for depreciation approximated 2.79%, 2.77% and 2.71% of beginning of the year depreciable plant, respectively.

Interest - Interest is generally not capitalized for financial reporting purposes as such procedure is usually not followed for rate-making purposes.

Revenues - Revenues include amounts billed to customers and an amount of unbilled revenue representing amounts to be billed for usage from the last meter reading date to the end of the accounting period.

Basic Earnings Per Common Share - Basic Earnings per Common Share are based upon the weighted average number of Common Shares outstanding and net income after deducting preferred dividend requirements. There are no dilutive securities. Accordingly, diluted earnings per share is not calculated.

Supply Cost Balancing Accounts - As permitted by the CPUC, the Company maintains water and electric supply cost balancing accounts to account for under-collections and over-collections of revenues designed to recover such costs. Recoverability of such costs is recorded in income and charged to balancing accounts when such costs are incurred. The balancing accounts are reversed when such costs are recovered through rate adjustments. The Company accrues interest on its supply cost balancing accounts at the rate prevailing for 90-day commercial paper.

Debt Issue Expense and Redemption Premiums - Original debt issue expenses are amortized over the lives of the respective issues. Premiums paid on the early redemption of debt which is reacquired through refunding are deferred and amortized over the life of the debt issued to finance the refunding. The redemption premium on debt reacquired without refunding is amortized over the remaining period the debt would have been outstanding.

Other Credits - Advances for construction represent amounts advanced by developers which are generally refundable at either a rate of 22% of the revenue received from the installations for which funds were advanced or in equal annual installments over a 40-year period. Contributions in aid of construction are similar to advances, but require no refunding and are amortized over the useful lives of the related property.

Cash and Cash Equivalents - For purposes of the Statements of Cash Flows, cash and cash equivalents include short-term cash investments with an original maturity of three months or less.

Financial Instrument Risk - The Company does not carry any financial instruments with off-balance sheet risk nor does its operations result in concentrations of credit risk.

Fair Value of Financial Instruments - The table below estimates the fair value of each represented class of financial instrument. For cash and cash equivalents, accounts receivable and short-term debt, the carrying amount is used. Otherwise, rates available to the Company at December 31, 1998 and 1997 for debt with similar terms and remaining maturities were used to estimate fair value for long-term debt. Changes in the assumptions will produce differing results.

| (dollars in thousands) | 1998 | | 1997 | |
|------------------------|-----------------|------------|-----------------|------------|
| | Carrying amount | Fair value | Carrying amount | Fair value |
| Financial assets: | | | | |
| Cash | \$ 620 | \$ 620 | \$ 4,186 | \$ 4,186 |
| Accounts receivable | 22,230 | 22,230 | 21,264 | 21,264 |
| Financial liabilities: | | | | |
| Short-term debt | 38,000 | 38,000 | 26,000 | 26,000 |
| Long-term debt | 120,809 | 135,092 | 115,326 | 126,930 |

NOTE 2 - CAPITAL STOCK

All of the series of Preferred Shares outstanding at December 31, 1998 are redeemable at the option of the Company. At December 31, 1998, the redemption price per share for each series of \$25 Preferred Shares was \$27.00, \$26.50 and \$25.25 for the 4%, 4 1/4% and 5% Series, respectively. To each of the redemption prices must be added accrued and unpaid dividends to the redemption date.

The \$25 Preferred Shares, 5% Series, are subject to mandatory redemption provisions of 1,600 shares per year. The annual aggregate mandatory redemption requirements for this Series for the five years subsequent to December 31, 1998 is \$40,000 each year.

In 1996, the Company issued 1,000,000 Common Shares through a secondary public offering. In January 1997, the Company issued 71,500 Common Shares through a secondary public offering. The net proceeds from this sale were used to repay a portion of short-term debt then outstanding.

For the years ended December 31, 1998 and December 31, 1997, all shares issued under the Company's Common Share Purchase and Dividend Reinvestment Plan (DRP) and the 401(k) Plan were purchased on the open market. For the year ended December 31, 1996, the Company issued 20,228 and 20,851 Common Shares, respectively, under the DRP and the 401(k) programs. There are 89,226 and 71,408 Common Shares reserved for issuance under the DRP and the 401(k) Plan, respectively, at December 31, 1998. Shares reserved for the 401(k) Plan are in relation to Company matching contributions and for investment purposes by participants.

As of December 31, 1998 there were no retained earnings restricted as to the payment of cash dividends on Common Shares.

In August 1998, the Board of Directors adopted a Shareholder Rights Plan (Rights Plan) and authorized a dividend distribution of one right (a Right) to purchase 1/1000th share of Junior Participating Preferred Stock for each outstanding share of Common Stock. The Rights became effective in September 1998 and will expire in September 2008. The Rights Plan is designed to provide shareholders' protection and to maximize shareholder value by encouraging a prospective acquirer to negotiate with the Board.

Each Right represents a right to purchase 1/1000th of Junior Participating Preferred Stock at the price of \$120, subject to adjustment (the Purchase Price). Each share of Junior Participating Preferred Stock is entitled to receive a dividend equal to 1000 times any dividend paid on common stock and 100 votes per share in any shareholder election. The Rights become exercisable upon occurrence of a Distribution Date. A Distribution Date event occurs if (i) any person accumulates 15% of the then outstanding Common stock, (ii) any person presents a tender offer which caused the person's ownership level to exceed 15% and the Board determines the tender offer not to be fair to AWR's shareholders, or (iii) the Board determines that a shareholder maintaining a 15% interest in the Common stock could have an adverse impact on AWR or could attempt to pressure AWR to repurchase the holder's shares at a premium.

Until the occurrence of a Distribution Date, each Right trades with the Common Stock and is not separately transferable. When a Distribution Date occurs, AWR would distribute separately Rights Certificates to Common Shareholders and the Rights would subsequently trade separate from the Common Stock and each holder of a Right, other than the acquiring person whose Rights will thereafter be void, will have the right to receive upon exercise at its then current Purchase Price that number of shares of Common Stock having a market value of two times the Purchase Price of the Right. If AWR merges into the acquiring person or enters into any transaction that unfairly favors the acquiring person or disfavors AWR's other shareholders, the Right becomes a right to purchase Common Stock of the acquiring person having market value of two times the Purchase Price.

The Board of Directors may determine that in certain circumstances a proposal which would cause a Distribution Date is in the best interest of AWR's shareholders. Therefore, the Board of Directors may, at its option, redeem the Rights at a redemption price of \$0.01 per Right.

NOTE 3 - COMPENSATING BALANCES AND BANK DEBT

At December 31, 1998, SCW maintained \$47.0 million in aggregate borrowing capacity with three commercial banks with no compensating balances required. Of this amount, \$38.0 million was outstanding at year-end. Loans can be obtained at the option of SCW and bear interest at rates based on floating prime borrowing rates or at money market rates.

Short-term borrowing activities for the last three years were as follows:

| (dollars in thousands, except percent) | December 31, | | |
|--|--------------|----------|----------|
| | 1998 | 1997 | 1996 |
| Balance Outstanding at December 31, | \$38,000 | \$26,000 | \$16,000 |
| Interest Rate at December 31, | 5.86% | 6.39% | 6.17% |
| Average Amount Outstanding | 19,309 | \$15,678 | \$26,109 |
| Weighted Average Annual Interest Rate | 6.78% | 6.27% | 5.97% |
| Maximum Amount Outstanding | \$39,000 | \$32,000 | \$36,000 |

NOTE 4 - LONG TERM DEBT

In December 1996, SCW sold \$8 million in tax-exempt debt that was issued through the California Pollution Control Financing Authority. The funds were deposited with a trustee and were used during 1997 to finance water main replacements.

In March 1998, SCW sold the remaining \$15 million under its Series B Medium Term Note Program and in December 1998, SCW redeemed all of its outstanding 10.10% Notes. In January 1999, \$40 million of Series C Medium Term Notes were sold. The funds were used initially to repay short-term bank borrowings and, after that, fund construction expenditures. The Company has no mortgage debt, and leases and other similar financial arrangements are not material.

SCW has posted an Irrevocable Letter of Credit, which expires July 31, 1999, in the amount of \$797,979 as security for its self-insured workers' compensation plan. SCW has also provided an Irrevocable Letter of Credit in the amount of \$6,296,000 to a trustee with respect to the variable rate obligation issued by the Three Valleys Municipal Water District.

Annual maturities of all long-term debt, including capitalized leases, amount to \$220,139, \$227,277, \$236,167, \$230,383 and \$199,841 for the 5 years ending December 31, 1999 through 2003, respectively.

NOTE 5 - TAXES ON INCOME

The Company provides deferred income taxes for temporary differences under Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" (SFAS No. 109) for certain transactions which are recognized for income tax purposes in a period different from that in which they are reported in the financial statements. The most significant items are the tax effects of accelerated depreciation, the supply cost balancing accounts and advances for and contributions in aid of construction. SFAS No. 109 also requires that rate-regulated enterprises record deferred income taxes for temporary differences accorded flow-through treatment at the direction of a regulatory commission. The resulting deferred tax assets and liabilities are recorded at the expected cash flow to be reflected in future rates. Since the CPUC has consistently permitted the recovery of pre-

viously flowed-through tax effects, SCW has established regulatory liabilities and assets offsetting such deferred tax assets and liabilities.

Deferred investment tax credits are being amortized to other income ratably over the lives of the property giving rise to the credits.

The significant components of deferred tax assets and deferred tax liabilities, as reflected in the balance sheets, and the accumulated net deferred income tax liabilities at December 31, 1998 and 1997 were:

| (dollars in thousands) | December 31, | |
|---|--------------|-------------|
| | 1998 | 1997 |
| Deferred tax assets: | | |
| Balancing accounts | \$ 33 | \$ 27 |
| State tax effect | 5,123 | 5,756 |
| | ----- | ----- |
| | 5,156 | 5,783 |
| | ----- | ----- |
| Deferred tax liabilities | | |
| Depreciation | (43,442) | (40,822) |
| Advances and contributions | 16,694 | 17,005 |
| Other property related | (11,488) | (9,602) |
| Other non-property related | (8,666) | (9,565) |
| | ----- | ----- |
| | (46,902) | (42,984) |
| | ----- | ----- |
| Accumulated deferred income taxes - net | \$ (41,746) | \$ (37,201) |
| | ----- | ----- |

The current and deferred components of income tax expense are as follows:

| (dollars in thousands) | December 31, | | |
|--|--------------|-----------|-----------|
| | 1998 | 1997 | 1996 |
| Current | | | |
| Federal | \$ 5,219 | \$ 7,205 | \$ 7,224 |
| State | 1,727 | 2,287 | 2,452 |
| | ----- | ----- | ----- |
| Total current tax expense | 6,946 | 9,492 | 9,676 |
| | ----- | ----- | ----- |
| Deferred - Federal and State: | | | |
| Accelerated depreciation | 3,319 | 2,996 | 3,175 |
| Balancing accounts | 6 | (871) | (798) |
| State Water Project | -- | -- | 296 |
| Advances and contributions | -- | (210) | (894) |
| California privilege year franchise tax | (544) | (617) | (683) |
| Adjustments to prior year provision | -- | -- | 410 |
| Other | (398) | (566) | (732) |
| | ----- | ----- | ----- |
| Total deferred tax expense | 2,383 | 732 | 774 |
| | ----- | ----- | ----- |
| Total income tax expense | \$ 9,329 | \$ 10,224 | \$ 10,450 |
| | ----- | ----- | ----- |
| Income taxes included in operating expenses | \$ 10,130 | \$ 9,830 | \$ 10,283 |
| Income taxes included in other income and expenses - net | (801) | 394 | 167 |
| | ----- | ----- | ----- |
| Total income tax expense | \$ 9,329 | \$ 10,224 | \$ 10,450 |
| | ----- | ----- | ----- |

Additional information regarding taxes on income is set forth in the following table:

| (dollars in thousands, except percent) | December 31, | | |
|--|--------------|-----------|-----------|
| | 1998 | 1997 | 1996 |
| Federal taxes on pre-tax income at statutory rates | \$ 8,470 | \$ 8,451 | \$ 8,368 |
| Increase (decrease) in taxes resulting from: | | | |
| State income tax expense | 1,654 | 1,864 | 2,051 |
| Depreciation | 944 | 853 | 716 |
| Federal benefit of state taxes | (579) | (652) | (718) |
| Adjustments to prior years' provisions | (97) | (143) | 254 |
| Payment of premium on redemption | (813) | -- | -- |
| Other - net | (250) | (149) | (221) |
| | ----- | ----- | ----- |
| Total income tax expense | \$ 9,329 | \$ 10,224 | \$ 10,450 |

| | | | |
|---------------------------|-----------|-----------|-----------|
| Pre-tax income | \$ 24,201 | \$ 24,145 | \$ 23,910 |
| Effective income tax rate | 38.5% | 42.3% | 43.7% |

NOTE 6 - EMPLOYEE BENEFIT PLANS

The Company maintains a pension plan (the Plan) which provides eligible employees (those age 21 and older, with one year of service) monthly benefits upon retirement based on average salaries and length of service. The normal retirement benefit is equal to 2% of the five highest consecutive years average earnings multiplied by the number of years of credited service, up to a maximum of 40 years, reduced by a percentage of primary social security benefits. There is also an early retirement option. Annual contributions are made to the Plan which comply with the funding requirements of the Employee Retirement Income Security Act (ERISA). At December 31, 1998, the Company had 431 employees participating in the Plan, 69 of these employees are covered by collective bargaining agreements, the earliest of which expires in 1999.

The Company also provides all active employees medical, dental and vision care benefits through a medical insurance plan. Eligible employees who retired prior to age 65, and/or their spouses, were able to retain the benefits under the active plan until reaching age 65. Upon reaching age 65, and for those employees retiring at or after age 65, and/or their spouses, continued coverage was provided through a Medicare supplement insurance policy paid for by the Company.

The CPUC has issued a decision which provides for the recovery in rates of tax-deductible contributions made to a separately trustee fund. In accordance with that decision, SCW established two separate trusts in 1995, one for those retirees who were subject to a collectively bargained agreement and another for all other retirees. The company's funding policy is to contribute annually an amount at least equal to the revenues authorized to be collected through rates for post-retirement benefit costs. Post-retirement benefit costs for 1993, 1994 and 1995 were estimated at a total of \$1.6 million and have been recorded as a regulatory asset for recovery over a 20 year period.

The following table sets forth the Plan's funded status and amounts recognized in the company's balance sheets and the components of net pension cost and accrued post-retirement liability at December 31, 1998 and 1997:

| (dollars in thousands) | Pension Benefits | | Other Benefits | |
|--|------------------|-----------|----------------|-----------|
| | 1998 | 1997 | 1998 | 1997 |
| Change in Benefit Obligation: | | | | |
| Benefit Obligation at beginning of year | \$ 33,410 | \$ 28,733 | \$ 4,503 | \$ 4,013 |
| Service Cost | 1,597 | 1,351 | 112 | 120 |
| Interest Cost | 2,278 | 2,112 | 283 | 295 |
| Actuarial Loss/(Gain) | 2,514 | 2,373 | (368) | 225 |
| Benefits Paid | (1,227) | (1,159) | (167) | (150) |
| Benefit Obligation at end of year | \$ 38,572 | \$ 33,410 | \$ 4,363 | \$ 4,503 |
| Changes in Plan Assets: | | | | |
| Fair Value of Plan Assets at beginning of year | \$ 33,433 | \$ 29,240 | \$ 1,104 | \$ 548 |
| Actual Return of Plan Assets | 6,051 | 4,065 | 44 | 49 |
| Employer Contributions | 1,284 | 1,287 | 461 | 656 |
| Benefits Paid | (1,227) | (1,159) | (167) | (150) |
| Fair Value of Plan Assets at end of year | \$ 39,541 | \$ 33,433 | \$ 1,442 | \$ 1,103 |
| Reconciliation of Funded Status: | | | | |
| Funded Status | \$ 969 | \$ 23 | \$(2,921) | \$(3,399) |
| Unrecognized Transition Obligation | 114 | 171 | 6,707 | 7,126 |
| Unrecognized Net Loss/(Gain) | 677 | 1,538 | (1,860) | (1,644) |
| Unrecognized Prior Service Cost | 400 | 444 | (3,427) | (3,627) |
| Prepaid/(Accrued) Pension Cost | \$ 2,160 | \$ 2,176 | \$(1,501) | \$(1,544) |
| Weighted-Average Assumptions as of December 31: | | | | |
| Discount Rate | 6.50% | 7.00% | 6.50% | 7.00% |
| Long-term Rate of Return | 8.00% | 8.00% | 8.00% | 8.00% |
| Salary Assumption | 4.00% | 4.00% | -- | -- |

A sliding scale for assumed health care cost increases was used for both periods, starting at 11% in 1996 declining 1% per year for five years and then remaining at 6% thereafter. The components of net periodic post-retirement benefits cost for 1998 and 1997 are as follows:

| (dollars in thousands) | Pension Benefits | | Other Benefits | |
|---|------------------|----------|----------------|--------|
| | 1998 | 1997 | 1998 | 1997 |
| Components of Net Periodic Benefits Cost | | | | |
| Service Cost | \$ 1,597 | \$ 1,351 | \$ 112 | \$ 120 |
| Interest Cost | 2,278 | 2,112 | 283 | 294 |
| Actual Return on Plan Assets | (6,051) | (4,065) | (44) | (48) |
| Net Amortization | 3,476 | 1,873 | 67 | 140 |
| Net Periodic Pension Cost | \$ 1,300 | \$ 1,271 | \$ 418 | \$ 506 |

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

| (dollars in thousands) | 1-Percentage-Point Increase | 1-Percentage-Point Decrease |
|---|-----------------------------|-----------------------------|
| Effect on Total of Service and Interest Cost Components | \$ 13 | \$ (11) |
| Effect on Postretirement Benefit Obligation | 206 | (180) |

The Company has a 401(k) Investment Incentive Program under which employees may

invest a percentage of their pay, up to a maximum investment prescribed by law, in an investment program managed by an outside investment manager. Company contributions to the 401(k) are based upon a percentage of individual employee contributions and, for 1998, 1997 and 1996, totaled \$874,113, \$785,687, and \$839,000, respectively.

NOTE 7 - BUSINESS RISKS AND CONCENTRATION OF SALES

The Company's utility operations are engaged in supplying water and electric service to the public. The Company is required to provide service and grant credit to customers within its defined service areas. Although the Company has a diversified base of residential, industrial and other customers, revenues derived from commercial and residential water customers accounted for approximately 91% and 93% of total water revenues in 1998 and 1997. The Company faces additional risks associated with weather conditions,

adequacy and quality of water supplies, regulatory decisions, pronouncements and laws, water-related litigation, general business conditions and condemnation.

Approximately 39% of the Company's water supply is purchased from wholesalers of imported water, with the remainder produced from Company-owned wells. The long term availability of imported water supplies is dependent upon, among other things, drought conditions throughout the state, increases in population, water quality standards and legislation that may potentially reduce water supplies. The Company does not anticipate any constraints on its imported water supplies in 1999.

NOTE 8 - CONTINGENCIES

In 1998, ASUS was formed to pursue non-regulated opportunities such as long-term leases, and operation and maintenance contracts of governmentally-owned water and wastewater systems. As a result, the Company anticipates terminating its Golden State Water Company joint venture during 1999. Accordingly, the Company reserved approximately \$336,000 against future losses and capital account adjustments.

Hearings were held before the CPUC in November 1998 on SCW's filing seeking recovery through rates of \$1.8 million in costs associated with its participation in the coastal aqueduct extension of the State Water Project. In February 1999, the Administrative Law Judge in this proceeding issued his proposed decision that denied rate recovery of SCW's costs in the project. A final order from the CPUC is anticipated in 1999. SCW is unable to predict if the CPUC will authorize recovery of all or any of the costs associated with its participation in the project. Alternate forms of recovery are also being pursued including assessment of costs to new construction based on an equivalent dwelling unit charge or other applicable unit of measurement, which assessment will require CPUC approval prior to implementation or, failing that, sale of SCW's participation in the project.

SCW has been named as a defendant in seven lawsuits which allege that the SCW delivered contaminated water to its customers. Plaintiffs in these actions seek damages, including general, special, and punitive damages, according to proof of trial, as well as attorney's fees on certain causes of action, costs of suit, and other unspecified relief. Stays have been issued by the respective courts in five of these cases pending the outcome of the CPUC's investigation into water quality discussed below. One action has been dismissed against SCW and SCW has petitioned for dismissal in the remaining case. Most activity related to these lawsuits has ceased due to the stays although SCW anticipates that plaintiff's attorneys will petition the courts to reconsider their prior decisions. In light of the breadth of plaintiff's claims, the lack of factual information regarding plaintiff's claims and injuries, if any, the fact that no discovery has yet been completed, SCW is unable to determine at this time what, if any, potential liability it may have with respect to these claims. SCW intends to vigorously defend itself against these allegations. Management can not predict the outcome of these proceedings and if SCW is found liable, SCW would pursue recovery through its insurance coverage providers.

In response to those lawsuits and similar actions, in March 1998 the CPUC issued an Order Instituting Investigation (OII) directed to all Class A and B water utilities in the state of California, including SCW, into whether existing standards and policies regarding drinking water quality adequately protect the public health and whether those standards and policies are being uniformly complied with by those water utilities. The OII notes the constitutional and statutory jurisdiction of the CPUC and the DOHS to establish and enforce adherence to water quality standards for water delivered by utilities to their customers and, in the case of the CPUC, to establish rates which permit water utilities to furnish safe water, meeting the established water quality standards at prices which are both affordable and that allow the utility to earn a reasonable return on its investment. SCW has made its filing in this proceeding on a series of questions dealing with the safety of current drinking water standards, compliance by water utilities with such standards, appropriate remedies for failure to comply with safe drinking standards and whether stricter or additional safety drinking water standards are required. The Water Division of the CPUC has issued its report based on these filings by the utilities. Although the OII leaves open the possibility of evidentiary hearings and further action by the CPUC, SCW is currently unable to predict the outcome of this proceeding.

Management believes that proper insurance coverage and reserves are in place to insure against anticipated property, general and product liability and workers' compensation claims.

NOTE 9 - CONSTRUCTION PROGRAM

SCW's 1999 construction budget provides for gross expenditures of approximately \$46.5 million of which \$4.4 million is anticipated to be obtained from developers and others. AWR and ASUS have no material capital expenditure programs.

NOTE 10 - ALLOWANCE FOR DOUBTFUL ACCOUNTS

The table below presents SCW's provision for doubtful accounts charged to expense and accounts written off, net of recoveries for the last three years.

| (dollars in thousands) | December 31, | | |
|---|--------------|--------|--------|
| | 1998 | 1997 | 1996 |
| Balance at beginning of year | \$ 466 | \$ 387 | \$ 648 |
| Provision charged to expense | 631 | 707 | 571 |
| Accounts written off, net of recoveries | (694) | (628) | (832) |
| Balance at end of year | \$ 403 | \$ 466 | \$ 387 |

Neither AWR nor ASUS have established any provision for doubtful accounts.

NOTE 11 - BUSINESS SEGMENTS

The Company has no material operations other than its SCW subsidiary. The tables below set forth information relating to SCW's operating segments. SCW manages its operations on a regional basis using the five categories below as broad-level measures of profitability. In addition to the amounts set forth, certain assets have been allocated. The identifiable assets are net of respective accumulated provisions for depreciation.

| (dollars in thousands) | Year Ended December 31, 1998 | | | |
|--------------------------------------|------------------------------|--------------------|------------|----------|
| | Region I | Water Region II | Region III | Electric |
| Operating revenues | \$24,927 | \$ 76,304 | \$ 33,552 | \$13,211 |
| Operating income before income taxes | 6,799 | 15,615 | 9,261 | 3,847 |
| Identifiable assets | 97,463 | 176,832 | 115,475 | 26,719 |
| Depreciation expense | 2,551 | 4,755 | 3,324 | 1,640 |
| Capital additions | \$13,206 | \$ 20,650 | \$ 9,714 | \$ 1,699 |

| (dollars in thousands) | Year Ended December 31, 1997 | | | |
|--------------------------------------|------------------------------|--------------------|------------|----------|
| | Region I | Water Region II | Region III | Electric |
| Operating revenues | \$24,340 | \$ 81,200 | \$ 35,436 | \$12,779 |
| Operating income before income taxes | 5,897 | 13,032 | 10,270 | 4,089 |
| Identifiable assets | 87,039 | 162,037 | 109,436 | 25,095 |
| Depreciation expense | 2,306 | 4,483 | 3,162 | 1,001 |
| Capital additions | \$10,065 | \$ 18,882 | \$ 8,139 | \$ 2,140 |

| (dollars in thousands) | Year Ended December 31, 1996 | | | |
|--------------------------------------|------------------------------|--------------------|------------|----------|
| | Region I | Water Region II | Region III | Electric |
| Operating revenues | \$23,536 | \$ 81,474 | \$ 34,980 | \$11,540 |
| Operating income before income taxes | 4,705 | 14,813 | 10,776 | 3,418 |
| Identifiable assets | 79,974 | 148,078 | 104,390 | 25,333 |
| Depreciation expense | 2,109 | 4,131 | 2,939 | 924 |
| Capital additions | \$ 5,975 | \$ 19,370 | \$ 6,537 | \$ 2,492 |

NOTE 12 - SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

The quarterly financial information presented below is unaudited. The business of the Company is of a seasonal nature and it is management's opinion that comparisons of earnings for the quarter periods do not reflect overall trends and changes in the Company's operations.

| (in thousands, except per share amounts) | Operating Revenues | | Operating Income | | Net Income | | Earnings per Share | |
|---|-----------------------|-----------|---------------------|----------|------------|----------|-----------------------|--------|
| | 1998 | 1997 | 1998 | 1997 | 1998 | 1997 | 1998 | 1997 |
| First Quarter | \$ 29,955 | \$ 32,206 | \$ 4,382 | \$ 3,738 | \$ 1,843 | \$ 1,312 | \$0.20 | \$0.14 |
| Second Quarter | 35,001 | 39,343 | 5,586 | 5,372 | 2,767 | 3,080 | 0.31 | 0.34 |
| Third Quarter | 47,002 | 45,700 | 9,432 | 8,385 | 6,374 | 6,044 | 0.71 | 0.67 |
| Fourth Quarter | 36,102 | 36,506 | 5,661 | 5,963 | 3,639 | 3,623 | 0.40 | 0.41 |
| Year | \$148,060 | \$153,755 | \$25,061 | \$23,458 | \$14,623 | \$14,059 | \$1.62 | \$1.56 |

NOTE 13 - YEAR 2000 READINESS

The Company continues to evaluate its exposure to the Year 2000 (Y2K) problem that arises from the fact that many existing computer systems may contain date sensitive embedded technology that uses only two digits to identify a year in the date field. Based on the assumption that the first two digits of the date field are always "19", such systems may misinterpret dates after December 31, 1999. Because the Company is dependent upon the proper functioning of these computer systems and other equipment containing date sensitive technology, a failure of these systems could have a material and adverse affect on the Company resulting in business interruption or shutdown, financial loss, regulatory citations and legal liability.

The Company has been actively assessing its Y2K readiness since early 1997 and has inventoried its significant computer hardware and software programs. Since the Company is dependent upon its management information and customer service systems, upgrades to these systems have been a priority. The Company has, since 1995, been in the process of replacing and/or upgrading as necessary its core business information and operating systems with newer technologies, all of which will be Y2K ready. All major upgrades to these systems are completed and were operational at year-end 1998. Costs associated with the implementation and upgrade of major management information and customer service software systems, as well as upgrades to mainframe hardware systems, have been approved by the CPUC and are being recovered through rates.

In addition to work being done on its internal systems, the Company has sought compliance certification from external vendors and service providers. Testing on the Company's interface with financial and other institutions with which it does business is being conducted to ensure Y2K readiness. In order to more fully address Y2K readiness of its field equipment, major vendors and service providers, the Company engaged the services of a nationally-recognized business consulting firm and has completed its written plan to address the Y2K issue. The Company has established a Year 2000 Task Force consisting of senior management and operating personnel which will complete the inventory of computer systems and other devices with embedded technology, as well as other considerations potentially not revealed in preliminary internal analyses.

The Company's general process for addressing the Y2K issue is (i) to inventory all systems that may have a potential Y2K impact, (ii) to determine the materiality of these non-Y2K ready systems, (iii) to replace and test, correct and test, or prepare for the failure of material items that have been determined to be non-Y2K ready, and (iv) to prepare contingency plans. Some, less critical systems may not be fully Y2K ready, but are not anticipated to materially affect the Company's operations.

The Company is significantly dependent on third party suppliers, such as energy and telecommunication companies and wholesale water suppliers. In order to conduct its business, the Company has initiated due diligence with certain of its major service providers to address their Y2K readiness. In the event that such suppliers might be adversely affected by Y2K, the Company is preparing its contingency plan which will likely include, among other things, increased staffing during critical periods, manual back-up for automated systems, the use of electric generators capable of providing power during a black-out. The Company does not have, and may never fully have, sufficient information about the Y2K exposure or remediation plans of these third parties to adequately predict the risks posed by them to the Company. If the third parties have Y2K problems that are not remedied, resulting problems could include loss of utility services and disruption of water supplies.

To date, there have been no significant costs associated with Y2K readiness that have not been approved by the CPUC for recovery through rates. The Company estimates that it may incur up to \$800,000 in costs depending on the results of on-going tests, to make critical systems Y2K ready. The Company believes that the future costs, which are prudently incurred, will also be allowed for recovery through rates. The CPUC has notified all utilities under its jurisdiction, including the Company, that it will review their Y2K preparations.

REPORT OF MANAGEMENT

The financial statements contained in this annual report were prepared by the management of American States Water Company, which is responsible for their integrity and objectivity. The financial statements were prepared in accordance with generally accepted accounting principles and include, where necessary, amounts based upon management's best estimates and judgments. All other financial information in the annual report is consistent with the financial statements and is also the responsibility of management.

The Company maintains systems of internal control which are designed to help safeguard the assets of the Company and provide reasonable assurance that accounting and financial records can be relied upon to generate accurate financial statements. These systems include the hiring and training of qualified personnel, appropriate segregation of duties, delegation of authority and an internal audit function which has reporting responsibility to the Audit Committee of the Board of Directors.

The Audit Committee, composed of three outside directors, exercises oversight of management's discharge of its responsibilities regarding the systems of internal control and financial reporting. The committee periodically meets with management, the internal auditor and the independent accountants to review the work and findings of each. The committee also reviews the qualifications of, and recommends to the Board of Directors, a firm of independent accountants.

The independent accountants, Arthur Andersen LLP, have performed an audit of the financial statements in accordance with generally accepted auditing standards. Their audit gave consideration to the company's system of internal accounting control as a basis for establishing the nature, timing and scope of their work. The result of their work is expressed in their Report of Independent Public Accountants.

/s/ Floyd E. Wicks
Floyd E. Wicks
President, Chief Executive Officer

/s/ McClellan Harris III
McClellan Harris III
Chief Financial Officer,
Vice President - Finance,
Treasurer and Corporate Secretary

February 8, 1999

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Shareholders and the Board of Directors of American States Water Company:

We have audited the balance sheets and statements of capitalization of American States Water Company (a California corporation) as of December 31, 1998 and 1997 and the related statements of income, changes in common shareholders' equity and cash flows for each of the three years in the period ended December 31, 1998. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of American States Water Company as of December 31, 1998 and 1997, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles.

/s/ Arthur Anderson
Arthur Andersen LLP
Los Angeles, California

February 8, 1999

SHAREHOLDER INFORMATION

ANNUAL MEETING OF SHAREHOLDERS

All shareholders are invited to attend the Annual Meeting of Shareholders which will be held on Tuesday, April 27, 1999, beginning at 10:00 am, at the Industry Hills Sheraton, One Industry Hills Parkway, City of Industry, California 91744. Notice of meeting and proxy materials will be mailed.

STOCK LISTING

Common Shares of American States Water Company are traded on the New York Stock Exchange under the symbol AWR. The high and low sales prices and dividends paid on the Common Shares for the past two years were:

| 1998 | High | Low | Dividends Paid |
|----------------|--------|-----------|----------------|
| | ----- | ----- | ----- |
| First Quarter | \$26 | \$23 1/16 | \$0.315 |
| Second Quarter | 27 1/8 | 21 1/8 | 0.315 |
| Third Quarter | 27 | 23 1/4 | 0.315 |
| Fourth Quarter | 29 1/4 | 24 7/8 | 0.315 |
| | ----- | ----- | ----- |
| | | | \$1.260 |
| 1997 | | | |
| First Quarter | \$23 | \$20 5/8 | \$0.310 |
| Second Quarter | 24 1/2 | 20 1/4 | 0.310 |
| Third Quarter | 24 5/8 | 20 1/2 | 0.310 |
| Fourth Quarter | 25 5/8 | 21 1/2 | 0.315 |
| | ----- | ----- | ----- |
| | | | \$1.245 |

INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Arthur Andersen LLP
633 West Fifth Street
Los Angeles, CA 90071

CORPORATE REPORTS

Shareholders with questions, or who wish to obtain a copy of the Company's reports to the Securities and Exchange Commission without charge, should contact:

AMERICAN STATES WATER COMPANY

Attn: Corporate Secretary
630 East Foothill Boulevard
San Dimas, CA 91773
Phone: (909) 394-3600
Fax: (909) 394-1382

SHAREHOLDER ASSISTANCE

Shareholders with questions about replacement of dividend checks, transferring stock, replacing lost or stolen certificates or other matters related to their ownership of stock, should contact:

ChaseMellon Shareholder Services, L.L.C.
Overpeck Centre
85 Challenger Road
Ridgefield Park, NJ 07660
(888) 816-6998
<http://www.cmsonline.com>

DIVIDEND REINVESTMENT AND COMMON SHARE PURCHASE PLAN

The Company has a Dividend Reinvestment and Common Share Purchase Plan that offers shareholders of record a convenient way to increase their holdings by reinvesting all or part of their cash dividends in additional Common Shares of the Company. A prospectus and enrollment form may be obtained from ChaseMellon Shareholder Services, L.L.C. or from the Company.

1999 DIVIDEND SCHEDULE

The following schedule shows the anticipated Common and Preferred Share record and payment dates for 1999:

| | |
|--------------|---------------|
| Record Dates | Payment Dates |
| February 8 | March 1 |
| May 10 | June 1 |
| August 9 | September 1 |
| November 8 | December 1 |

INTERNET ADDRESS

<http://www.aswater.com>

STATISTICAL REVIEW

(dollars in thousands, except per share and per customer amounts)

| | 1998 | 1997 | 1996 | 1995 | 1994 |
|--|-----------|-----------|-----------|-----------|-----------|
| Financial Information | | | | | |
| Revenues by Classification | | | | | |
| Residential and Commercial | \$123,271 | \$131,007 | \$126,456 | \$106,480 | \$100,796 |
| Industrial | 1,917 | 1,998 | 1,847 | 1,674 | 1,459 |
| Fire Service | 1,329 | 1,319 | 1,269 | 1,211 | 1,181 |
| Other | 8,342 | 6,664 | 10,425 | 9,557 | 8,651 |
| Total Water | 134,859 | 140,988 | 139,997 | 118,922 | 112,087 |
| Electric | 13,201 | 12,767 | 11,532 | 10,891 | 10,588 |
| Total operation revenues | 148,060 | 153,755 | 151,529 | 129,813 | 122,675 |
| Net Income | 14,623 | 14,059 | 13,460 | 12,165 | 11,338 |
| Earnings available for common shareholders | 14,533 | 13,967 | 13,366 | 12,069 | 11,240 |
| Earnings per common share | 1.62 | 1.56 | 1.69 | 1.54 | 1.43 |
| Dividends declared per common share | 1.26 | 1.25 | 1.23 | 1.21 | 1.20 |
| Book value per common share | 17.23 | 16.86 | 16.52 | 15.50 | 15.16 |
| Total assets | | | | | |
| Net Utility plant | 414,753 | 383,623 | 357,776 | 334,968 | 317,879 |
| Capital additions | 45,269 | 39,226 | 34,374 | 28,761 | 30,307 |
| Long-term debt | 120,809 | 115,286 | 107,190 | 107,455 | 92,891 |
| Preferred Shares | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 |
| Preferred shares -- mandatory redemption | 400 | 440 | 480 | 520 | 560 |
| Investment per customer | \$ 2,099 | \$ 1,900 | \$ 1,808 | \$ 1,688 | \$ 1,578 |
| Operation Information | | | | | |
| Water sold by Classification (mg) | | | | | |
| Residential and Commercial | 49,302 | 54,623 | 52,843 | 49,641 | 51,084 |
| Industrial | 832 | 899 | 828 | 802 | 818 |
| Fire Service | 649 | 417 | 831 | 130 | 308 |
| Other | 4,201 | 5,070 | 4,932 | 4,706 | 4,537 |
| Total Water | 54,984 | 61,009 | 59,434 | 55,279 | 56,747 |
| Total electric sales (mwh) | 123,791 | 121,315 | 117,139 | 111,519 | 110,234 |
| Customers by Classification | | | | | |
| Residential and Commercial | 237,157 | 236,270 | 235,244 | 233,920 | 232,879 |
| Industrial | 332 | 331 | 333 | 326 | 323 |
| Fire Service | 3,112 | 2,964 | 2,925 | 2,909 | 2,896 |
| Other | 2,033 | 2,016 | 2,046 | 1,807 | 1,807 |
| Total Water | 242,634 | 241,581 | 240,548 | 238,962 | 237,905 |
| Electric | 20,865 | 20,698 | 20,437 | 20,475 | 20,331 |
| Total company | 263,499 | 262,279 | 260,985 | 259,437 | 258,236 |
| Water Production by Source (mg) | | | | | |
| Purchased | 22,885 | 28,894 | 27,147 | 24,356 | 25,940 |
| Pumped -- electric | 35,596 | 34,531 | 35,216 | 34,105 | 33,337 |
| Pumped -- gas | 75 | 316 | 40 | 218 | 198 |
| Gravity and Surface | 74 | 1,147 | 932 | 979 | 967 |
| Total Supply | 58,630 | 64,888 | 63,335 | 59,658 | 60,442 |
| Miles of Main in Service | 2,768 | 2,638 | 2,603 | 2,587 | 2,567 |
| Number of Employees | 470 | 467 | 463 | 448 | 467 |

mg=Millions of Gallons mwh=Mega-Watt Hours

(dollars in thousands, except per share and per customer amounts)

| | 1993 | 1992 | 1991 | 1990 | 1989 |
|--|-----------|-----------|-----------|-----------|-----------|
| Financial Information | | | | | |
| Revenues by Classification | | | | | |
| Residential and Commercial | \$ 86,918 | \$ 82,112 | \$ 68,063 | \$ 69,161 | \$ 67,404 |
| Industrial | 1,134 | 1,110 | 1,019 | 1,021 | 1,074 |
| Fire Service | 1,149 | 1,067 | 927 | 954 | 785 |
| Other | 8,954 | 6,336 | 8,273 | 5,150 | 4,909 |
| Total Water | 98,155 | 90,625 | 78,282 | 76,286 | 74,172 |
| Electric | 10,351 | 10,035 | 12,378 | 11,054 | 10,043 |
| Total operation revenues | 108,506 | 100,660 | 90,660 | 87,340 | 84,215 |
| Net Income | | | | | |
| Net Income | 12,026 | 12,142 | 15,363 | 8,907 | 8,730 |
| Earnings available for common shareholders | 11,926 | 12,040 | 15,259 | 8,801 | 8,622 |
| Earnings per common share | 1.66 | 1.82 | 2.34 | 1.40 | 1.38 |
| Dividends declared per common share | 1.19 | 1.15 | 1.10 | 1.08 | 1.04 |
| Book value per common share | 14.92 | 13.28 | 12.59 | 11.31 | 10.97 |
| Total assets | | | | | |
| Total assets | 358,533 | 312,491 | 293,444 | 268,028 | 254,346 |
| Net Utility plant | 294,990 | 277,525 | 258,558 | 235,713 | 214,465 |
| Capital additions | 28,626 | 26,975 | 32,472 | 27,078 | 25,726 |
| Long-term debt | 84,621 | 84,195 | 82,634 | 67,246 | 67,767 |
| Preferred Shares | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 |
| Preferred shares -- mandatory redemption | 600 | 640 | 680 | 720 | 760 |
| Investment per customer | \$ 1,480 | \$ 1,388 | \$ 1,297 | \$ 1,213 | \$ 1,125 |
| Operation Information | | | | | |
| Water sold by Classification (mg) | | | | | |
| Residential and Commercial | 48,033 | 47,541 | 44,528 | 51,696 | 51,841 |
| Industrial | 679 | 699 | 737 | 937 | 966 |
| Fire Service | 33 | 23 | 11 | 50 | 25 |
| Other | 4,019 | 3,890 | 3,807 | 4,511 | 4,635 |
| Total Water | 52,764 | 52,153 | 49,083 | 57,194 | 57,467 |
| Total electric sales (mwh) | | | | | |
| Total electric sales | 106,234 | 105,346 | 101,923 | 103,376 | 97,583 |
| Customers by Classification | | | | | |
| Residential and Commercial | 231,966 | 230,956 | 230,175 | 221,888 | 220,876 |
| Industrial | 322 | 330 | 347 | 376 | 385 |
| Fire Service | 2,877 | 2,846 | 2,779 | 2,610 | 2,562 |
| Other | 1,820 | 1,795 | 1,812 | 1,819 | 1,813 |
| Total Water | 236,985 | 235,927 | 235,113 | 226,693 | 225,636 |
| Electric | 20,131 | 20,039 | 19,780 | 19,559 | 19,215 |
| Total company | 257,116 | 255,966 | 254,893 | 246,252 | 244,851 |
| Water Production by Source (mg) | | | | | |
| Purchased | 25,156 | 24,377 | 23,221 | 31,021 | 32,189 |
| Pumped -- electric | 32,056 | 30,406 | 28,640 | 28,923 | 29,733 |
| Pumped -- gas | 195 | 177 | 245 | 270 | 306 |
| Gravity and Surface | 658 | 1,249 | 1,046 | 1,255 | 361 |
| Total Supply | 58,065 | 56,209 | 53,152 | 61,469 | 62,589 |
| Miles of Main in Service | | | | | |
| Miles of Main in Service | 2,560 | 2,549 | 2,535 | 2,517 | 2,488 |
| Number of Employees | | | | | |
| Number of Employees | 486 | 445 | 422 | 410 | 388 |

mg=Millions of Gallons mwh=Mega-Watt Hours

CUSTOMER SERVICE AREAS SERVED BY SOUTHERN CALIFORNIA WATER COMPANY

Number of Customers

Region I

| | |
|-------------------|--------|
| Northern District | |
| Arden-Cordova | 13,700 |
| Bay Point | 4,900 |
| Clearlake | 2,000 |

| | |
|------------------|--------|
| Coastal District | |
| Los Osos | 3,100 |
| Ojai | 2,800 |
| Santa Maria | 12,600 |
| Simi Valley | 12,500 |

Region II

| | |
|--------------------|--------|
| Central District | |
| Central Basin East | 19,600 |
| Central Basin West | 19,300 |
| Culver City | 9,300 |

| | |
|------------------------|--------|
| Orange County District | |
| Los Alamitos | 26,200 |
| Placentia | 14,400 |

| | |
|--------------------|--------|
| Southwest District | 49,300 |
|--------------------|--------|

Region III

| | |
|--------------------|--------|
| Foothill District | |
| Claremont | 10,400 |
| San Dimas | 15,600 |
| San Gabriel Valley | 11,800 |

| | |
|--------------------------|-------|
| Mountain/Desert District | |
| Apple Valley | 2,300 |
| Barstow | 8,400 |
| Calipatria | 1,100 |
| Morongo Valley | 800 |
| Wrightwood | 2,500 |

| | |
|-------------|---------|
| Total Water | 242,600 |
|-------------|---------|

| | |
|----------------------|--------|
| Bear Valley Electric | 20,900 |
|----------------------|--------|

| | |
|-----------------|---------|
| Total Customers | 263,500 |
|-----------------|---------|

CORPORATE INFORMATION

Board of Directors of American States Water Company, Southern California Water Company and American States Utility Services, Inc.

W. V. Caveney (72,18)(a,c)
Chairman of the Board

Floyd E. Wicks (55,9)(c,d)
President, Chief Executive Officer

James L Anderson (57,2)(a,c)
Senior Vice President
Americo Life Inc.
Laguna Hills, California

Jean E. Auer (62,3)(a,b,c,d)
Consultant and member of the
Board of Directors of the Water
Education Foundation

Vice Mayor of the
Town of Hillsborough, California

N. P. Dodge, Jr. (62,8)(a,b)
President, N.P. Dodge Company
Omaha, Nebraska

Anne M. Holloway (45,1)(a,c)
Vice President, Peterson Worldwide, LLP
Atherton, California

Robert F. Kathol (57,3)(a,b)
Executive Vice President
Kirkpatrick, Pettis, Smith, Polian Inc.
Omaha, Nebraska

Lloyd E. Ross (57,3)(a,c,d)
Managing Partner, Invermex L.P.
Irvine, California

ELECTED OFFICERS

W. V. Caveney (72,30)(e)
Chairman of the Board

Floyd E. Wicks (55,11)(e)
President, Chief Executive Officer

McClellan Harris III (47,8)(e)
Chief Financial Officer, Vice President-Finance,
Treasurer and Corporate Secretary

Joel A. Dickson (46,8)(f)
Vice President-Business Development

Donald K. Sadoris (55,31)(g)
Vice President-Customer Service, Region I

Randell J. Vogel (63,6)(g)(h)
Vice President-Customer Service, Region II

James B. Gallagher (44,11)(g)
Vice President-Customer Service, Region III

Joseph F. Young (53,21)(g)
Vice President-Government Affairs

Denise L. Kruger (34,6)(g)
Vice President-Water Quality

Susan L. Conway (37,10)(g)
Vice President-Regulatory Affairs

(age, years of service as a Board member)

(a) Member - Compensation Committee

(b) Member - Audit Committee

(c) Member - Business Opportunities Committee

(d) Member - Nominating Committee

(e) Holds same title in Southern California Water Company and American States Utility Services, Inc.

(f) Holds same title in American States Utility Services, Inc. and holds title of Vice President - Customer and

Operations Support in Southern California Water Company

(g) Officer of Southern California Water Company only

(h) Mr. Vogel retired in February 1999

[PHOTO P. IBC]

IBC

AMERICAN STATES WATER COMPANY
630 East Foothill Boulevard, San Dimas, California 91773-1212
(909) 394-3600
www.aswater.com

BACK COVER

Page 2

Three graphical representations displaying Book Value per Common Share, Basic Earnings per Common Share and Dividends Declared per Common Share from 1994 through 1998. Book Value per Share was \$15.16 in 1994, \$15.50 in 1995, \$16.52 in 1996, \$16.86 in 1997 and \$17.23 in 1998. Basic Earnings per Common Share was \$1.43 in 1994, \$1.54 in 1995, \$1.69 in 1996, \$1.56 in 1997 and \$1.62 in 1998. Dividends Declared per Common Share was \$1.20 in 1994, \$1.21 in 1995, \$1.23 in 1996, \$1.25 in 1997 and 1.26 in 1998.

Page 5

A 2 by 2 inch photograph of W. V. Caveney, Chairman and Floyd E. Wicks, President and Chief Executive Officer.

Page 6

A table reflecting asset growth from 1929-1998. At the end of the first 48 years of the Company's existence between 1929 and 1977, Total Assets equaled \$102.0 million. At the end of the period 1977 through 1986, a period of 9 years, Total Assets equaled \$209.0 million. At the end of the period 1986 through 1992, a period of 6 years, Total Assets equaled \$313.0 million. At the end of the period 1992 through 1995, a period of 3 years, Total Assets equaled \$406.0 million. At the end of the period 1995 through 1998, a 3 year period, Total Assets equaled \$485.0 million

Page 7

Graphical representation of Total Assets for the period 1994 through 1998. Total Assets equaled \$383,627,000 in 1994, \$406,255,000 in 1995, \$430,922,000 in 1996, \$457,074 in 1997, and \$484,671 in 1998.

Page 9

Five pictorial representations including: Family of three with drinking glasses, active lawn sprinklers, man reading newspaper while sitting next to a fountain, children in swimming pool talking with adult male on edge of pool, and an aerial view of a residential development.

Page 10

Graphical representation of Net Income for the period of 1994 through 1998. Net Income was \$11,338,000 in 1994, \$12,165,000 in 1995, \$13,460,000 in 1996, \$14,059,000 in 1997 and \$14,623,000 in 1998.

Page 11

Graphical representation of Total Capitalization and Net Utility Plant for the period 1994 through 1998. Total Capitalization was \$214,013,000 in 1994, \$231,151,000 in 1995, \$256,036,000 in 1996, \$268,379,000 in 1997, and \$277,108,000 in 1998. Net Utility Plant was \$317,879,000 in 1994, \$334,968,000 in 1995, \$357,776,000 in 1996, \$383,623,000 in 1997, and \$414,753,000 in 1998.

Page 12

A 2 by 1 1/2 inch photograph of W.V. Caveney, Chairman of the Board.

Page 36

A topographical map, with altitude legend, of the state of California with bullet points marking all of Southern California Water Company's Customer Service Areas.

Page IBC

A 3 3/8 by 2 1/2 inch photograph of the Board of Directors of American States Water Company, Southern California Water Company and American States Utility Services, Inc. From the left, seated, are Lloyd E. Ross and James L. Anderson. From the left, standing, are Anne M. Holloway, W. V. Caveney, Jean E. Auer, Robert F. Kathol, N. P. Dodge, Jr., Floyd E. Wicks.

SUBSIDIARIES OF REGISTRANT

- 1.0 American States Water Company (Commission File No. 333-47647)
- 1.1 Southern California Water Company
- 1.2 American States Utility Services, Incorporated
- 2.0 Southern California Water Company (Commission File No. 000-01121)
- 2.1 No material subsidiaries

CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS

As independent public accountants, we hereby consent to the incorporation by reference in this Form 10-K of our report dated March 26, 1999 in the American States Water Company and Southern California Water Company Registration Statements below. It should be noted that we have not audited any financial statements of the Company subsequent to December 31, 1998.

| Registration Form | Registration No. | Effective Date |
|-------------------|------------------|-------------------|
| S - 3 | 33-42218 | August 22, 1991 |
| S - 8 | 33-71226 | November 4, 1993 |
| S - 3 | 333-68201 | December 16, 1998 |
| S - 3 | 333-68299 | December 22, 1998 |

s/ ARTHUR ANDERSEN LLP

Los Angeles, California
March 26, 1999

UT

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM BALANCE SHEETS AND INCOME STATEMENTS FOR THE TWELVE MONTHS ENDED DECEMBER 31, 1998 AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS FILED HEREWITH.

0001056903
SOUTHERN CALIFORNIA WATER COMPANY
1,000

| YEAR | DEC-31-1998 | JAN-01-1998 | DEC-31-1998 | PER-BOOK |
|---------|-------------|-------------|-------------|----------|
| | 414,753 | | | |
| | 1,077 | | | |
| | 39,288 | | | |
| | 29,553 | | | |
| | | 0 | | |
| | | 484,671 | | |
| | | | 22,394 | |
| | 74,937 | | | |
| | 56,968 | | | |
| 154,299 | | | | |
| | 440 | | | |
| | | 1,600 | | |
| | 120,112 | | | |
| | 38,000 | | | |
| | 1 | | | |
| 0 | | | | |
| 95 | | | | |
| | 40 | | | |
| | 916 | | | |
| | | 125 | | |
| 169,564 | | | | |
| 484,671 | | | | |
| | 148,060 | | | |
| | 10,130 | | | |
| | 112,869 | | | |
| | 122,999 | | | |
| | 25,061 | | | |
| | | 769 | | |
| 25,830 | | | | |
| | 11,207 | | | |
| | | 14,623 | | |
| | 90 | | | |
| 14,533 | | | | |
| | 11,296 | | | |
| | 0 | | | |
| | 31,404 | | | |
| | | 1.62 | | |
| | | 1.62 | | |