

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

- Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended September 30, 2003 or
- Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from _____ to _____

Commission file number 333-47647

American States Water Company

(Exact Name of Registrant as Specified in Its Charter)

California

95-4676679

(State or Other Jurisdiction of Incorporation or Organization)

(IRS Employer Identification No.)

630 East Foothill Boulevard, San Dimas

91773

(Address of Principal Executive Offices)

(Zip Code)

(909) 394-3600

(Registrant's Telephone Number, Including Area Code)

Not Applicable

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Commission file number 000-01121

Southern California Water Company

(Exact Name of Registrant as Specified in Its Charter)

California

95-1243678

(State or Other Jurisdiction of Incorporation or Organization)

(IRS Employer Identification No.)

630 East Foothill Boulevard, San Dimas

91773

(Address of Principal Executive Offices)

(Zip Code)

(909) 394-3600

(Registrant's Telephone Number, Including Area Code)

Not Applicable

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

American States Water Company
Southern California Water Company

Yes No
Yes No

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Act.).

American States Water Company
Southern California Water Company

Yes No
Yes No

As of November 14, 2003, the number of Common Shares outstanding of American States Water Company was 15,202,152 shares.

As of November 14, 2003, all of the 110 outstanding Common Shares of Southern California Water Company were owned by American States Water Company.

TABLE OF CONTENTS

PART I

Item 1. Financial Statements

AMERICAN STATES WATER COMPANY CONSOLIDATED BALANCE SHEETS

AMERICAN STATES WATER COMPANY CONSOLIDATED STATEMENTS OF INCOME FOR THE THREE MONTHS

AMERICAN STATES WATER COMPANY CONSOLIDATED STATEMENTS OF INCOME FOR THE NINE MONTHS

AMERICAN STATES WATER COMPANY CONSOLIDATED STATEMENTS OF INCOME FOR THE TWELVE MONTHS

AMERICAN STATES WATER COMPANY CONSOLIDATED CASH FLOW STATEMENTS

SOUTHERN CALIFORNIA WATER COMPANY BALANCE SHEETS

SOUTHERN CALIFORNIA WATER COMPANY STATEMENTS OF INCOME FOR THE THREE MONTHS

SOUTHERN CALIFORNIA WATER COMPANY STATEMENTS OF INCOME FOR THE NINE MONTHS

SOUTHERN CALIFORNIA WATER COMPANY STATEMENTS OF INCOME FOR THE TWELVE MONTHS

SOUTHERN CALIFORNIA WATER COMPANY CASH FLOW STATEMENTS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operation

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Item 4. Controls and Procedures

PART II

Item 1. Legal Proceedings

Item 2. Changes in Securities

Item 3. Defaults Upon Senior Securities

Item 4. Submission of Matters to a Vote of Security Holders

Item 5. Other Information

Item 6. Exhibits and Reports on Form 8-K

SIGNATURE

EXHIBIT 10.1

EXHIBIT 31.1

EXHIBIT 31.2

EXHIBIT 32.1

EXHIBIT 32.2

**AMERICAN STATES WATER COMPANY
and
SOUTHERN CALIFORNIA WATER COMPANY
FORM 10-Q**

INDEX

	<u>Page No.</u>	
Part I	Financial Information	
Item		
1:	Financial Statements	1
	Consolidated Balance Sheets of American States Water Company as of September 30, 2003 and December 31, 2002	2
	Consolidated Statements of Income of American States Water Company for the Three Months Ended September 30, 2003 and September 30, 2002	4
	Consolidated Statements of Income of American States Water Company for the Nine Months Ended September 30, 2003 and September 30, 2002	5
	Consolidated Statements of Income of American States Water Company for the Twelve Months Ended September 30, 2003 and September 30, 2002	6
	Consolidated Statements of Cash Flow of American States Water Company for the Nine Months Ended September 30, 2003 and September 30, 2002	7
	Consolidated Balance Sheets of Southern California Water Company as of September 30, 2003 and December 31, 2002	8
	Consolidated Statements of Income of Southern California Water Company for the Three Months Ended September 30, 2003 and September 30, 2002	10
	Consolidated Statements of Income of Southern California Water Company for the Nine Months Ended September 30, 2003 and September 30, 2002	11
	Consolidated Statements of Income of Southern California Water Company for the Twelve Months Ended September 30, 2003 and September 30, 2002	12
	Consolidated Statements of Cash Flow of Southern California Water Company for the Nine Months Ended September 30, 2003 and September 30, 2002	13
	Notes to Consolidated Financial Statements	14
Item		
2:	Management's Discussion and Analysis of Financial Condition and Results of Operation	23
Item		
3:	Quantitative and Qualitative Disclosures About Market Risks	59
Item		
4:	Controls and Procedures	60
Part II	Other Information	
Item		
1:	Legal Proceedings	61
Item		
2:	Changes in Securities	64
Item		
3:	Defaults Upon Senior Securities	65
Item		
4:	Submission of Matters to a Vote of Security Holders	65
Item		
5:	Other Information	65
Item		
6:	Exhibits and Reports on Form 8-K	65
	Signature	66
	Certifications	67

PART I

Item 1. Financial Statements

General

The basic financial statements included herein have been prepared by Registrant, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission.

Certain information and footnote disclosures normally included in financial statements, prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted pursuant to such rules and regulations, although Registrant believes that the disclosures are adequate to make the information presented not misleading. In the opinion of management, all adjustments necessary for a fair statement of results for the interim period have been made.

It is suggested that these financial statements be read in conjunction with the financial statements and notes thereto in the latest Annual Report on Form 10-K of American States Water Company and its wholly owned subsidiary, Southern California Water Company.

Filing Format

This quarterly report on Form 10-Q is a combined report being filed by two separate Registrants: American States Water Company (hereinafter "AWR") and Southern California Water Company (hereinafter "SCW"). For more information, please see Note 1 to the *Notes to Financial Statements* and the heading entitled *General* in *Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operation*. 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.

AMERICAN STATES WATER COMPANY
CONSOLIDATED BALANCE SHEETS
ASSETS
(Unaudited)

(in thousands)	September 30, 2003	December 31, 2002
Utility Plant, at cost		
Water	\$ 708,779	\$ 693,949
Electric	41,519	41,017
	<u>750,298</u>	<u>734,966</u>
Less - Accumulated depreciation	(220,295)	(206,873)
	<u>530,003</u>	<u>528,093</u>
Construction work in progress	54,369	35,218
	<u>584,372</u>	<u>563,311</u>
Net utility plant	584,372	563,311
Other Property and Investments	<u>22,035</u>	<u>22,670</u>
	<u>606,407</u>	<u>606,081</u>
Current Assets		
Cash and cash equivalents	11,368	18,397
Accounts receivable-customers (less allowance for doubtful accounts of \$950 at 2003 and \$769 at 2002)	13,193	10,833
Unbilled revenue	15,459	12,277
Other accounts receivable	1,732	2,411
Taxes receivable	—	557
Materials and supplies, at average cost	1,525	936
Supply cost balancing accounts - current	4,190	3,215
Prepayments and other	2,455	3,220
	<u>49,922</u>	<u>51,846</u>
Deferred Charges and Other Long-Term Assets		
Regulatory tax-related assets	13,916	12,828
Supply cost balancing accounts	21,257	24,255
Other accounts receivable	3,370	3,370
Other	28,336	23,370
	<u>66,879</u>	<u>63,823</u>
Total Assets	<u>\$ 723,208</u>	<u>\$ 701,650</u>

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

AMERICAN STATES WATER COMPANY
CONSOLIDATED BALANCE SHEETS
CAPITALIZATION AND LIABILITIES
(Unaudited)

(in thousands)	September 30, 2003	December 31, 2002
Capitalization		
Common shareholders' equity	\$217,404	\$213,279
Long-term debt	230,121	231,089
Total capitalization	447,525	444,368
Current Liabilities		
Notes payable to banks	33,000	35,000
Long-term debt - current	13,305	13,305
Accounts payable	11,514	11,600
Taxes payable	2,074	—
Accrued employee expenses	6,059	5,105
Accrued interest	5,119	1,941
Other	10,990	12,569
Total current liabilities	82,061	79,520
Other Credits		
Advances for construction	74,586	70,208
Contributions in aid of construction - net	49,744	47,751
Accumulated deferred income taxes - net	60,382	53,817
Unamortized investment tax credits	2,723	2,791
Regulatory tax-related liability	1,987	2,011
Other	4,200	1,184
Total other credits	193,622	177,762
Commitments and Contingencies (Note 7)	—	—
Total Capitalization and Liabilities	\$723,208	\$701,650

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

AMERICAN STATES WATER COMPANY
CONSOLIDATED STATEMENTS OF INCOME
FOR THE THREE MONTHS
ENDED SEPTEMBER 30, 2003 AND 2002
(Unaudited)

(in thousands, except per share amounts)	Three Months Ended September 30,	
	2003	2002
Operating Revenues		
Water	\$57,574	\$55,866
Electric	5,906	5,529
Other	245	217
	<u>63,725</u>	<u>61,612</u>
Operating Expenses		
Water purchased	13,740	14,205
Power purchased for pumping	3,330	3,327
Power purchased for resale	3,382	3,645
Unrealized loss on purchased power contracts	420	—
Groundwater production assessment	2,089	1,831
Supply cost balancing accounts	650	(428)
Other operating expenses	4,805	4,883
Administrative and general expenses	10,058	7,848
Depreciation and amortization	4,944	4,622
Maintenance	2,181	2,546
Taxes on income	3,915	5,207
Other taxes	2,032	2,062
	<u>51,546</u>	<u>49,748</u>
Operating Income	12,179	11,864
Other Income (Loss)		
Other income - net	128	157
	<u>128</u>	<u>157</u>
Interest Charges		
Interest on long-term debt	4,229	4,213
Other interest and amortization of debt expense	282	169
	<u>4,511</u>	<u>4,382</u>
Net Income	7,796	7,639
Dividends on Preferred Shares	—	—
	<u>—</u>	<u>—</u>
Earnings Available for Common Shareholders	\$ 7,796	\$ 7,639
	<u>—</u>	<u>—</u>
Weighted Average Number of Shares Outstanding	15,202	15,154
Basic Earnings Per Common Share	\$ 0.51	\$ 0.50
Weighted Average Number of Diluted Shares	15,244	15,170
Fully Diluted Earnings Per Share	\$ 0.51	\$ 0.50
Dividends Declared Per Common Share	\$ 0.221	\$ 0.217

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

AMERICAN STATES WATER COMPANY
CONSOLIDATED STATEMENTS OF INCOME
FOR THE NINE MONTHS ENDED
SEPTEMBER 30, 2003 AND 2002
(Unaudited)

(in thousands, except per share amounts)	Nine Months Ended September 30,	
	2003	2002
Operating Revenues		
Water	\$ 143,206	\$ 143,722
Electric	18,263	14,574
Other	749	603
	<u>162,218</u>	<u>158,899</u>
Operating Expenses		
Water purchased	32,098	32,523
Power purchased for pumping	7,696	7,767
Power purchased for resale	10,052	13,973
Unrealized gain on purchased power contracts	(854)	—
Groundwater production assessment	5,485	5,427
Supply cost balancing accounts	2,109	(6,243)
Other operating expenses	13,931	12,811
Administrative and general expenses	29,472	24,291
Depreciation and amortization	14,836	13,728
Maintenance	6,430	6,632
Taxes on income	7,700	12,355
Other taxes	6,110	5,967
	<u>135,065</u>	<u>129,231</u>
Operating Income	27,153	29,668
Other Income (Loss)		
Other income - net	159	326
	<u>159</u>	<u>326</u>
Interest Charges		
Interest on long-term debt	12,704	12,717
Other interest and amortization of debt expense	911	396
	<u>13,615</u>	<u>13,113</u>
Net Income	13,697	16,881
Dividends on Preferred Shares	—	(29)
	<u>13,697</u>	<u>16,852</u>
Earnings Available for Common Shareholders	\$ 13,697	\$ 16,852
Weighted Average Number of Shares Outstanding	15,198	15,135
Basic Earnings Per Common Share	\$ 0.90	\$ 1.11
Weighted Average Number of Diluted Shares	15,230	15,153
Fully Diluted Earnings Per Share	\$ 0.90	\$ 1.11
Dividends Declared Per Common Share	\$ 0.663	\$ 0.651

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

**AMERICAN STATES WATER COMPANY
CONSOLIDATED STATEMENTS OF INCOME
FOR THE TWELVE MONTHS ENDED
SEPTEMBER 30, 2003 AND 2002
(Unaudited)**

(in thousands, except per share amounts)	Twelve Months Ended September 30,	
	2003	2002
Operating Revenues		Restated Note 2
Water	\$ 186,544	\$ 187,144
Electric	24,988	18,885
Other	991	813
	<u>212,523</u>	<u>206,842</u>
Operating Expenses		
Water purchased	42,434	40,190
Power purchased for pumping	10,506	10,565
Power purchased for resale	11,896	18,530
Unrealized loss on purchased power contracts	1,676	—
Groundwater production assessment	7,474	7,150
Supply cost balancing accounts	4,947	(9,444)
Other operating expenses	18,103	16,939
Administrative and general expenses	35,191	36,927
Depreciation and amortization	19,410	18,216
Maintenance	9,636	9,206
Taxes on income	8,293	14,228
Other taxes	7,824	7,654
	<u>177,390</u>	<u>170,161</u>
Operating Income	35,133	36,681
Other Income (Loss)		
Other income - net	224	39
	<u>224</u>	<u>39</u>
Interest Charges		
Interest on long-term debt	16,959	16,311
Other interest and amortization of debt expense	1,242	776
	<u>18,201</u>	<u>17,087</u>
Net Income	17,156	19,633
Dividends on Preferred Shares		(50)
	<u>\$ 17,156</u>	<u>\$ 19,583</u>
Earnings Available for Common Shareholders	\$ 17,156	\$ 19,583
Weighted Average Number of Shares Outstanding	15,192	15,131
Basic Earnings Per Common Share	\$ 1.13	\$ 1.29
Weighted Average Number of Diluted Shares	15,222	15,146
Fully Diluted Earnings Per Share	\$ 1.13	\$ 1.29
Dividends Declared Per Common Share	\$ 0.884	\$ 0.868

The accompanying notes are an integral part of these financial statements

AMERICAN STATES WATER COMPANY
CONSOLIDATED CASH FLOW STATEMENTS
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002
(Unaudited)

(in thousands)	Nine Months Ended September 30,	
	2003	2002
Cash Flows From Operating Activities:		
Net income	\$ 13,697	\$ 16,881
Adjustments for non-cash items:		
Depreciation and amortization	14,836	13,728
Deferred income taxes and investment tax credits	5,385	5,205
Unrealized gain on purchased power contracts	(854)	—
Other - net	1,282	2,099
Changes in assets and liabilities:		
Accounts receivable - customers	(2,360)	(3,549)
Unbilled revenue	(3,182)	(3,082)
Other accounts receivable	679	(370)
Prepayments and other current assets	176	332
Supply cost balancing accounts	2,109	(6,243)
Deferred charges and other assets	(2,828)	(3,936)
Accounts payable	(86)	4,088
Taxes payable	2,631	1,685
Other current liabilities	1,868	1,470
Net cash provided	<u>33,353</u>	<u>28,308</u>
Cash Flows From Investing Activities:		
Construction expenditures	(33,904)	(32,313)
Net cash used	<u>(33,904)</u>	<u>(32,313)</u>
Cash Flows From Financing Activities:		
Proceeds from issuance of common shares	505	1,100
Receipt of advances for and contributions in aid of construction	7,687	5,828
Refunds on advances for construction	(3,165)	(3,455)
Cash received on financing portion of purchased power contracts	1,539	—
Redemption of preferred shares	—	(1,880)
Repayment of long-term debt	(968)	(542)
Net change in notes payable to banks	(2,000)	(6,000)
Common and preferred dividends paid	(10,076)	(9,869)
Net cash used	<u>(6,478)</u>	<u>(14,818)</u>
Net decrease in cash and cash equivalents	(7,029)	(18,823)
Cash and cash equivalents, beginning of period	18,397	30,496
Cash and cash equivalents, end of period	<u>\$ 11,368</u>	<u>\$ 11,673</u>
Non-cash activities - supplemental disclosures:		
Adoption of new accounting standard for asset retirement obligations:		
Cumulative effect of adoption - Regulatory asset	\$ 2,495	—
Utility plant, net	223	—
Asset retirement obligations	(2,718)	—

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

SOUTHERN CALIFORNIA WATER COMPANY
BALANCE SHEETS
ASSETS
(Unaudited)

(in thousands)	September 30, 2003	December 31, 2002
Utility Plant, at cost		
Water	\$ 670,538	\$ 656,331
Electric	41,519	41,017
	<u>712,057</u>	<u>697,348</u>
Less - Accumulated depreciation	(209,384)	(196,660)
	<u>502,673</u>	<u>500,688</u>
Construction work in progress	51,555	33,705
	<u>554,228</u>	<u>534,393</u>
Net utility plant	554,228	534,393
Other Property and Investments	7,382	8,018
Current Assets		
Cash and cash equivalents	6,935	11,677
Accounts receivable-customers (less allowance for doubtful accounts of \$899 at 2003 and \$729 at 2002)	12,903	10,609
Unbilled revenue	15,170	12,060
Intercompany receivable	448	1,044
Other accounts receivable	1,608	2,234
Materials and supplies, at average cost	1,495	905
Supply cost balancing accounts - current	4,190	3,215
Prepayments and other	2,325	3,005
	<u>45,074</u>	<u>44,749</u>
Total current assets	45,074	44,749
Deferred Charges and Other Long-Term Assets		
Regulatory tax-related assets	13,916	12,828
Supply cost balancing accounts	21,257	24,255
Other accounts receivable	3,370	3,370
Other	27,447	22,398
	<u>65,990</u>	<u>62,851</u>
Total deferred charges	65,990	62,851
Total Assets	\$ 672,674	\$ 650,011

The accompanying notes are an integral part of these financial statements

SOUTHERN CALIFORNIA WATER COMPANY
BALANCE SHEETS
CAPITALIZATION AND LIABILITIES
(Unaudited)

(in thousands)	September 30, 2003	December 31, 2002
Capitalization		
Common shareholder's equity	\$211,151	\$207,562
Long-term debt	222,048	222,725
Total capitalization	433,199	430,287
Current Liabilities		
Long-term debt - current	12,780	12,780
Accounts payable	10,885	10,576
Intercompany payable	11,000	13,000
Taxes payable	4,776	1,099
Accrued employee expenses	5,934	5,033
Accrued interest	4,898	1,843
Other	10,652	12,276
Total current liabilities	60,925	56,607
Other Credits		
Advances for construction	64,263	59,640
Contributions in aid of construction	49,471	47,480
Accumulated deferred income taxes-net	57,208	51,195
Unamortized investment tax credits	2,723	2,791
Regulatory tax-related liability	1,987	2,011
Other credits	2,898	—
Total other credits	178,550	163,117
Commitments and Contingencies (Note 7)		
	—	—
Total Capitalization and Liabilities	\$672,674	\$650,011

The accompanying notes are an integral part of these financial statements

SOUTHERN CALIFORNIA WATER COMPANY
STATEMENTS OF INCOME
FOR THE THREE MONTHS
ENDED SEPTEMBER 30, 2003 AND 2002
(Unaudited)

(in thousands, except per share amounts)	Three Months Ended September	
	2003	2002
Operating Revenues		
Water	\$55,777	\$54,052
Electric	5,906	5,529
	<u>61,683</u>	<u>59,581</u>
Operating Expenses		
Water purchased	13,572	14,025
Power purchased for pumping	3,168	3,187
Power purchased for resale	3,383	3,645
Unrealized loss on purchased power contracts	420	—
Groundwater production assessment	2,089	1,831
Supply cost balancing accounts	650	(428)
Other operating expenses	4,441	4,505
Administrative and general expenses	8,602	7,003
Depreciation and amortization	4,709	4,387
Maintenance	2,101	2,488
Taxes on income	4,153	5,283
Other taxes	1,979	1,939
	<u>49,267</u>	<u>47,865</u>
Total operating expenses	49,267	47,865
Operating Income	12,416	11,716
Other Income (Loss)		
Other income - net	113	141
	<u>113</u>	<u>141</u>
Total other income (loss) - net	113	141
Interest Charges		
Interest on long-term debt	4,114	4,106
Other interest and amortization of debt expense	159	21
	<u>4,273</u>	<u>4,127</u>
Total interest charges	4,273	4,127
Net Income	\$ 8,256	\$ 7,730
	<u>110</u>	<u>110</u>
Weighted Average Number of Shares Outstanding	110	110
Basic Earnings Per Common Share	\$75,055	\$70,273
Dividends Declared Per Common Share	\$35,000	\$40,000

The accompanying notes are an integral part of these financial statements

SOUTHERN CALIFORNIA WATER COMPANY
STATEMENTS OF INCOME
FOR THE NINE MONTHS
ENDED SEPTEMBER 30, 2003 AND 2002
(Unaudited)

(in thousands, except per share amounts)	Nine Months Ended September 30,	
	2003	2002
Operating Revenues		
Water	\$ 138,636	\$ 138,854
Electric	18,263	14,574
	<u>156,899</u>	<u>153,428</u>
Operating Expenses		
Water purchased	31,566	31,999
Power purchased for pumping	7,339	7,444
Power purchased for resale	10,052	13,973
Unrealized gain on purchased power contracts	(854)	—
Groundwater production assessment	5,485	5,427
Supply cost balancing accounts	2,109	(6,243)
Other operating expenses	12,959	11,955
Administrative and general expenses	25,609	21,719
Depreciation and amortization	14,140	13,038
Maintenance	6,203	6,448
Taxes on income	8,601	12,698
Other taxes	5,845	5,612
	<u>129,054</u>	<u>124,070</u>
Total operating expenses	129,054	124,070
Operating Income	27,845	29,358
Other Income (Loss)		
Other income - net	131	289
	<u>131</u>	<u>289</u>
Total other income (loss)	131	289
Interest Charges		
Interest on long-term debt	12,361	12,378
Other interest and amortization of debt expense	474	(71)
	<u>12,835</u>	<u>12,307</u>
Total interest charges	12,835	12,307
Net Income	\$ 15,141	\$ 17,340
	<u>110</u>	<u>110</u>
Weighted Average Number of Shares Outstanding	110	110
Basic Earnings Per Common Share	\$ 137,645	\$ 157,636
Dividends Declared Per Common Share	\$ 105,000	\$ 100,000

The accompanying notes are an integral part of these financial statements

SOUTHERN CALIFORNIA WATER COMPANY
STATEMENTS OF INCOME
FOR THE TWELVE MONTHS
ENDED SEPTEMBER 30, 2003 AND 2002
(Unaudited)

(in thousands, except per share amounts)	Twelve Months Ended September 30,	
	2003	2002
Operating Revenues		Restated Note 2
Water	\$ 180,685	\$ 180,746
Electric	24,988	18,885
	<u>205,673</u>	<u>199,631</u>
Operating Expenses		
Water purchased	41,749	39,494
Power purchased for pumping	10,062	10,105
Power purchased for resale	11,896	18,530
Unrealized loss on purchased power contracts	1,676	—
Groundwater production assessment	7,474	7,150
Supply cost balancing accounts	4,947	(9,444)
Other operating expenses	16,826	15,840
Administrative and general expenses	30,064	34,007
Depreciation and amortization	18,487	17,215
Maintenance	9,357	8,949
Taxes on income	9,509	14,591
Other taxes	7,600	7,126
	<u>169,647</u>	<u>163,563</u>
Operating Income	36,026	36,068
Other Income (Loss)		
Other income (loss) - net	161	(32)
	<u>161</u>	<u>(32)</u>
Interest Charges		
Interest on long-term debt	16,503	15,812
Other interest and amortization of debt expense	662	136
	<u>17,165</u>	<u>15,948</u>
Net Income	\$ 19,022	\$ 20,088
Weighted Average Number of Shares Outstanding	110	110
Basic Earnings Per Common Share	\$172,927	\$182,618
Dividends Declared Per Common Share	\$138,000	\$130,000

The accompanying notes are an integral part of these financial statements

SOUTHERN CALIFORNIA WATER COMPANY
CASH FLOW STATEMENTS
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2003 AND 2002
(Unaudited)

(in thousands)	Nine Months Ended September 30,	
	2003	2002
Cash Flows From Operating Activities:		
Net income	\$ 15,141	\$ 17,340
Adjustments for non-cash items:		
Depreciation and amortization	14,140	13,038
Deferred income taxes and investment tax credits	4,833	5,052
Unrealized gain on purchased power contracts	(854)	—
Other - net	1,056	2,302
Changes in assets and liabilities:		
Accounts receivable - customers	(2,294)	(3,338)
Unbilled revenue	(3,110)	(2,995)
Other accounts receivable	626	(269)
Prepayments and other current assets	90	200
Supply cost balancing accounts	2,109	(6,243)
Deferred charges and other assets	(2,809)	(3,951)
Accounts payable	309	3,815
Intercompany payable	(1,404)	(7,325)
Taxes payable	3,677	1,559
Other current liabilities	1,647	1,254
Net Cash Provided	33,157	20,439
Cash Flows From Investing Activities:		
Construction expenditures	(31,974)	(31,685)
Net Cash Used	(31,974)	(31,685)
Cash Flows From Financing Activities:		
Receipt of advances for and contributions in aid of construction	7,576	5,723
Refunds on advances for construction	(2,811)	(3,089)
Cash received on financing portion of purchased power contracts	1,539	—
Repayments of long-term debt	(679)	(236)
Common and preferred dividends paid	(11,550)	(11,000)
Net Cash Used	(5,925)	(8,602)
Net decrease in cash and cash equivalents	(4,742)	(19,848)
Cash and cash equivalents, beginning of period	11,677	26,079
Cash and cash equivalents, end of period	\$ 6,935	\$ 6,231
Non-cash activities - supplemental disclosures:		
Adoption of new accounting standard for asset retirement obligations:		
Cumulative effect of adoption - Regulatory asset	\$ 2,479	—
Utility plant, net	221	—
Asset retirement obligations	(2,700)	—

The accompanying notes are an integral part of these financial statements

**AMERICAN STATES WATER COMPANY
AND
SOUTHERN CALIFORNIA WATER COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)**

American States Water Company (AWR), incorporated in 1998, is the parent company of Southern California Water Company (SCW), American States Utility Services, Inc. (ASUS) and Chaparral City Water Company (CCWC). More than 90% of AWR's assets consist of the common stock of SCW. SCW is a public utility company engaged principally in the purchase, production, distribution and sale of water in California. In addition, SCW distributes and sells electric energy in several mountain communities in California. Unless otherwise stated in this report, the term Registrant applies to both AWR and SCW, collectively.

Note 1 - Basis of Presentation: The consolidated financial statements included herein have been prepared by AWR, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America for annual financial statements have been condensed or omitted pursuant to such rules and regulations. The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. In the opinion of management, all adjustments, consisting of normal recurring items and estimates necessary for a fair statement of the results for the interim periods, have been made. It is suggested that these consolidated financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in the Form 10-K for the year ended December 31, 2002 filed with the SEC. Certain prior year amounts have been reclassified to conform to current year presentation.

Note 2 - Restatement of Previously Issued Financial Statements: In connection with a deferred tax analysis of Registrant's tax accounts performed in 2002, Registrant determined that it had miscalculated its net accumulated deferred income taxes over several years, resulting in taxes on income not being recognized in the proper period, and overstating Registrant's net deferred tax liabilities and current taxes payable. Registrant further determined that the amount of the overstatements, which totaled approximately \$4.7 million and \$4.9 million as of December 31, 2001 for AWR and SCW, respectively, arose in prior years and that prior years' financial statements should be restated to reduce net accumulated deferred income taxes, taxes payable and the related tax expense to reflect amounts currently due and deferred. The financial information for the twelve months ended September 30, 2002 included in these consolidated financial statements has been adjusted to give effect to the restatement. Although the total amount of the restatement was \$4.9 million to AWR as of December 31, 2001, the impact to the twelve months ended September 30, 2002 of this restatement was to increase taxes on income and decrease net income by \$70,000. Basic and diluted earnings per share decreased \$0.01 for the twelve months ended September 30, 2002 as a result of the restatement.

Note 3 - Earnings Per Share: Basic earnings per common share are calculated pursuant to Statement of Financial Accounting Standards (SFAS) No. 128, "Earnings per Share", and are based on the weighted average number of common shares outstanding during each period and net income after deducting preferred dividend requirements. Under the American States Water Company 2000 Stock Incentive Plan, stock options are granted to certain eligible employees. As a result, fully diluted earnings per share amounts are shown. Earnings per share for all periods presented also reflect a three-for-two split of Registrant's common shares effective June 7, 2002. In addition, during the nine months ended September 30, 2003, Registrant issued approximately 20,000 shares of common stock pursuant to its Dividend Reinvestment Plan and the 401(k) Investment Incentive Program for total proceeds of approximately \$505,000.

[Table of Contents](#)

Note 4 – Stock Incentive Plan: Registrant has a Stock Incentive Plan and applies Accounting Principles Board Opinion (APB) No. 25, “Accounting for Stock Issued to Employees”, in accounting for its stock options. Accordingly, no compensation cost for the Plan has been recognized for options granted at fair value at the date of grant. Registrant has also adopted the disclosure only requirements of SFAS No. 123, “Accounting for Stock-Based Compensation”. If Registrant had elected to adopt the optional recognition provisions of SFAS No. 123 for its stock options, net income and earnings per share applicable to common shareholders would have been changed to the pro forma amounts indicated below.

dollars in thousands except EPS	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Earnings available – common:				
As reported	\$7,796	\$7,639	\$13,697	\$16,852
Add: Stock-based compensation expense included in reported net income, net of tax	—	—	—	—
Less: Stock-based compensation expense determined under the fair-value accounting method, net of tax	(88)	(60)	(265)	(181)
Pro forma	\$7,708	\$7,579	\$13,432	\$16,671
Basic earnings per share:				
As reported	\$ 0.51	\$ 0.50	\$ 0.90	\$ 1.11
Pro forma	\$ 0.51	\$ 0.50	\$ 0.88	\$ 1.10
Diluted earnings per share:				
As reported	\$ 0.51	\$ 0.50	\$ 0.90	\$ 1.11
Pro forma	\$ 0.51	\$ 0.50	\$ 0.88	\$ 1.10

Note 5 - Regulatory Matters:

Changes in Rates:

Step increases of approximately \$321,600 for four of seven ratemaking districts in SCW’s Region I were implemented in January 2002. Region I also received attrition increases of \$219,400 effective January 2003.

On January 16, 2003, the California Public Utilities Commission (CPUC) approved rate increases of approximately \$2.7 million annually, effective January 22, 2003, in SCW’s Metropolitan district to recover costs associated with an increase in Region II rate base associated with SCW’s 2002 infrastructure replacement program and, additionally, to recover general increases in operating expenses. On January 31, 2003, the CPUC also approved SCW’s Advice Letter filed for the Region II 2003 infrastructure replacement program with rate increases of \$3.5 million annually, effective February 4, 2003.

Note 5 - Regulatory Matters (Continued):

Balancing Accounts:

As permitted by the CPUC, SCW has historically maintained water supply balancing accounts prior to November 29, 2001 and electric supply balancing accounts to account for under-collections and over-collections of revenues designed to recover such costs. Costs are 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 or through refunds of previously incurred costs. SCW accrues interest on its supply cost balancing accounts at the rate prevailing for 90-day commercial paper. CCWC does not maintain a supply cost balancing account.

Water Balancing Account – On November 29, 2001, the CPUC ordered water utilities with existing water supply balancing accounts to cease booking amounts to such accounts. In its place, water utilities are now required to establish a memorandum supply cost account. The over- or under-collection of water supply costs is recorded in this memorandum account in a manner similar to the balancing account. The income statements of SCW will no longer include entries reflecting differences between authorized water supply unit costs included in rates and actual water supply costs. As a result, any changes in water supply costs as well as any future authorized revenue increases for supply expenses may directly impact earnings.

In a decision issued on June 19, 2003 related to the memorandum supply cost account, the CPUC concluded that (i) if a utility is within its 3-year rate case cycle and does not earn in excess of its authorized rate of return, the utility is entitled to recover its costs in the memorandum supply cost account, subject to a reasonableness review by the CPUC; (ii) if a utility is either within or outside of its rate case cycle and earns in excess of its authorized rate-of-return, the utility's recovery of expenses from the memorandum supply cost account will be reduced by the amount exceeding the authorized rate-of- return, and (iii) a utility is required to seek review of under and over collections by filing an advice letter annually by March 31. Pursuant to the resolution, SCW filed advice letters on September 12, 2003 seeking recovery of an under-collected balance of \$2.6 million for the period November 29, 2001 through December 31, 2002. Upon receiving approval from the CPUC, SCW will recognize the authorized under-collected amount as supply cost balancing accounts on its books. As of September 30, 2003, SCW has an under-collection of approximately \$5.7 million in its memorandum supply cost account, including the \$2.6 million filed with the CPUC. SCW intends to file advice letters annually by March 31. Amounts included in the memorandum supply cost account are not capitalized until a rate order is received from the CPUC.

With respect to pre-November 29, 2001 water supply balancing accounts, SCW has a net under-collection position of \$2.2 million recorded at September 30, 2003. Of this amount, recovery of approximately \$2.1 million has been included in rates authorized on June 19, 2003. The remaining \$75,000 has been deferred to Region I's next rate case.

Note 5 - Regulatory Matters (Continued):

Electric Balancing Account – Electric power costs incurred by SCW’s Bear Valley Electric division continue to be charged to its electric supply cost balancing account. The under-collection in the electric balancing account is \$23.2 million at September 30, 2003. The CPUC has authorized SCW to collect a surcharge from its customers of 2.2¢ per kilowatt hour for a period of up to ten years to enable SCW to recover the under-collection. SCW sold 30,069,000, 98,041,000 and 131,874,000 kilowatt hours of electricity to its Bear Valley Electric division customers for the three, nine and twelve months ended September 30, 2003, respectively, and 30,815,000, 97,994,000 and 130,057,000 kilowatt hours for the comparable periods in 2002. SCW anticipates electricity sales to be sufficient during a ten year period for it to recover the amount of the under-collection. SCW is allowed to only include up to a weighted annual energy purchase cost of \$77 per MWh each year for 10 years in its electric supply cost balancing account. To the extent that actual weighted average annual cost for power purchased exceeds the \$77 per MWh amount, SCW will not be able to include these amounts in its balancing account and such amounts will be expensed. During the nine months ended September 30, 2003, approximately \$145,000 was expensed.

CCWC, subject to regulation by the Arizona Corporation Commission (ACC), does not maintain balancing accounts and increases in costs are normally expensed as incurred and recovered through adjustments in general rate case applications.

Note 6 - New Accounting Pronouncements:

Effective January 1, 2003, Registrant adopted SFAS No. 143, “*Accounting for Asset Retirement Obligations*”, which requires businesses to record the fair value of a liability for an asset retirement obligation in the period in which it is incurred. When the liability is initially recorded, the entity capitalizes a cost by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the liability, an entity either settles the obligation for its recorded amount or incurs a gain or loss upon settlement. Registrant’s legal obligations for retirement reflect principally the retirement of wells, which by law need to be destroyed and filled at the time of removal. As such, the regulated subsidiaries of AWR incur asset retirement obligations. Retirement cost has historically been recovered through rates at the time of retirement. Accordingly, at implementation of SFAS No. 143, the cumulative effect has been reflected as a regulatory asset. Registrant will also reflect the gain or loss at settlement as a regulatory asset or liability on the balance sheet.

Upon adoption of SFAS No. 143 on January 1, 2003, Registrant recorded the fair value of the asset retirement obligation of \$13.2 million at its net present value of \$2.7 million, increased depreciable assets by \$0.4 million for asset retirement costs, increased regulatory assets by \$2.5 million and increased accumulated depreciation by \$0.2 million. Amounts recorded under SFAS No. 143 are subject to various assumptions and determinations, such as determining whether a legal obligation exists to remove assets, and estimating the fair value of the costs of removal, when final removal will occur and the credit-adjusted risk-free interest rates to be utilized on discounting future liabilities. Changes that may arise over time with regard to these assumptions will change amounts recorded in the future. The following is a reconciliation of the beginning and ending aggregate carrying amount of the asset retirement obligations (“ARO”):

Note 6 - New Accounting Pronouncements (Continued):

Nine Months Ended September 30, 2003

	Balance at Adoption January 1, 2003	Liabilities Incurred	Liabilities Settled	Accretion	Balance At September 30, 2003
ARO	\$2,718,079	60,000	—	160,314	\$2,938,393

In April 2003, the Financial Accounting Standards Board (FASB) issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities". This Statement amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities under SFAS 133, "Accounting for Derivative Instruments and Hedging Activities". This Statement is effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003. All provisions of this Statement will be applied prospectively. Registrant has not entered into or modified any contracts or designated any hedging relationships after June 30, 2003. This Statement also requires that any financing element of a derivative contract should be included in cash flows from financing activities in the Statement of Cash Flows. For the nine months ended September 30, 2003, Registrant has reflected in its Statement of Cash Flows approximately \$1.5 million of cash received related to the financing portion of the purchased power contracts with Pinnacle West.

In June 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity". This Statement specifies that instruments within its scope embody obligations of the issuer and that, therefore, the issuer must classify them as liabilities. This Statement was effective July 1, 2003. Registrant does not have any financial instruments with characteristics of both liabilities and equity.

Note 7 – Contingencies

SCW has been named as a defendant in twenty two lawsuits that allege that SCW and other water utilities, delivered unsafe water to their customers. Plaintiffs in these actions 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. Nineteen of the lawsuits involve customer service areas located in Los Angeles County in the southern portion of California; three of the lawsuits involve a customer service area located in Sacramento County in northern California. On September 1, 1999, the Court of Appeal in San Francisco held that the CPUC had preemptive jurisdiction over regulated public utilities and ordered dismissal of a series of these lawsuits. On October 11, 1999, one group of plaintiffs appealed the decision to the California Supreme Court.

On February 4, 2002, the California Supreme Court concluded that (i) the CPUC had preemptive jurisdiction over claims seeking injunctive relief and claims based on the theory that a public utility regulated by the CPUC provided unsafe drinking water even though it had complied with federal and state drinking water standards, but (ii) the CPUC did not have preemptive jurisdiction over damage claims alleging violations of federal and state drinking water standards by public utilities regulated by the CPUC. As a result, damage claims based on allegations of violations of federal and state drinking water standards may proceed while the other claims must be dismissed. In light of the breadth of plaintiffs' claims, the lack of factual information regarding plaintiffs' claims and injuries, if any, the impact of the California Supreme Court decision on plaintiffs' claims 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 claims based on allegations of violation of federal and state drinking water standards.

Note 7 – Contingencies (Continued)

On October 25, 1999, SCW sued Aerojet-General Corporation (Aerojet) for causing the contamination of the Sacramento County Groundwater Basin servicing SCW wells. A cross complaint in 2000 filed by Aerojet against SCW for negligence and constituting a public nuisance was dismissed by the court in October 2002. On October 10, 2003 Registrant entered into a confidential memorandum of understanding with the Aerojet-General subsidiary of GenCorp, Inc. for the settlement of legal actions brought by SCW. The memorandum of understanding outlines the present financial terms of a settlement. A final settlement agreement incorporating the terms of the memorandum of understanding is underway and being negotiated at the date of this filing. As the parties continue to address issues related and additional to the memorandum of understanding, certain disagreements have developed. The parties continue to negotiate in an attempt to resolve those issues. However, no complete, documented agreement has been reached and it is presently impossible to predict when a final settlement of all issues will be reached.

In a separate case, also filed on October 25, 1999, SCW filed a lawsuit against the State of California and its State Water Resources Control Board, Central Valley Regional Water Quality Control Board, and Department of Toxic Substances Control (collectively, the State) alleging that the State had substantially participated in a project to inject chemical pollution into portions of the Sacramento County Groundwater Basin and that pollution is progressively destroying the groundwater supply in SCW's Rancho Cordova water system. SCW and the State have entered into a comprehensive \$2,475,000 settlement for all of SCW's claims against the State, contingent upon the court's approval of the good faith of the settlement, which Registrant received in full during the third quarter of 2003.

The CPUC has authorized memorandum accounts to allow for recovery, from customers, of costs incurred by SCW in prosecuting the cases against the State and Aerojet, less any recovery from the defendants or others. As of September 30, 2003, approximately \$14.9 million has been recorded as Other Deferred Charges. The CPUC has authorized SCW to increase rates, effective April 28, 2001, for recovery over a six-year period of approximately \$1.8 million, in expenses that were incurred on or before August 31, 2000. SCW has filed to replace the current six year amortization to reflect the current memorandum account balance, net of any reimbursement amount, and maintain a long-term amortization period in the abbreviated general rate case application for its Region I. Management believes these costs are recoverable but cannot give assurance that the CPUC will ultimately allow recovery of all or any of the remaining costs through rates. As previously mentioned, SCW has entered into a confidential memorandum agreement with Aerojet pending final negotiations and the necessary approvals. It is management's intention to offset any settlement that may occur from these actions against the balance in the memorandum accounts at the time of settlement.

The compound MTBE has been detected in a well serving SCW's Los Osos water system. For some time, SCW has been working with the Regional Water Quality Control Board as well as the owner of a gas service station. Although the owner of the service station has attempted remediation with funds provided through the California Underground Storage Tank Fund ("CUSTF"), it appears there will be insufficient funds from the CUSTF to complete remediation sufficient to return the well to service. In order to prevent the running of the statute of limitations, on August 12, 2002 SCW filed suit in the Superior Court of the State of California for the County of San Luis Obispo against the operators and owners of the service station facility, and Chevron USA Products, Inc., the supplier. A settlement with Chevron has been reached and a filing has been made for dismissal by the Court. The impacted well may need to be removed permanently from service and the settlement with Chevron is expected to afford SCW sufficient funds to commence siting and construction of a replacement well.

Note 7 – Contingencies (Continued)

Volatile Organic Compounds (VOC) and perchlorate have been detected in two wells servicing SCW's San Gabriel System. SCW filed suit, along with two other affected water purveyors and the San Gabriel Basin Water Quality Authority (WQA), in the federal court against some of those responsible for the contamination. Some of the other potential defendants settled with SCW, other water purveyors and the WQA on VOC related issues, prior to the filing of the lawsuit. In response to the filing of the Federal lawsuit, the Potentially Responsible Party (PRP) defendants filed motions to dismiss the suit or strike certain portions of the suit. The judge issued a ruling on April 1, 2003 granting in part and denying in part the defendant's motions. A key ruling of the court was that the water purveyors, including the Registrant, by virtue of their ownership of wells contaminated with hazardous chemicals are themselves PRPs under the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA). Registrant amended its suit to claim certain affirmative defenses as an "innocent" party under CERCLA. Registrant is presently unable to predict the outcome of this ruling on its ability to fully recover from the PRPs future costs associated with the treatment of these wells.

On August 29, 2003, the US Environmental Protection Agency issued Unilateral Administrative Orders (UAO) against 41 parties deemed responsible for polluting the groundwater in that portion of the San Gabriel Valley from which SCW's two impacted wells draw water. SCW was not named as a party to the UAO. The UAO requires that these parties remediate the contamination. As a result of the issuance of the UAO, these parties have begun settlement discussions regarding the Federal lawsuits with SCW, the other two affected water purveyors and WQA. Registrant is presently unable to predict the ultimate outcome of these settlement discussions.

SCW has been, in conjunction with the Southern California Edison (Edison) unit of Edison International, planning to upgrade transmission facilities to 115kv (the 115kv Project) in order to meet increased energy and demand requirements for SCW's Bear Valley Electric service area. On December 27, 2000, SCW filed a lawsuit against Edison for declaratory relief and seeking damages for breach of contract as a result of delays in the 115kv Project as well as for violations of good faith and fair dealing, negligent misrepresentation, intentional misrepresentation and unjust enrichment. Subsequently, Edison filed a cross-complaint against SCW for breach of contract, anticipatory breach, and quantum meruit. To date, SCW has spent approximately \$3.0 million in this matter, all of which has been expensed. SCW has attended two mediation meetings with Edison in this matter, and is discussing a settlement proposal. The parties have not, however, yet reached a mutually agreeable definitive settlement of the issues.

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, where doing so is in the public interest. In addition, however, the laws of the State of California also provide: (1) that the owner of the utility property may contest whether the condemnation is actually in the public interest; and (2) that the owner is entitled to receive the fair market value of its property if the property is ultimately taken. Although the City of Claremont, California located in SCW's Region III has not initiated the formal condemnation process pursuant to California law, the City has authorized the hiring of a consultant to perform an appraisal of the value of Registrant's water system serving that city. SCW intends to vigorously defend itself against any condemnation action initiated by the City.

Registrant is also subject to ordinary routine litigation incidental to its business. Other than those disclosed above, no other legal proceedings are pending, which are believed to be material. Management believes that proper insurance coverage and reserves are in place to insure against property, general liability and workers' compensation claims incurred in the ordinary course of business.

Note 8 – Business Segments:

AWR has three principal business units: water and electric distribution units, through its SCW subsidiary, a water service utility operation conducted through its CCWC unit, and a non-regulated activity unit through the ASUS subsidiary. All activities of SCW currently are geographically located within California. All activities of CCWC are located in the state of Arizona. Both SCW and CCWC are regulated utilities. On a stand-alone basis, AWR has no material assets other than its investments in its subsidiaries. The tables below set forth information relating to SCW's water and electric operating segments, CCWC, and non-regulated businesses, consisting of ASUS and AWR corporate expenses. Included in the amounts set forth, certain assets, revenues and expenses have been allocated. The identifiable assets are net of respective accumulated provisions for depreciation. Capital additions reflect capital expenditures paid in cash and exclude property installed by developers and conveyed to Registrant.

	(dollars in thousands)					
	As Of And For The Three Months Ended September 30, 2003					
	SCW		CCWC Water	Non- Regulated	Eliminations	Consolidated AWR
Water	Electric					
Operating revenues	\$ 55,777	\$ 5,906	\$ 1,818	\$ 245	(\$21)	\$ 63,725
Operating income (loss) before income taxes	16,989	(420)	548	(1,023)		16,094
Interest expense, net	3,923	350	121	117		4,511
Identifiable assets	521,327	32,901	30,045	99		584,372
Depreciation expense	4,317	392	230	5		4,944
Capital additions	9,395	6,235	815	4		16,449

	(dollars in thousands)					
	As Of And For The Three Months Ended September 30, 2002					
	SCW		CCWC Water	Non- Regulated	Eliminations	Consolidated AWR
Water	Electric					
Operating revenues	\$ 54,052	\$ 5,529	\$ 1,814	\$ 217		\$ 61,612
Operating income (loss) before income taxes	16,452	547	578	(506)		17,071
Interest expense, net	3,789	338	112	143		4,382
Identifiable assets	502,402	27,402	28,573	16		558,393
Depreciation expense	4,019	368	235	—		4,622
Capital additions	10,957	434	230	15		11,636

	(dollars in thousands)					
	As Of And For The Nine Months Ended September 30, 2003					
	SCW		CCWC Water	Non- Regulated	Eliminations	Consolidated AWR
Water	Electric					
Operating revenues	\$138,636	\$18,263	\$ 4,632	\$ 749	(\$62)	\$162,218
Operating income (loss) before income taxes	35,990	456	1,031	(2,624)		34,853
Interest expense, net	11,785	1,050	363	417		13,615
Identifiable assets	521,327	32,901	30,045	99		584,372
Depreciation expense	12,965	1,175	690	6		14,836
Capital additions	24,360	7,614	1,893	37		33,904

Note 8 - Business Segments (Continued):

(dollars in thousands)	As Of And For The Nine Months Ended September 30, 2002					
	SCW					Consolidated AWR
	Water	Electric	CCWC Water	Non- Regulated	Eliminations	
Operating revenues	\$138,854	\$14,574	\$ 4,868	\$ 603		\$158,899
Operating income (loss) before income taxes	41,457	599	1,500	(1,533)		42,023
Interest expense, net	11,300	1,007	359	447		13,113
Identifiable assets	502,402	27,402	28,573	16		558,393
Depreciation expense	11,935	1,103	690	—		13,728
Capital additions	30,284	1,401	613	15		32,313

(dollars in thousands)	As Of And For The Twelve Months Ended September 30, 2003					
	SCW					Consolidated AWR
	Water	Electric	CCWC Water	Non- Regulated	Eliminations	
Operating revenues	\$180,685	\$24,988	\$ 5,921	\$ 991	(\$62)	\$212,523
Operating income (loss) before income taxes	42,511	3,024	1,277	(3,386)		43,426
Interest expense, net	15,761	1,404	486	550		18,201
Identifiable assets	521,327	32,901	30,045	99		584,372
Depreciation expense	16,945	1,542	917	6		19,410
Capital additions	32,657	7,120	2,380	89		42,246

(dollars in thousands)	As Of And For The Twelve Months Ended September 30, 2002					
	SCW					Consolidated AWR
	Water	Electric	CCWC Water	Non- Regulated	Eliminations	
Operating revenues	\$180,746	\$18,885	\$ 6,398	\$ 813		\$206,842
Operating income (loss) before income taxes	53,778	(3,119)	1,790	(1,540)		50,909
Interest expense, net	14,643	1,305	532	607		17,087
Identifiable assets	502,402	27,402	28,573	16		558,393
Depreciation expense	15,751	1,464	1,001	—		18,216
Capital additions	42,017	1,775	683	15		44,490

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operation

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 Registrant "believes," "anticipates," "expects" or words of similar import. Similarly, statements that describe Registrant'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, SCW's ability to recover electric and water supply costs from ratepayers, liquidity and capital resources, and accounting matters. Actual results in each case could differ materially from those currently anticipated in such statements, by reason of factors such as changes in utility regulation, including ongoing local, state and federal activities; future economic conditions, including changes in customer demand and changes in water and energy supply cost; future climatic conditions; and legislative, regulatory and other circumstances affecting anticipated revenues and costs. See the section entitled "*Risk Factors*" for more information.

General

American States Water Company (AWR), incorporated in 1998, is engaged in the business of holding, for investment, the stock primarily of utility companies. AWR's principal investment is the stock of SCW. SCW is a California 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 Public Utilities Commission of the State of California (CPUC) and was incorporated on December 31, 1929. SCW is organized into one electric customer service area and three water service 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 4 customer service areas located in Los Angeles County; Region III incorporates 10 water customer service areas in eastern Los Angeles County, and in Orange, San Bernardino and Imperial counties. SCW also provides electric service to the City of Big Bear Lake and surrounding areas in San Bernardino County through its Bear Valley electric service division.

SCW served 249,810 water customers and 22,199 electric customers at September 30, 2003, or a total of 272,009 customers, compared with 268,057 total customers at September 30, 2002.

SCW's utility operations exhibit seasonal trends. Although SCW's water utility operations have a diversified customer base, residential and commercial customers account for the majority of SCW's water sales and revenues. Revenues derived from commercial and residential water customers accounted for approximately 86.4%, 88.9% and 91.1% of total water revenues for the three, nine and twelve months ended September 30, 2003, respectively, as compared to 87.8%, 89.0% and 91.2% for the three, nine and twelve months ended September 30, 2002, respectively.

AWR also owns two other subsidiaries. American States Utility Services, Inc. (ASUS) was formed to lease, operate and maintain water and wastewater systems owned by others and to provide related services, such as billing and meter reading. ASUS currently provides related services to approximately 91,500 accounts. Chaparral City Water Company (CCWC) is an Arizona public utility company serving 12,067 customers as of September 30, 2003, compared with 11,683 customers at September 30, 2002, in the town of Fountain Hills, Arizona and a portion of the City of Scottsdale, Arizona. The majority of CCWC's customers are residential. The Arizona Corporation Commission (ACC) regulates CCWC.

Neither AWR nor ASUS is directly regulated by either the CPUC or the ACC.

Introduction

As described in Note 2 to the accompanying consolidated financial statements, Registrant has restated its financial statements for the twelve months ended September 30, 2002. In connection with a deferred tax analysis of Registrant's tax accounts performed in 2002, Registrant determined that it had miscalculated its net accumulated deferred income taxes and current tax payable account over several years, resulting in taxes on income not being recognized in the proper period, and overstating Registrant's net deferred tax liabilities and current taxes payable. Registrant further determined that the amount of the overstatements, which totaled approximately \$4.7 million and \$4.9 million as of December 31, 2001 for AWR and SCW, respectively, arose in prior years and prior years' financial statements should be restated. The financial information for the twelve months ended September 30, 2002 included in these consolidated financial statements has been adjusted to give effect to the restatement. Although the total amount of the restatement was \$4.9 million to AWR as of December 31, 2001, the impact to the twelve months ended September 30, 2002 of this restatement was to increase taxes on income and decrease net income by \$70,000. Basic and diluted earnings per share decreased \$0.01 for the twelve months ended September 30, 2002 as a result of the restatement.

Results of Operation**RESULTS OF THIRD QUARTER 2003 OPERATIONS**

	3 MOS ENDED 9/30/03	3 MOS ENDED 9/30/02	\$ CHANGE	% CHANGE
OPERATING REVENUES				
Water	\$57,574	\$55,866	\$ 1,708	3.1%
Electric	5,906	5,529	377	6.8%
Other	245	217	28	12.9%
	<u>63,725</u>	<u>61,612</u>	<u>2,113</u>	<u>3.4%</u>
OPERATING EXPENSES				
Water purchased	13,740	14,205	(465)	-3.3%
Power purchased for pumping	3,330	3,327	3	0.1%
Power purchased for resale	3,382	3,645	(263)	-7.2%
Unrealized loss on purchased power contracts	420	—	420	100.0%
Groundwater production assessment	2,089	1,831	258	14.1%
Supply cost balancing accounts	650	(428)	1,078	251.9%
Other operating expenses	4,805	4,883	(78)	-1.6%
Administrative and general expenses	10,058	7,848	2,210	28.2%
Depreciation and amortization	4,944	4,622	322	7.0%
Maintenance	2,181	2,546	(365)	-14.3%
Taxes on income	3,915	5,207	(1,292)	-24.8%
Other taxes	2,032	2,062	(30)	-1.5%
	<u>51,546</u>	<u>49,748</u>	<u>1,798</u>	<u>3.6%</u>
Operating income	<u>12,179</u>	<u>11,864</u>	<u>315</u>	<u>2.7%</u>
OTHER INCOME (LOSS) - NET	<u>128</u>	<u>157</u>	<u>(29)</u>	<u>-18.5%</u>
INTEREST CHARGES	<u>4,511</u>	<u>4,382</u>	<u>129</u>	<u>2.9%</u>
NET INCOME	<u>\$ 7,796</u>	<u>\$ 7,639</u>	<u>\$ 157</u>	<u>2.1%</u>

Table of Contents

Third quarter net income increased 2.1% to \$7.8 million, equivalent to \$0.51 per common share on a basic and fully diluted basis, compared to \$7.6 million or \$0.50 per share earned in 2002's third quarter.

Operating Revenues

For the three months ended September 30, 2003, revenues from water operations increased 3.1% to \$57.6 million compared to \$55.9 million for the three months ended September 30, 2002. The increase was due to two rate increases for SCW's Region II that were effective on January 21, 2003 and February 4, 2003, respectively. These two rate increases are expected to generate additional revenues of approximately \$6.2 million annually. The rate increases were offset by a 2.8% decrease in water consumption resulting from wetter and cooler temperatures in most of SCW's service areas. Differences in temperature and rainfall in Registrant's service areas impact sales of water to customers causing fluctuations in Registrant's revenues and earnings between comparative periods.

For the three months ended September 30, 2003, revenues from electric operations increased by 6.8% to \$5.9 million compared to \$5.5 million for the three months ended September 30, 2002. The increase reflects rate increases authorized by the CPUC at the end of July 2002, which subsequently became effective, to cover purchased power costs under various power supply agreements. Offsetting the increase was kilowatt-hour sales decreasing by 2.4%.

Operating Expenses

For the three months ended September 30, 2003, purchased water costs decreased by 3.3% to \$13.7 million compared to \$14.2 million for the three months ended September 30, 2002. The decrease was primarily due to a decrease in the costs of leased water rights to pump in SCW's Region II and an adjustment of approximately \$350,000 to decrease purchased water in SCW's Orange County customer service area due to the in-lieu program. The in-lieu program has been implemented by the Metropolitan Water District of Southern California (MWD) to help preserve groundwater level in the areas, which allows SCW to purchase treated water from MWD essentially at SCW's groundwater pumping cost. The decreases are partially offset by additional purchased water volume necessary during the third quarter of 2003 to replace pumped water supply lost due to wells being temporarily removed from service as a result of water quality issues and mechanical problems. For the three months ended September 30, 2003, 47% of our supply mix was purchased water as compared to 46% purchased for the three months ended September 30, 2002.

For the three months ended September 30, 2003, cost of power purchased for pumping increased slightly by 0.1% to \$3.33 million compared to \$3.32 million for three months ended September 30, 2002.

For the three months ended September 30, 2003, cost of power purchased for resale to customers in SCW's Bear Valley Electric division decreased by 7.2% to \$3.4 million compared to \$3.6 million for the three months ended September 30, 2002. The decrease is primarily due to lower power costs at a price of \$74.65 per megawatt hour (MWh) effective November 2002 under SCW's power supply agreements with Pinnacle West Capital Corporation (PWCC) as compared to \$95 per MWh for energy purchased from Mirant Americas Energy Marketing, LP (Mirant) under then existing contracts in the same period of 2002.

The entry for unrealized gain and loss on purchased power contracts represents gains and losses recorded for SCW's power purchase agreements, with PWCC, which qualify as derivative instruments under Statement of Financial Accounting Standards (SFAS) No. 133, "*Accounting for Derivative Instruments and Hedging Activities*". The \$420,000 pre-tax unrealized loss for the three months ended September 30, 2003 is due to decreases in current forward market prices. This results in an increase in SCW's cumulative unrealized loss on these contracts which totaled \$1.7 million as of September 30, 2003. There is no cash flow impact from these gains and losses. Management is evaluating alternatives to

Table of Contents

minimize future unrealized losses. Unrealized gains and losses at Bear Valley Electric will continue to impact earnings during the life of the contract with PWCC. Management expects there to be no cumulative impact on SCW's Bear Valley electric division earnings at the end of the contract period, in 2008.

For the three months ended September 30, 2003, groundwater production assessments increased by 14.1% to \$2.1 million compared to \$1.8 million for the three months ended September 30, 2002 due primarily to increases in assessment rates levied against groundwater production effective July 2003 and an adjustment to increase pumped cost resulting from the in-lieu program as mentioned previously under purchased water.

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. An increase in the provision of supply cost balancing accounts of \$1.1 million for the three months ended September 30, 2003 when compared to the three months ended September 30, 2002, primarily reflects new rates authorized in July of 2002 to recover electric power costs at SCW's Bear Valley electric division. At September 30, 2003, Registrant had a combined net under-collected position of \$25.4 million in both its water and electric supply balancing accounts due primarily to the previous increases in energy costs.

For the three months ended September 30, 2003, other operating expenses decreased by 1.6% to \$4.8 million compared to \$4.9 million for the three months ended September 30, 2002. The decrease was due primarily to lower chemicals and water treatment costs.

For the three months ended September 30, 2003, administrative and general expenses increased by 28.2% to \$10.1 million compared to \$7.8 million for the three months ended September 30, 2002. The increase was due primarily to (i) a \$745,000 increase in outside consulting and legal services in connection with new business development primarily related to privatization of water and wastewater systems at various military bases, and the Edison lawsuit for Bear Valley Electric, (ii) higher labor cost, and (iii) approximately \$373,000 increase in pensions and benefits due to actuarial assumption changes in the discount rate and expected long-term rate of return on plan assets, and increases in various benefit costs.

For the three months ended September 30, 2003, depreciation expense increased by 7.0% to \$4.9 million compared to \$4.6 million for the three months ended September 30, 2002. The increase reflects, among other things, the effects of recording approximately \$51 million in utility plant during 2002, depreciation on which began in January 2003.

For the three months ended September 30, 2003, maintenance expense decreased by 14.3% to \$2.2 million compared to \$2.5 million due principally to costs of approximately \$408,000 incurred in connection with the trucking of water in SCW's Wrightwood customer service area due to a sudden and unexplained drop in groundwater levels in the area during the early part of the third quarter of 2002. There were no comparable costs during the three months ended September 30, 2003.

For the three months ended September 30, 2003, taxes on income decreased by 24.8% to \$3.9 million compared to \$5.2 million for the three months ended September 30, 2002 due primarily to a decrease in the estimated effective rate, the effects of flow-through adjustments, and lower pre-tax operating income.

For the three months ended September 30, 2003, other taxes decreased slightly by 1.5% to \$2 million compared to \$2.1 million for the three months ended September 30, 2002 reflecting decreases in property taxes at Registrant's Arizona facility due to an adjustment based on actual property tax statements.

[Table of Contents](#)**Other Income (Loss)**

For the three months ended September 30, 2003, other income decreased by 18.5% to \$128,000 net income compared to a net income of \$157,000 for the three months ended September 30, 2002 reflecting increases in taxes and expenses associated with SCW's 500 acre foot entitlement to water from the State Water Project.

Interest Charges

For the three months ended September 30, 2003, interest expense increased by 2.9% to \$4.5 million compared to \$4.4 million for the three months ended September 30, 2002 due primarily to higher short-term borrowings incurred to finance capital expenditures.

RESULTS OF NINE MONTHS ENDED SEPTEMBER 30, 2003

	9 MOS ENDED 9/30/03	9 MOS ENDED 9/30/02	\$ CHANGE	% CHANGE
OPERATING REVENUES				
Water	\$143,206	\$143,722	\$ (516)	-0.4%
Electric	18,263	14,574	3,689	25.3%
Other	749	603	146	24.2%
Total operating revenues	162,218	158,899	3,319	2.1%
OPERATING EXPENSES				
Water purchased	32,098	32,523	(425)	-1.3%
Power purchased for pumping	7,696	7,767	(71)	-0.9%
Power purchased for resale	10,052	13,973	(3,921)	-28.1%
Unrealized gain on purchased power contracts	(854)	—	(854)	-100.0%
Groundwater production assessment	5,485	5,427	58	1.1%
Supply cost balancing accounts	2,109	(6,243)	8,352	133.8%
Other operating expenses	13,931	12,811	1,120	8.7%
Administrative and general expenses	29,472	24,291	5,181	21.3%
Depreciation and amortization	14,836	13,728	1,108	8.1%
Maintenance	6,430	6,632	(202)	-3.0%
Taxes on income	7,700	12,355	(4,655)	-37.7%
Other taxes	6,110	5,967	143	2.4%
Total operating expenses	135,065	129,231	5,834	4.5%
Operating income	27,153	29,668	(2,515)	-8.5%
OTHER INCOME (LOSS) - NET	159	326	(167)	-51.2%
INTEREST CHARGES	13,615	13,113	502	3.8%
NET INCOME	\$ 13,697	\$ 16,881	\$(3,184)	-18.9%

Net income for the nine months ended September 30, 2003 decreased 18.9% to \$13.7 million, equivalent to \$0.90 per common share on a basic and fully diluted basis, compared to \$16.9 million or \$1.11 per share for the nine months ended September 30, 2002.

Operating Revenues

For the nine months ended September 30, 2003, revenues from water operations decreased slightly by 0.4% to \$143.2 million compared to \$143.7 million for the nine months ended September 30, 2002. The decrease was due to a 4.7% decrease in water consumption resulting from wetter and cooler temperatures in most of SCW's service areas, offset by two rate increases for SCW's Region II that were effective on January 21, 2003 and February 4, 2003, respectively. As mentioned earlier, these two rate increases are expected to generate additional water revenues of approximately \$6.2 million annually. Differences in temperature and rainfall in Registrant's service areas impact sales of water to customers causing fluctuations in Registrant's revenues and earnings between comparative periods.

For the nine months ended September 30, 2003, revenues from electric operations increased by 25.3% to \$18.3 million compared to \$14.6 million for the nine months ended September 30, 2002. The increase reflects rate increases in July 2002 authorized by the CPUC to cover purchased power costs under various power supply agreements.

Operating Expenses

For the nine months ended September 30, 2003, purchased water costs decreased slightly by 1.3% to \$32.1 million compared to \$32.5 million for the nine months ended September 30, 2002. These results reflect a 4.7% decrease in water consumption, offset by an increase in the costs of water rights pumped in SCW's Region II. For the nine months ended September 30, 2003, 45% of our supply mix was purchased water as compared to 44% purchased water for the nine months ended September 30, 2002.

For the nine months ended September 30, 2003, cost of power purchased for pumping decreased slightly by 0.9% to \$7.7 million compared to \$7.8 million for the nine months ended September 30, 2002 due to lower consumption and additional wells down for maintenance and water quality issues. The effect of wells being offline was partially offset by increased power rates.

For the nine months ended September 30, 2003, cost of power purchased for resale to customers in SCW's Bear Valley Electric division decreased by 28.1% to \$10.1 million compared to \$14.0 million for nine months ended September 30, 2002. This significant decrease is due primarily to (i) lower power costs at a price of \$74.65 per megawatt hour (MWh) effective November 2002 under SCW's power supply agreements with PWCC as compared to \$95 per MWh for energy purchased from Mirant under then existing contracts in the same period of 2002, and (ii) additional accruals of \$2.2 million for purchased power costs based on adjusted invoices received in April of 2002 from Dynegy for purchased power incurred during prior periods. There were no comparable accruals during the nine months ended September 30, 2003.

The \$854,000 pre-tax unrealized gain on purchased power contracts for the nine months ended September 30, 2003 is due to an increase in the current forward market prices since December 31, 2002. There is no cash flow impact from the gains and losses on the purchased power contracts.

For the nine months ended September 30, 2003, groundwater production assessments increased by 1.1% to \$5.5 million compared to \$5.4 million for the nine months ended September 30, 2002 due primarily to increases in assessment rates levied against groundwater production effective July 2003.

An increase of \$8.4 million during the nine months ended September 30, 2003 in the provision for supply cost balancing accounts when compared to the nine months ended September 30, 2002 primarily reflects new rates authorized in 2002 to recover electric power costs, and additional accruals of \$2.2 million for purchased power costs recorded in April 2002 as discussed under power purchased for resale.

Table of Contents

For the nine months ended September 30, 2003, other operating expenses increased by 8.7% to \$13.9 million compared to \$12.8 million for the nine months ended September 30, 2002 due primarily to (i) higher labor costs which increased by almost \$670,000, (ii) approximately \$165,000 of refunds for a sewer service overpayment in June 2002 for which there was no counterpart in 2003; and (iii) reimbursements totaling \$205,000 received during the nine months ended September 30, 2002 from settling parties for expenses incurred in the San Gabriel basin to meet water quality standards for which there was no counterpart in 2003.

For the nine months ended September 30, 2003, administrative and general expenses increased by 21.3% to \$29.5 million compared to \$24.3 million for the nine months ended September 30, 2002 due primarily to (i) approximately \$3.6 million increase in outside legal and consulting services incurred in connection with new business development, most specifically in the area of privatization of water and wastewater systems at military bases, and in defense of the Edison lawsuit for Bear Valley Electric, (ii) the write-off of \$680,000 in legal costs incurred to obtain water storage rights in SCW's Central basin area due to an unfavorable court decision that will likely result in SCW's inability to obtain the rights, and (iii) approximately \$775,000 increase in pensions and benefits due to actuarial assumption changes in the discount rate and expected long-term rate of return on plan assets, and increases in various benefit costs.

For the nine months ended September 30, 2003, depreciation expense increased by 8.1% to \$14.8 million compared to \$13.7 million for the nine months ended September 30, 2002 reflecting, among other things, the effects of recording approximately \$51 million in utility plant during 2002, depreciation on which began in January 2003.

For the nine months ended September 30, 2003, maintenance expense decreased by 3.0% to \$6.4 million compared to \$6.6 million for the nine months ended September 30, 2002 due principally to costs of approximately \$408,000 incurred in connection with the trucking of water in SCW's Wrightwood customer service area due to a sudden and unexplained drop in groundwater levels in the area during the early part of the third quarter of 2002. There were no comparable costs during the nine months ended September 30, 2003.

For the nine months ended September 30, 2003, taxes on income decreased by 37.7% to \$7.7 million compared to \$12.4 million for nine months ended September 30, 2002 due primarily to lower pre-tax operating income and the effects of flow-through adjustments.

For the nine months ended September 30, 2003, other taxes increased by 2.4% to \$6.1 million compared to \$6.0 million for the nine months ended September 30, 2002 reflecting additional property taxes resulting from higher assessed values, and increases in payroll taxes based on increased labor costs.

Other Income (Loss)

For the nine months ended September 30, 2003, other income decreased to \$159,000 compared to \$326,000 for the nine months ended September 30, 2002. The net decrease reflects the sale of a parcel of non-operating property in Region II of SCW in the first quarter of 2002 for which there was a gain of approximately \$506,000, offset by the recording of certain non-regulated expenses to administrative and general expenses of ASUS, a non-regulated subsidiary, and a decrease in taxes.

[Table of Contents](#)**Interest Charges**

For the nine months ended September 30, 2003, interest expense increased by 3.8% to \$13.6 million compared to \$13.1 million for the nine months ended September 30, 2002 due primarily to higher short-term borrowings incurred to finance capital expenditures.

RESULTS OF TWELVE MONTHS ENDED SEPTEMBER 30, 2003

	12 MOS ENDED 9/30/03	12 MOS ENDED 9/30/02	\$ CHANGE	% CHANGE
OPERATING REVENUES				
Water	\$186,544	\$187,144	\$ (600)	-0.3%
Electric	24,988	18,885	6,103	32.3%
Other	991	813	178	21.9%
Total operating revenues	212,523	206,842	5,681	2.7%
OPERATING EXPENSES				
Water purchased	42,434	40,190	2,244	5.6%
Power purchased for pumping	10,506	10,565	(59)	-0.6%
Power purchased for resale	11,896	18,530	(6,634)	-35.8%
Unrealized loss on purchased power contracts	1,676	—	1,676	100.0%
Groundwater production assessment	7,474	7,150	324	4.5%
Supply cost balancing accounts	4,947	(9,444)	14,391	152.4%
Other operating expenses	18,103	16,939	1,164	6.9%
Administrative and general expenses	35,191	36,927	(1,736)	-4.7%
Depreciation and amortization	19,410	18,216	1,194	6.6%
Maintenance	9,636	9,206	430	4.7%
Taxes on income	8,293	14,228	(5,935)	-41.7%
Other taxes	7,824	7,654	170	2.2%
Total operating expenses	177,390	170,161	7,229	4.2%
Operating income	35,133	36,681	(1,548)	-4.2%
OTHER INCOME (LOSS) - NET	224	39	185	474.4%
INTEREST CHARGES	18,201	17,087	1,114	6.5%
NET INCOME	\$ 17,156	\$ 19,633	\$(2,477)	-12.6%

Net income for the twelve months ended September 30, 2003 decreased 12.6% to \$17.2 million, equivalent to \$1.13 per common share on a basic and fully diluted basis, compared to \$19.6 million or \$1.29 per share for the twelve months ended September 30, 2002.

Operating Revenues

For the twelve months ended September 30, 2003, revenues from water operations decreased slightly by 0.3% to \$186.5 million compared to \$187.1 million for the twelve months ended September 30, 2002. The decrease was due primarily to a decrease of 3.6% in water consumption, and the termination of a surcharge totaling approximately \$600,000, which was authorized to decrease the balancing account under-collection in SCW's Metropolitan customer service area. These decreases were offset by rate

Table of Contents

increases in Region II as discussed earlier, and step and attrition rate increases in the customer service areas that comprise SCW's Region I which were effective January 2002 and January 2003, respectively.

For the twelve months ended September 30, 2003, revenues from electric operations increased by 32.3% to \$24.9 million compared to \$18.9 million for the twelve months ended September 30, 2002. As discussed earlier, the increase reflects rate increases in July 2002 authorized by the CPUC to cover purchased power costs under various power supply agreements. In addition, there was an increase of 1.4% in kilowatt-hour consumption, primarily due to heavier use of snow making machines at ski resorts in the area in the fourth quarter of 2002.

Operating Expenses

For the twelve months ended September 30, 2003, purchased water costs increased by 5.6% to \$42.4 million compared to \$40.2 million for the twelve months ended September 30, 2002. The increase was due to an increase in purchased water volume resulting from additional purchased water necessary during the twelve months ended September 30, 2003 to replace pumped water supply lost due to wells being temporarily removed from service as a result of water quality issues and mechanical problems, particularly in SCW's Arden/Cordova and Foothill districts. For the twelve months ended September 30, 2003, 44% of the supply mix was purchased as compared to 43% purchased water for the twelve months ended September 30, 2002. In addition, the twelve-months ended September 30, 2003 include costs of approximately \$1.4 million, incurred in connection with the purchasing and trucking of water, in SCW's Wrightwood customer service area due to a sudden and unexplained drop in groundwater level in the area during the early part of the third quarter of 2002. The water hauling ended in January 2003.

For the twelve months ended September 30, 2003, cost of power purchased for pumping decreased slightly by 0.6% to \$10.5 million compared to \$10.6 million for the twelve months ended September 30, 2002 due to lower consumption and additional wells down for maintenance and water quality issues. The effect of wells being offline was partially offset by increased power rates. Additionally, a credit of \$440,000 recorded in the fourth quarter of 2001 for the sale of groundwater in the Chino Basin also impacted the twelve-month comparison. There was no similar credit in the comparable period of 2003.

For the twelve months ended September 30, 2003, cost of power purchased for resale to customers in SCW's Bear Valley Electric division decreased by 35.8% to \$11.9 million compared to \$18.5 million for the twelve months ended September 30, 2002. This significant decrease is due to (i) lower power costs at a price of \$74.65 per megawatt hour (MWh) effective November 2002 under SCW's power supply agreements with PWCC as compared to \$95 per MWh for energy purchased from Mirant under then existing contracts in the same period of 2002, (ii) additional accruals of \$2.2 million for purchased power costs based on adjusted invoices received in April of 2002 from Dynegy for purchased power incurred during prior periods; there were no comparable accruals during the twelve months ended September 30, 2003; and (iii) the reversal of an accrual totaling approximately \$2.2 million in October 2002 resulting from a settlement with Dynegy.

For the twelve months ended September 30, 2003, the \$1.7 million pre-tax unrealized loss on purchased power contracts resulted from the contract prices with PWCC being higher than current forward market prices. There is no cash flow impact of this loss.

For the twelve months ended September 30, 2003, groundwater production assessments increased by 4.5% to \$7.5 million compared to \$7.2 million for the twelve months ended September 30, 2002 due primarily to higher assessments levied against production for the water year 2002-2003 as compared with the previous year.

Table of Contents

An increase of \$14.4 million during the twelve months ended September 30, 2003 in the provision for supply cost balancing accounts when compared to the twelve months ended September 30, 2002 primarily reflects new rates and surcharges authorized in 2001 and 2002 to recover electric power costs and under-collection in the electric balancing account. Factors impacting power purchased for resale as previously discussed also impact the supply cost balancing accounts.

For the twelve months ended September 30, 2003, other operating expenses increased by 6.9% to \$18.1 million compared to \$16.9 million for the twelve months ended September 30, 2002 due primarily to higher water treatment costs and labor costs which increased by almost \$1 million.

For the twelve months ended September 30, 2003, administrative and general expenses decreased by 4.7% to \$35.2 million compared to \$36.9 million for the twelve months ended September 30, 2002 due primarily to the reversal of the remaining reserve of \$6.5 million in the fourth quarter of 2002 for potential non-recovery of electric power costs incurred to serve customers at SCW's Bear Valley Electric customer service area. The reserve was established in late 2001, which also impact the comparison between periods, to offset future impacts to earnings for the difference between authorized rates and SCW's actual electric power costs under its agreement with Mirant. The agreements SCW entered into with PWCC in September 2002 enable it to purchase power at a cost lower than that authorized by the CPUC, thereby removing the need for the reserve. The decrease was offset by an increase totaling approximately \$6.2 million in outside services primarily for new business development, legal costs incurred in defense of the Edison lawsuit for Bear Valley Electric, and legal costs for resolution of amounts charged under various power purchase contracts. In addition, there was an approximate \$1.6 million increase in pensions and benefits due to actuarial assumption changes in the discount rate and expected long-term rate of return on plan assets, and increases in various benefit costs. The twelve month comparison is also impacted by increased expenses related to privatization of water and wastewater systems at military bases.

For the twelve months ended September 30, 2003, depreciation expense increased by 6.6% to \$19.4 million compared to \$18.2 million for the twelve months ended September 30, 2002 reflecting, among other things, the effects of recording approximately \$51 million in utility plant during 2002, depreciation on which began in January 2003.

For the twelve months ended September 30, 2003, maintenance expense increased by 4.7% to \$9.6 million compared to \$9.2 million for the twelve months ended September 30, 2002 due principally to the termination of SCW's Cash Preservation Program ("CPP") in August 2002 following the CPUC's approval of rate increases permitting SCW to begin recovery of power costs incurred during the energy crisis of 2000-2001 to serve customers of its Bear Valley Electric division. The CPP was initially implemented in 2001 to control costs and temporarily limit capital and maintenance expenditures principally to those projects that were believed necessary to meet public safety and health requirements or otherwise provide for continued service. The CPP impacted both the electric and water businesses of SCW.

For the twelve months ended September 30, 2003, taxes on income decreased by 41.7% to \$8.3 million compared to \$14.2 million for the twelve months ended September 30, 2002 due primarily to lower pre-tax operating income and the effects of flow-through adjustments.

For the twelve months ended September 30, 2003, other taxes increased by 2.2% to \$7.8 million compared to \$7.7 million for the twelve months ended September 30, 2002 reflecting additional property taxes resulting from higher assessed values, and increases in payroll taxes based on increased labor costs.

Table of Contents

Other Income (Loss)

For the twelve months ended September 30, 2003, other income increased to \$224,000 compared to \$39,000 for the twelve months ended September 30, 2002 due to recording of certain non-regulated expenses to administrative and general expenses of ASUS, a non-regulated subsidiary which totaled approximately \$400,000, and the write-off of approximately \$312,000 in expenses associated with the termination of the acquisition of Peerless Water Co. in the fourth quarter of 2001. These increases were offset by the sale of a parcel of non-operating property in Region II of SCW in the first quarter of 2002 for which there was a gain of approximately \$506,000.

Interest Charges

For the twelve months ended September 30, 2003, interest expense increased by 6.5% to \$18.2 million compared to \$17.1 million for the twelve months ended September 30, 2002 due primarily to the issuance of \$50 million in long-term debt by SCW in December 2001.

Accounting for Supply Costs

As permitted by the CPUC, SCW has historically maintained water supply balancing accounts prior to November 29, 2001 and electric supply balancing accounts to account for under-collections and over-collections of revenues designed to recover such costs. Costs have been recorded in income and charged to balancing accounts when such costs were incurred. The balancing accounts were reversed when such costs were recovered through rate adjustments or through refunds of previously incurred costs. SCW accrued interest on its supply cost balancing accounts at the rate prevailing for 90-day commercial paper. CCWC does not maintain a supply cost balancing account.

On November 29, 2001, the CPUC ordered water utilities with existing water supply balancing accounts to cease booking amounts to such accounts. In its place, water utilities are now required to establish a memorandum supply cost account. The over- or under-collection of water supply costs is recorded in this memorandum account in a manner similar to the balancing account. However, the income statements of SCW no longer include entries reflecting differences between authorized water supply unit costs included in rates and actual water supply costs. As a result, any changes in water supply costs as well as any future revenue increases that may be authorized for supply expenses may directly impact earnings. SCW's basic earnings per share for the three, nine and twelve months ended September 30, 2003 were \$0.04, \$0.11 and \$0.22, respectively, less than they would have been if the November 2001 CPUC order had not been issued.

In a decision issued on June 19, 2003 related to the memorandum supply cost account, the CPUC concluded that (i) if a utility is within its 3-year rate case cycle and does not earn in excess of its authorized rate of return, the utility is entitled to recover its costs in the memorandum supply cost account, subject to a reasonableness review by the CPUC; (ii) if a utility is either within or outside of its rate case cycle and earns in excess of its authorized rate-of-return, the utility's recovery of expenses from the memorandum supply cost account will be reduced by the amount exceeding the authorized rate-of- return, and (iii) a utility is required to seek review of under and over collections by filing an advice letter annually by March 31. Pursuant to the resolution, SCW filed advice letters on September 12, 2003 seeking recovery of an under-collected balance of \$2.6 million for the period November 29, 2001 through December 31, 2002. Upon receiving approval from the CPUC, SCW will recognize the authorized under-collected amount as supply cost balancing accounts on its books. As of September 30, 2003, SCW had an under-collection of approximately \$5.7 million in its memorandum supply cost account, including the \$2.6 million filed with the CPUC. SCW intends to file advice letters annually by March 31. Amounts included in the memorandum supply cost account are not capitalized until a rate order is received from the CPUC.

Table of Contents

With respect to pre-November 29, 2001 water supply balancing accounts, SCW has a net under-collection position of \$2.2 million recorded at September 30, 2003. Of this amount, recovery of approximately \$2.1 million has been included in rates authorized on June 19, 2003. The remaining \$75,000 has been deferred to Region I's next rate case.

Electric power costs incurred by SCW's Bear Valley Electric division continue to be charged to its electric supply cost balancing account. The under-collection in the electric balancing account is \$23.2 million at September 30, 2003. The CPUC has authorized SCW to collect a surcharge from its customers of 2.2¢ per kilowatt hour for a period of up to ten years to enable SCW to recover the under-collection. SCW sold 30,069,000, 98,041,000 and 131,874,000 kilowatt hours of electricity to its Bear Valley Electric division customers for the three, nine and twelve months ended September 30, 2003, respectively, and 30,815,000, 97,994,000 and 130,057,000 kilowatt hours for the comparable periods in 2002. SCW anticipates electricity sales to be sufficient during a ten year period for it to recover the amount of the under-collection. SCW is allowed to only include up to a weighted annual energy purchase cost of \$77 per MWh each year for 10 years in its electric supply cost balancing account. To the extent that actual weighted average annual cost for power purchased exceeds the \$77 per MWh amount, SCW will not be able to include these amounts in its balancing account and such amounts will be expensed. During the nine months ended September 30, 2003, approximately \$145,000 was expensed. For further information, see the sections entitled "Regulatory Matters" and "Electric Energy Situation in California" included in Part I, Item 2 in Management's Discussion and Analysis of Financial Condition and Results of Operation.

Critical Accounting Policies

Critical accounting policies are those that are important to the portrayal of AWR's financial condition, results of operations and cash flows, and require the most difficult, subjective or complex judgments of AWR's management. The need to make estimates about the effect of items that are uncertain is what makes these judgments difficult, subjective and/or complex. Management makes subjective judgments about the accounting and regulatory treatment of many items. The following are examples of accounting policies that are critical to the financial statements of AWR.

Accounting for Rate Regulation

- Management believes that regulation and the effects of regulatory accounting have the most significant impact on the financial statements. When either SCW or CCWC file for adjustments to rates, capital assets, operating costs and other matters are subject to review, and disallowances could occur. Regulatory disallowances in the past have not been frequent but have on occasion significantly impacted AWR's results of operations.
- The utility subsidiaries, SCW and CCWC, have incurred various costs and received various credits reflected as regulatory assets and liabilities. Accounting for such costs and credits as regulatory assets and liabilities is in accordance with Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation". This statement sets forth the application of generally accepted accounting principles for those companies whose rates are established by or are subject to approval by an independent third-party regulator. Under SFAS 71, utility companies defer costs and credits on the balance sheet as regulatory assets and liabilities when it is probable that those costs and credits will be recognized in the rate making process in a period different from the period in which they would have been reflected in income by an unregulated company. These deferred regulatory assets and liabilities are then reflected in the income statement in the period in which the same amounts are reflected in the rates charged for service. If rate recovery is no longer probable, Registrant is required to write off the related regulatory asset.

Table of Contents

- Registrant's income tax calculations require estimates due principally to the regulated nature of the operations of SCW and CCWC, the multiple states in which Registrant operates, and potential future tax rate changes. Registrant uses the asset and liability method of accounting for income taxes under which deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. A change in the regulatory treatment, or significant changes in tax-related estimates or assumptions or changes in law, could have a material impact on the financial position and results of operations of Registrant.
- Depreciation is computed at composite rates, based on depreciable plant at the beginning of each year, considered sufficient to amortize costs over the estimated remaining lives of assets. Depreciation studies are performed periodically and prospective changes in rates are estimated to make up for past differences. These studies are reviewed and approved by either the CPUC or the ACC. Changes in estimates of depreciable lives or changes in depreciation rates mandated by regulations could impact results of operations of Registrant in periods subsequent to the change. Depreciation is computed on the straight-line, remaining-life basis.
- As prescribed by the CPUC under its Uniform System of Accounts for Water Utilities, SCW is allowed to capitalize a portion of general costs such as engineering, supervision, general office salaries and expenses, legal expenses, insurance, injuries and damages, pensions and benefits, and taxes, as overhead construction costs included in SCW's Utility Plant. All overhead construction costs are charged to jobs on the basis of the amounts of such overhead expenses reasonably applicable thereto, so that each job bears its equitable proportion of such costs and its direct costs.

Accounting for Derivative Instruments

In June 1998, the FASB issued SFAS No. 133, "*Accounting for Derivative Instruments and Hedging Activities*". A derivative financial instrument or other contract derives its value from another investment or designated benchmark. SFAS No. 133 requires companies to record derivatives on the balance sheet as assets and liabilities, and to measure those instruments at their fair value. SCW is a party to various block-forward purchase power contracts. Certain of these contracts qualify as an exception provided under SFAS No. 133 for activities that are considered normal purchases and normal sales. These contracts are reflected in the statements of income at the time of contract settlement. Contracts that do not qualify for the normal purchases and normal sales exception have been recognized at fair market value on the balance sheet as an asset or liability and an unrealized gain or loss against earnings. On a quarterly basis, the related asset or liability will be adjusted to reflect the fair market value at the end of the quarter. As these contracts are settled, the realized gains or losses will be recorded and the unrealized gains or losses will be reversed.

The unrealized gains of \$854,000 for the nine months ended September 30, 2003 resulted from increases in the current forward market prices since December 31, 2002, causing a decrease in the cumulative unrealized loss for the contracts. For the three and twelve months ended September 30, 2003, the unrealized loss of \$420,000 and \$1,676,000, respectively, resulted from the contract prices with PWCC being higher than current forward market prices. There is no cash flow impact for the gains and losses. Management is evaluating alternatives to minimize future unrealized loss. These unrealized gains and losses at Bear Valley Electric will continue to impact earnings during the life of the contract with PWCC; both negatively and positively. SCW projects that there will be no cumulative impact on Bear Valley Electric earnings at the end of the contract period, in 2008.

Accounting for Asset Retirement Obligations

SFAS No. 143, "Accounting for Asset Retirement Obligations," requires businesses to record the fair value of a liability for a legal obligation to retire an asset in the period in which the liability is incurred. A legal obligation is a liability that a party is required to settle as a result of an existing or enacted law, statute, ordinance or contract. When the liability is initially recorded, the entity capitalizes the cost by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset. Upon settlement of the liability, an entity either settles the obligation for its recorded amount or incurs a gain or loss upon settlement. Registrant adopted SFAS No. 143 on January 1, 2003, as required. Registrant's legal obligations for retirement reflect principally the retirement of wells, which by law need to be destroyed and filled at the time of removal. As such, the regulated subsidiaries of Registrant incur asset retirement obligations. Retirement cost has historically been recovered through rates at the time of retirement. As a result, the cumulative effect upon adoption was reflected as a regulatory asset or liability. Accordingly, Registrant will also reflect the gain or loss at settlement as a regulatory asset or liability on the balance sheet.

Upon adoption on January 1, 2003, Registrant recorded an asset retirement obligation of \$13.2 million at its net present value of \$2.7 million, increased depreciable assets by \$0.4 million for asset retirement costs, increased regulatory assets by \$2.5 million and increased accumulated depreciation by \$0.2 million. Amounts recorded under SFAS No. 143 are subject to various assumptions and determinations, such as determining whether a legal obligation exists to remove assets, and estimating the fair value of the costs of removal, when final removal will occur and the credit-adjusted risk-free interest rates to be utilized on discounting future liabilities. Changes that may arise over time with regard to these assumptions will change amounts recorded in the future. The following is a reconciliation of the beginning and ending aggregate carrying amount of the asset retirement obligations ("ARO"):

	For the Nine Months Ended September 30, 2003				
	Balance at Adoption January 1, 2003	Liabilities Incurred	Liabilities Settled	Accretion	Balance At September 30, 2003
ARO	\$2,718,079	60,000	—	160,314	\$2,938,393

Accounting for Pension and Other Postretirement Benefits

Registrant records plan assets, obligations and expenses related to its pension and other postretirement benefit plans based on actuarial valuations. Key assumptions in these valuations include discount rates, expected returns on plan assets, compensation increases and health care cost trend rates. Registrant believes that the assumptions utilized in recording obligations under the plans are reasonable based on prior experience, market conditions and the advice of its plan actuary. Net periodic pension cost is expected to increase from \$1.8 million for the plan year ended December 2002 to \$3.0 million for the year ending December 31, 2003 due to actuarial assumption changes in discount rate and expected long-term rate of return on plan assets. Postretirement benefit cost is also expected to increase. The increases are generally recovered through rates. Net periodic pension and postretirement benefit costs for 2003 were computed using a discount rate and expected long-term rate of return on plan assets of 6.75% and 7.0%, respectively, as compared to 7.25% and 8.0% in 2002. Both pension and postretirement liabilities, and future pension and postretirement expense increase as the discount rate is reduced. In addition, pension and postretirement expense increase as the expected rate of return on plan assets decreases.

Unbilled Revenues

SCW and CCWC record water and electric utility operating revenues when the service is provided to customers. Operating revenues include unbilled revenues which are earned (service has been provided) but not billed by the end of each accounting period. By using the billed revenues based on the last meter reading and billed customer numbers, an average amount billed per customer is used to estimate the unbilled revenues for estimated average remaining days to the end of the reporting period. Unbilled revenues are recorded for both monthly and bi-monthly customers.

Liquidity and Capital Resources

AWR

Net cash provided by operating activities was \$33.4 million for the nine months ended September 30, 2003 as compared to \$28.3 million for the nine months ended September 30, 2002. The increase of \$5.1 million in cash provided by operations was primarily attributable to new electric rates and surcharges to decrease under-collected electric supply cost balancing account balances, and favorable changes in other operating assets and liabilities between the two periods, offset by the decrease in net income, and by an unrealized gain on purchased power contracts.

Net cash used in investing activities was \$33.9 million for the nine months ended September 30, 2003 as compared to \$32.3 million for the nine months ended September 30, 2002 due to higher capital expenditures.

Net cash used in financing activities was \$6.5 million for the nine months ended September 30, 2003 as compared to \$14.8 million for the nine months ended September 30, 2002. The decrease was due primarily to (i) the redemption of preferred shares in 2002 totaling \$1.9 million, (ii) a reduction of \$4 million in payments made to banks for notes payable, (iii) increases of \$1.9 million in receipt of advances for and contributions in aid of construction, and (iv) the receipt of \$1.5 million of cash related to the financing portion of SCW's purchased power contracts with Pinnacle West.

AWR funds its operating expenses and pays dividends on its outstanding Common Shares primarily through dividends from its subsidiaries, principally SCW. AWR has a Registration Statement on file 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. As of September 30, 2003, approximately \$31.1 million remained for issuance under this Registration Statement. AWR intends to issue shares sufficient to utilize the remaining \$31.1 million pursuant to this Registration Statement within the fourth quarter of this year. The net proceeds will be used to make equity investments in SCW and ASUS.

In June 2002, AWR established a \$75 million revolving credit facility that matures in June 2005. Up to \$15 million of this facility may be used for letters of credit. As of September 30, 2003, an aggregate of \$33 million in cash borrowing was outstanding. Approximately \$8 million of letters of credit were outstanding under this facility.

On April 19, 2002, AWR completed the redemption of all of its outstanding 4%, 4-1/4% and 5% series of preferred shares.

SCW

Net cash provided by operating activities was \$33.2 million for the nine months ended September 30, 2003 as compared to \$20.4 million for the nine months ended September 30, 2002. The increase of \$12.8 million in cash provided by operations was primarily attributable to new electric rates and

Table of Contents

surcharges to decrease under-collected electric supply cost balancing account balances, and favorable changes in other operating assets and liabilities between the two periods, offset by the decrease in net income, and by an unrealized gain on purchased power contracts.

Net cash used in investing activities increased slightly to \$32.0 million for the nine months ended September 30, 2003 as compared to \$31.7 million for the same period of 2002.

Net cash used in financing activities was \$5.9 million for the nine months ended September 30, 2003 as compared to \$8.6 million for the nine months ended September 30, 2002, reflecting increases in receipt of advances for and contributions in aid of construction, and the receipt of \$1.5 million of cash related to the financing portion of SCW's purchased power contracts with Pinnacle West.

SCW funds the majority of its operating expenses, payments on its debt, and dividends on its outstanding common shares through internal sources. Internal sources of cash flow are provided primarily by retention of a portion of earnings from operating activities. Internal cash generation is influenced by factors such as weather patterns, environmental regulation, litigation, changes in supply costs and regulatory decisions affecting SCW's ability to recover these supply costs, and timing of rate relief. For further information, see the sections entitled "*Risk Factors*" and "*Electric Energy Situation in California*" included in Part I, Item 2 in Management's Discussion and Analysis of Financial Condition and Results of Operation.

SCW also relies on external sources, including equity investments and short-term borrowings from AWR, long-term debt, contributions-in-aid-of-construction, advances for construction and install-and-convey advances, to fund the majority of its construction expenditures. On March 30, 2001, AWR made an additional \$25 million equity investment in SCW. On November 14, 2001, SCW filed a Registration Statement with the SEC for issuance, from time to time, of up to \$100 million in debt securities. SCW anticipates that it will be necessary to issue additional long-term debt to refund retirement obligations and fund capital expenditures. In December 2001, SCW issued \$50 million of long-term debt under this Registration Statement that initially reduced bank borrowings incurred to fund capital expenditures and purchased power costs.

Outstanding debt of SCW issued in the public markets is rated by both Moody's Investor Services and Standard & Poor's Corporation. Ratings assigned by these agencies are subject to periodic review of various factors including, but not limited to, the effects of regulation. SCW management will hold its annual review with each of the agencies before year-end 2003. Following the annual review, each agency will determine if the current rating will remain in place, be upgraded or downgraded. A downgrade in SCW's rating will likely result in an increase in the cost of borrowing from current levels.

CCWC

CCWC funds the majority of its operating expenses, payments on its debt and dividends, if any, through internal sources. CCWC also relies on external sources, including long-term debt, contributions-in-aid-of-construction, advances for construction and install-and-convey advances, to fund the majority of its construction expenditures.

ASUS

ASUS funds its operating expenses primarily through contractual management fees and investments by or loans from AWR.

Contractual Obligations and Other Commitments

In addition to contractual maturities, Registrant has certain debt instruments that contain annual sinking fund or other principal payments. Registrant believes that it will be able to refinance debt instruments at their maturity through public issuance, or private placement, of debt or equity. Annual principal payments are generally made from cash flow from operations. In the case of the \$12,500,000 in notes due October 2003, SCW intends to refinance this obligation through issuance of equity by its parent, AWR, or through additional long-term debt issuance.

Table of Contents

The following table reflects Registrant's contractual obligations and commitments to make future payments pursuant to contracts as of September 30, 2003. All obligations and commitments are obligations and commitments of SCW unless otherwise noted.

(\$ in thousands)	Payments/Commitments Due by Period (1)				
	Total	Less than 1 Year	1-3 Years	4-5 Years	After 5 Years
Notes/Debentures(2)	\$185,600	\$12,500	—	—	\$173,100
Private Placement Notes(3)	28,000	—	—	—	28,000
Tax-Exempt Obligations(4)	18,887	91	\$ 194	\$ 218	18,384
Other Debt Instruments(5)	2,341	195	404	453	1,289
Purchased Power Contracts(6)	63,295	12,014	23,988	23,947	3,347
Operating Leases (7)	6,674	2,023	4,062	589	—
Other Commitments (8)	75,753	—	—	—	—
Chaparral City Water Co. (9)	8,598	550	913	550	6,585
TOTAL	\$389,148	\$27,373	\$29,561	\$25,757	\$230,705

(1) Excludes interest, dividends, commitments and facility fees.

(2) The Notes and Debentures are issued under an Indenture dated as of September 1, 1993. The Notes and Debentures do not contain any financial covenants that Registrant believes to be material, or cross default provisions.

(3) The private placement notes are issued pursuant to the terms of Note Agreements with substantially similar terms. The Note Agreements contain restrictions on the payment of dividends, minimum interest coverage requirements, maximum debt to capitalization ratio and a negative pledge. Pursuant to the Note Agreements, SCW must maintain a minimum interest coverage ratio of two times interest expense. SCW does not currently have any outstanding mortgages or other encumbrances on its properties.

(4) Consists of obligations under a loan agreement supporting \$8 million in debt issued by the California Pollution Control Financing Authority, \$6 million in obligations supporting \$6 million in certificates of participation issued by the Three Valleys Municipal Water District and \$5.0 million of obligations incurred by SCW with respect to its 500 acre foot entitlement to water from the State Water Project (SWP). Except as described in paragraph (6) below, these obligations do not contain any financial covenants believed to be material to Registrant or any cross default provisions. SCW's obligations with respect to the certificates of participation issued by the Three Valleys Municipal Water District are supported by a letter of credit issued by Wells Fargo Bank. In regards to its SWP entitlement, SCW has entered into agreements with various developers for 439 acre-feet, in aggregate, of its 500 acre-foot entitlement to water from the SWP.

(5) Consists of \$1.5 million outstanding under a fixed rate obligation incurred to fund construction of water storage and delivery facilities with the Three Valleys Municipal Water District, \$0.5 million outstanding under a variable rate obligation incurred to fund construction of water delivery facilities with the Three Valleys Municipal Water District and an aggregate of \$0.3 million outstanding under capital lease obligations. These obligations do not contain any financial covenants believed to be material to Registrant or any cross default provisions.

(6) Consists of \$63.3 million of purchased power contracts until December 2008.

(7) Reflects Registrant's future minimum payments under non-cancelable operating leases.

Table of Contents

(8) Other commitments of Registrant consist of (i) \$75 million syndicated revolving credit facility, expiring in June 2005, (ii) an amount of \$296,000 with respect to a \$6,296,000 irrevocable letter of credit issued by Wells Fargo Bank to support the certificates of participation of Three Valleys Municipal Water District (the other \$6,000,000 is reflected under tax-exempt obligations), (iii) an irrevocable letter of credit in the amount of \$400,000 that expires on October 2003 for the deductible in Registrant's business automobile insurance policy (iv) an irrevocable letter of credit that expires June 30, 2005 for its energy scheduling agreement with Automated Power Exchange as security for the purchase of power; the amount of the credit is \$585,000 for the months from November to March, and \$270,000 to cover the months from April to October, and (v) outstanding performance bonds of \$11,450 to secure performance under franchise agreements with governmental agencies. All of the letters of credit are issued pursuant to the syndicated revolving credit facility. The syndicated revolving credit facility contains restrictions on prepayments, deposition of property, mergers, liens and negative pledges, indebtedness and guaranty obligations, transactions with affiliates, minimum interest coverage requirements, a maximum debt to capitalization ratio, and a minimum debt rating. Pursuant to the Credit Agreement, AWR must maintain a minimum interest coverage ratio of 3.25 times interest expense, a maximum total funded debt ratio of 0.65 to 1.00 and a minimum debt rating of Baa1 or BBB+.

(9) Consists of \$7.9 million of obligations under a loan agreement supporting Industrial Development Revenue Bonds due in 2006 and a \$0.7 million repayment obligation to the United States Bureau of Reclamation. The loan agreement contains provisions that establishes a maximum of 65% debt in the capital structure, limits cash distributions when the percentage of debt in the capital structure exceeds 55% and requires a debt service coverage ratio of two times. The Bureau of Reclamation obligation does not contain any financial covenants believed to be material to Registrant or any cross default provisions.

Under the terms of its power purchase contracts with Mirant and PWCC, SCW is required to post security, at the request of the seller, if SCW is in default under the terms of the contract and the future value of the contract is greater than the future value of contracts of a similar term on the date of default. SCW will be in default under the terms of these contracts if its debt is rated less than BBB- by Standard & Poor's Ratings Service ("S&P") or Fitch, Inc. ("Fitch") or less than Baa3 by Moody's Investor Services, Inc ("Moody's"). SCW currently has a rating of A+ by S & P and A2 by Moody's. Fitch does not rate SCW.

S&P debt ratings range from AAA (highest rating possible) to D (obligation is in default). Moody's debt ratings range from Aaa (best quality) to C (lowest quality). Securities ratings are not recommendations to buy, sell or hold a security and are subject to change or withdrawal at any time by the rating agency.

Electric Energy Situation in California

Background Information

On January 17, 2001, the Governor of the State of California proclaimed a state of emergency in California due to shortages of electricity available to certain of California's utilities (resulting in blackouts), the unanticipated and dramatic increases in electricity prices and the insufficiency of electricity available from certain of California's utilities to prevent disruption of electric service in California. The Federal Energy Regulatory Commission ("FERC") also implemented a number of changes to the tariff for the California Independent Operator System ("Cal ISO") beginning in December 15, 2000 in an attempt to stabilize the market. The reasons for the high cost of energy are under investigation but are reported to include, among other things, limited supply caused by a lack of investment in new power plants to meet growth in demand, planned and unplanned outages of power plants, decreased availability of hydroelectric power from the Pacific Northwest due to lower than usual precipitation and higher demand for electricity in the region, transmission line constraints, increased prices for natural gas, the fuel used in many of the power plants serving the region, a dysfunctional power

market and market manipulation through the withholding of generation and a variety of “gaming” strategies.

As of September 30, 2003, SCW had accrued \$23.2 million in under-collected power costs that SCW mostly incurred during the energy crisis in connection with providing service to its Bear Valley Electric customers. In addition, SCW established \$7.9 million in reserves in 2001 for potential non-recovery of these power costs. In 2002, SCW charged \$1.7 million against the reserves due to its inability to recover all of its costs associated with entering into a long-term power contract with Mirant in March 2001. In the fourth quarter of 2002, SCW reversed the remaining reserves due to various new contracts entered into with PWCC in September 2002 as discussed below.

On July 17, 2002, the FERC extended and modified the mitigation measures that were set to expire on September 30, 2002, citing delays in construction of new generation resources in California and throughout the West, delays in adopting a new market design and market rules by the Cal ISO, transmission line constraints, constraints on natural gas pipeline capacity and continuing dysfunctions in the California power market. It remains unclear how long the FERC will leave its mitigation measures in place. The premature termination of such mitigation measures could result in substantial increases in spot market prices and the prices of long-term contracts for power and capacity. In addition, FERC is considering a number of market reforms, some of which could materially increase SCW’s costs for power. Increased costs would be included in SCW’s electric supply cost balancing account. However, as mentioned previously, SCW is only allowed to include up to a weighted annual energy purchase cost of \$77 per MWh each year for 10 years in its electric supply cost balancing account. To the extent that actual weighted average annual cost for power purchased exceeds the \$77 per MWh amount, SCW will not be able to include these amounts in its balancing account and such amounts will be expensed.

Power Supply Arrangements at SCW’s Bear Valley Electric Service Area

All electric energy sold by SCW to customers in its Bear Valley Electric customer service area is purchased from others. Under the terms of contracts with Dynegy that expired on April 30, 2002, Dynegy provided electric energy to SCW, acted as scheduling coordinator and provided other ancillary services. Various disputes arose between the parties regarding the services provided by Dynegy and the amounts charged by Dynegy. As a result of these disputes, SCW withheld payment from Dynegy of certain amounts invoiced by Dynegy. On November 1, 2002, Dynegy accepted \$3.5 million from SCW as payment in full for the disputed amounts.

SCW entered into a five-year and nine-month, block forward purchase contract with Mirant for 15 MWs of electric energy at a price of \$95 per MWh beginning April 1, 2001 through December 31, 2006. On December 20, 2001, SCW filed a complaint with FERC seeking to reduce the amount charged by Mirant under the terms of this contract to a just and reasonable price. In June 2003, the FERC issued a final order denying SCW’s complaint. On November 10, 2003, the FERC denied SCW’s rehearing request. SCW is currently reviewing its options with respect to the FERC’s latest order denying rehearing and is determining if it will appeal the decision in Federal Court.

In June 2001, SCW executed an agreement with PWCC for an additional 8 MWs of electric energy to meet peak winter demands. The contract provided for pricing of \$75 per MWh from November 1, 2001 to September 30, 2002, \$48 per MWh from November 1, 2002 to September 30, 2003, and \$36 per MWh from November 1, 2003 to June 30, 2004.

In September 2002, SCW entered into a series of purchased power contracts with PWCC. Under the agreements, SCW will sell 15 MWs to PWCC of electric energy at a price of \$95 per MWh beginning November 1, 2002 through December 31, 2006, and the 8 MWs of electric energy covered under the energy purchase agreement with PWCC discussed previously. In return, PWCC will supply SCW with 15 MWs of electric energy at a price of \$74.65 per MWh beginning November 1, 2002 through December

Table of Contents

31, 2008, and an additional 8 MWs at \$74.65 per MWh beginning on November 1, 2002 through September 30, 2003 and each succeeding November 1 through March 31 period through June 30, 2008, and for the period November 1, 2008 through December 31, 2008. These contracts do not qualify for the normal purchases and normal sales exception, under SFAS No. 133, and have been recognized at fair market value on the balance sheet as a liability of \$1.7 million at September 30, 2003 and an unrealized loss of \$420,000 for the three months ended September and an unrealized gain of \$854,000 for the nine months ended September 30, 2003.

The average minimum load at SCW's Bear Valley Electric customer service area has been approximately 12 MWs. The average winter load has been 18 MWs with a winter peak of 39 MWs when the snowmaking machines at the ski resorts are operating. In addition to the power purchase contracts, SCW buys additional energy from the spot market to meet peak demand and sells surplus power to the spot market as well. The average cost of power purchased, including the transactions in the spot market, was approximately \$76.4, \$78.3 and \$79.9 per MWh, respectively, for the three, nine and twelve months ended September 30, 2003. SCW's average energy costs will be impacted by pricing fluctuations on the spot market.

Transmission Constraints

Demand for energy in SCW's Bear Valley Electric customer service area generally has been increasing. However, the ability of SCW to deliver purchased power to these customers is limited by the ability of the transmission facilities owned by Southern California Edison Company (Edison) to transmit this power. On December 27, 2000, SCW filed a lawsuit against Edison for breach of contract as a result of delays in upgrading these transmission facilities as well as for violations of good faith and fair dealing, negligent misrepresentation, intentional misrepresentation and unjust enrichment. It is unlikely that the transmission upgrade will occur as a result of the delays and the pending litigation. As previously mentioned, SCW has attended two mediation meetings with Edison in this matter, and is discussing a settlement proposal. The parties have not, however, yet reached a mutually agreeable definitive settlement of the issues. Therefore, SCW is constructing a natural gas-fueled 8.4 MW generation facility to be owned by SCW as a means of meeting these increasing demands for energy. A Certificate of Public Convenience and Necessity filed with the CPUC seeking authorization for construction of the generation facility was approved on July 10, 2003. It is expected that the generator will be on line during the second quarter of 2004, and should assist SCW in controlling its spot purchase prices, as discussed above.

Southern California Wild Fires

The October 2003 wild fires in Southern California have had some impact on certain of our Southern California Water Company units. We have several water customer service areas where fires were present. SCW has had minimal damage to its water facilities. In our Bear Valley Electric area, located in the mountains north of Los Angeles, our people have stayed on the job to make certain that electric service continues; this in spite of isolated damage to certain electric distribution facilities. We will be filing with the CPUC for recovery of the extra expenses incurred in meeting these community needs. These costs will be accumulated in Catastrophic Event Memorandum Accounts and amortized pursuant to prescribed procedures after review by the CPUC.

Construction Program

SCW maintains an ongoing water distribution main replacement program throughout its customer service areas based on the priority of leaks detected, fire protection enhancement and a reflection of the underlying replacement schedule. In addition, SCW upgrades its electric and water supply facilities in accordance with industry standards, local requirements and CPUC requirements. SCW's Board of Directors has approved anticipated net capital expenditures of approximately \$81.6 million for 2003

Table of Contents

principally reflecting the 2003 infrastructure replacement program in SCW's Metropolitan customer service area, a water treatment plant upgrade, water supply related projects, and security related costs.

CCWC's Board of Directors has approved a net capital budget of \$3.0 million for 2003 primarily reflecting improvement and upgrade of a water treatment plant. It is anticipated that CCWC's capital budget may be increased by up to \$600,000 if it is determined by the ACC that CCWC should construct additional water infrastructure to serve new development in its service territory without developer advances.

AWR and ASUS have no material capital commitments. However, ASUS actively seeks opportunities to own, lease or operate water and wastewater systems for governmental entities, which may involve significant capital commitments.

Registrant does not have any material capital expenditures for specific environmental control facilities or measures.

Registrant currently has formalized procedures covering the bidding of capital projects. These procedures are designed to achieve the lowest bid price from qualified contractors as well as to promote diversity among contractors. The procedures also provide for bypass of a formal bid process for emergency situations. In response to a recent review, Registrant has discovered that a greater than anticipated percentage of contracts in certain areas were being let on an emergency basis and to fewer than anticipated contractors. Registrant is currently evaluating its procedures and may, based on the results of this review, modify those procedures in order to ensure that the objectives are being met in a consistently applied manner.

Regulatory Matters

Rate Regulation

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 public convenience and necessity as to the extension of services and facilities and various other matters. CCWC is subject to regulation by the ACC.

Rates that SCW and CCWC are authorized to charge are determined by the CPUC and the ACC, respectively, in general rate cases and are derived using rate base, cost of service and cost of capital, as projected for a future test year in California and using an historical test year, as adjusted in Arizona. Rates charged to customers vary according to customer class and rate jurisdiction and are generally set at levels allowing for recovery of prudently incurred costs, including a return on rate base. Rate base generally consists of the original cost of utility plant in service, plus certain other assets, such as working capital and inventory, less accumulated depreciation on utility plant in service, deferred income tax liabilities and certain other deductions.

Neither AWR nor ASUS are directly regulated by the CPUC. The CPUC does, however, regulate certain transactions between SCW and its affiliates. The ACC also regulates certain transactions between CCWC and its affiliates.

For rate-making purposes, the 22 customer service areas of SCW are grouped into 9 water districts and 1 electric district. Water rates vary among the 9 water 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: (i) general rate case increases (GRC's), (ii) offsets for certain expense increases,

Table of Contents

including, but not limited to, supply cost offset and balancing account amortization, and (iii) advice letter filings related to certain plant additions and other operating cost increases. GRC's are typically for three-year periods, which include step increases for the second year and attrition increases for the third year. Rates are based on a forecast of expenses and capital costs. GRC's have a typical regulatory lag of one year. Offset rate increases and advice letter filings typically have a two to four month regulatory lag. In addition, recovery of water supply costs incurred after November 29, 2001 will be considered as part of GRC's.

Changes in Rates

Step increases of approximately \$321,600 for four of seven ratemaking districts in SCW's Region I were implemented in January 2002. Region I also received attrition increases of \$219,400 effective January 2003.

On January 16, 2003, the CPUC approved rate increases of approximately \$2.7 million annually, effective January 22, 2003, in SCW's Metropolitan district to recover costs associated with an increase in Region II rate base associated with SCW's 2002 infrastructure replacement program and, additionally, to recover general increases in operating expenses. On January 31, 2003, the CPUC also approved SCW's Advice Letter filed for the 2003 infrastructure replacement program with rate increases of \$3.5 million annually effective February 4, 2003.

As of September 30, 2003, SCW had accrued approximately \$23.6 million in under-collected purchased power costs included in the electric balancing account. In 2001, the CPUC approved two Advice Letters which allow SCW to collect a surcharge of 2.2¢ per kilowatt hour, for recovery of its under-collection in the electric balancing account for costs incurred during the energy crisis.

On August 17, 2001, SCW filed an application with the CPUC seeking recovery of an average cost of \$87 per megawatt hour (MWh) for electric energy purchased pursuant to power purchase contracts with Mirant and PWCC. On July 17, 2002, CPUC approved a settlement agreement reached among SCW, all intervening parties and the Office of Ratepayer Advocates (ORA). The authorization permits SCW to recover \$77 per MWh of purchased power costs through rates. SCW is allowed to include its actual purchased power costs up to an average annual weighted cost of \$77 per MWh each year, through August 2011, for 10 years in its balancing account. To the extent SCW's actual average annual weighted cost for purchased power is less than \$77 per MWh, the differential would offset amounts included in the electric supply balancing account. Conversely, to the extent that actual average annual weighted costs for power purchased exceed the \$77 per MWh amount, SCW would not be able to include these amounts in its balancing account and such amounts would be expensed against income.

The CPUC settlement also extended the previously approved surcharges of 2.2¢ per kilowatt hour for an additional five years through August of 2011 to allow SCW an opportunity to collect amounts remaining in its electric cost balancing account. SCW anticipates that electricity sales will be sufficient to enable SCW to fully recover the under-collection in its balancing account during this ten year period.

SCW previously established approximately \$7.9 million in reserves against potential non-recovery of electric power costs. In 2002, \$1.7 million was written off against the reserve based on the settlement with the CPUC as previously discussed. In September 2002, SCW entered into various agreements with PWCC, which enable SCW to purchase energy at a lower cost. As a result, the remaining reserve of \$6.5 million was reversed into income in 2002.

The settlement requires SCW to pursue its complaint filed with FERC in which SCW has requested FERC to reduce the prices in its power purchase contract with Mirant to a just and reasonable price. If SCW is ultimately successful in obtaining a reduction in prices under this contract, SCW is required, based on the settlement, to file an Advice Letter to notify the CPUC within 30 days of the resolution of its complaint. In June 2003 the FERC issued a final order denying SCW's complaint. On November 10, 2003, the FERC denied SCW's rehearing request. SCW is currently reviewing its options with respect to the FERC's latest order denying rehearing and is determining if it will appeal the decision in Federal Court.

Pending Rate Requests

On July 10, 2003, the CPUC approved the Certificate of Public Convenience and Necessity (CPCN) filed by SCW in March 2002 seeking authorization to construct an 8.4 MW natural gas-fueled generation facility on a portion of its property in the City of Big Bear Lake. The capital cost of the generating facility is estimated to be approximately \$13 million. The CPUC's order authorizes construction and enables SCW to file a rate application to generate an annual revenue increase of about \$2.4 million. SCW will file for increased rates using a special filing called a "Major Adjustment Clause" or "MAC" filing that should result in at least 75% of the revenue requirement related to this facility being included in rates. The remainder will be subject to recovery in a general rate case filing.

In October 2002, SCW filed an application to increase water rates in the customer service areas that comprise Region III. SCW also filed a concurrent application requesting a rate increase applicable to SCW's entire customer base to recover costs associated with the general office functions of SCW. With a proposed return on equity of 12.45%, the new water rates in these filings, as stipulated by SCW, would generate an initial annual increase in revenues of approximately \$12.9 million for the Region III customer service areas. However, the CPUC staff has not yet stipulated to this return on equity. Due to unresolved differences between SCWC and the CPUC staff, we cannot predict the increases. A final decision on these applications is anticipated in the fourth quarter of 2003.

We filed an application to increase water rates in the Region II customer service areas on September 11, 2003, which was accepted by the CPUC on October 6, 2003. The new water rates in this filing, if approved, would generate an initial annual increase in revenues of \$15.4 million. A decision is not expected until the third quarter of 2004.

On October 27, 2003, SCW also filed an abbreviated application to the CPUC to request for an inflationary increase in three of the Region I customer services areas. As part of the Region I filing, SCW requested a long-term amortization of the balance of costs included in the Aerojet litigation memorandum account, net of any reimbursement amount. For more information, see the section entitled "*Other Water Quality Litigations*" included in Part I, Item 3 in Legal Proceedings.

In 1993, the CPUC disallowed \$1.6 million of costs incurred in construction of a water treatment facility in SCW's Clearlake customer service area and Registrant wrote off the disallowed amount at that time. Based on new water quality standards, in 2000, SCW re-applied to the CPUC for inclusion of the disallowed amount in rate base. A draft decision issued on March 30, 2001 by the CPUC would have allowed SCW to include \$500,000 of the \$1.6 million in the regulated rate base. An alternate draft decision issued by one of the CPUC Commissioners proposed to deny the relief sought by SCW in its application. An Administrative Law Judge subsequently reopened the proceeding in August 2001 requiring additional information. We cannot predict when the final order will be issued, nor can we give assurance that the CPUC will ultimately allow recovery of all or any of the remaining costs through rates.

Other Regulatory Matters

On November 29, 2001, the CPUC adopted an Order Instituting Rulemaking (OIR) to (i) evaluate existing practices and policies, (ii) determine whether new procedures or policies for processing offset rate increases and balancing accounts should be made and (iii) determine whether the new memorandum account procedures adopted on November 29, 2001 should be made permanent.

Table of Contents

Pursuant to a resolution issued by the CPUC on December 17, 2002, SCW filed advice letters on March 17, 2003 requesting recovery of \$2.2 million under-collections remaining in the balancing accounts for water supply costs incurred prior to November 29, 2001. On June 19, 2003, the CPUC authorized increases in rates in total of \$2.1 million, effective June 24, 2003, for SCW to recover the pre-November 29, 2001 balances. The remaining \$75,000 is to be deferred to the rate case of Region I.

In a decision issued on June 19, 2003, the CPUC concluded that (i) if a utility is within its rate case cycle and does not earn over its authorized rate of return, the utility shall recover its account subject to reasonableness review by the CPUC; (ii) if a utility is either within or outside of its rate case cycle and earns over the authorized return, the utility's recovery of expenses from the accounts will be reduced by the amount exceeding the authorized rate of return; and (iii) a utility is required to seek review of under and over collections by filing an advice letter annually by March 31. Pursuant to the resolution, SCW filed advice letters, on September 12, 2003, seeking recovery for under-collected balance of \$2.6 million for the period of November 29, 2001 through December 31, 2002. For more information, see the section entitled "*Accounting for Supply Costs*" included in Part I, Item 2 in Management's Discussion and Analysis of Financial Condition and Results of Operation

Environmental Matters

1996 Amendments to Federal Safe Drinking Water Act

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. This law allows the EPA to bypass the selection process and adopt interim regulations for contaminants in order to address urgent health threats. The California Department of Health Services (DOHS), acting on behalf of the EPA, administers the EPA's program in California.

The EPA may 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 costs for each such MCL.

SCW and CCWC currently test their wells and water systems according to requirements listed in the Safe Drinking Water Act ("SDWA"). Water from wells found to contain levels of contaminants above the established MCL's is treated to reduce contaminants to acceptable levels before it is delivered to customers. If treatment is not possible, the wells are shut down. Since the SDWA became effective, SCW and CCWC have experienced increased operating costs for testing to determine the levels, if any, of the constituents in their 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 and/or CCWC to experience additional capital costs as well as increased operating costs. The CPUC and ACC ratemaking processes provide SCW and CCWC with the opportunity to recover prudently incurred capital and operating costs associated with water quality. Management believes that such incurred and expected future costs should be authorized for recovery by the CPUC and ACC, as applicable.

Enhanced Surface Water Treatment Rules

The EPA has adopted Enhanced Surface Water Treatment Rules (ESWTR), which require increased surface-water treatment to decrease the risk of microbial contamination. These rules apply to each of SCW's five surface water treatment plants and CCWC's surface water treatment plant. Registrant anticipates that all plants will achieve compliance within the three-year to five-year time frames identified by EPA. Registrant is required to be in compliance by June 1, 2006. SCW has initiated phased construction of a new treatment plant in the Calipatria-Niland customer service area (see further discussion below under *Regulation of Disinfectant/Disinfection By-Products*) to bring that facility into compliance. Once this project is completed, all the surface water plants in SCW and CCWC should be in compliance with these rules.

Regulation of Disinfection/Disinfection By-Products

SCW and CCWC are also subject to regulations concerning disinfection/disinfection by-products (DBP's). Stage I of the regulations was effective in November 1998 with full compliance required for systems serving 10,000 or more persons by 2002 and for systems serving fewer than 10,000 persons by 2004. Stage I requires reduction of trihalomethane contaminants from 100 micrograms per liter to 80 micrograms per liter. SCW has already implemented modifications to the treatment process in its Bay Point and Cordova systems to achieve compliance and the Calipatria plant is undergoing treatment modifications, which will also address the requirements under the ESWTR, in order to comply with the DBP's by 2004.

The EPA is not allowed to use the cost/benefit analysis provided for in the 1996 SDWA amendments for establishing the Stage II rules applicable to DBP's but may utilize the regulatory negotiating process provided for in the 1996 SDWA amendments to develop the Stage II rule. The final rule is not expected until 2004.

Ground Water Rule

On May 10, 2000, the EPA published the proposed Ground Water Rule (GWR), which establishes multiple barriers to protect against bacteria and viruses in drinking water systems that use ground water. The proposed rule will apply to all U.S. public water systems that use ground water as a source. The proposed GWR includes system sanitary surveys conducted by the state to identify significant deficiencies; hydrogeologic sensitivity assessments for undisinfected systems; source water microbial monitoring by systems that do not disinfect and draw from hydrogeologically sensitive aquifers or have detected fecal indicators within a distribution system; corrective action; and compliance monitoring for systems which disinfect to ensure that they reliably achieve 4-log (99.99%) inactivation or removal of viruses. The GWR is scheduled to be issued as a final regulation by the end of 2003. While no assurance can be given as to the nature and cost of any additional compliance measures, if any, SCW and CCWC do not believe that such regulations will impose significant compliance costs, since they already currently engage in disinfection of the majority of their groundwater systems.

Regulation of Radon and Arsenic

On October 31, 2001, EPA announced that the arsenic standard in drinking water would be 10 parts per billion (ppb). Compliance with an MCL of 10 ppb will require implementation of wellhead treatment remedies for eight affected wells in SCW's system and two wells in CCWC's system. The effective date for utilities to comply with the standard will be January 2006. In California, the Office of Environmental Health Hazard Assessment (OEHHA) issued a Public Health Goal for arsenic of 4 parts per trillion in March 2003 that may result in California adopting a lower MCL for arsenic.

Table of Contents

The EPA has proposed new radon regulations following a National Academy of Sciences risk assessment and study of risk-reduction benefits associated with various mitigation measures. The National Academy of Sciences study is in agreement with much of EPA's original findings but has slightly reduced the ingestion risk initially assumed by EPA. EPA established an MCL of 300 Pico Curies per liter based on the findings and has also established an alternative MCL of 4000 Pico Curies per liter, based upon potential mitigation measures for overall radon reduction. Registrant is currently waiting for the EPA to establish a MCL to determine the impact.

Voluntary Efforts to Provide Treated Surface Water Below Minimum Surface Water Treatment Requirements

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 treat surface water to levels much lower than the minimum operating requirements governing surface water treatment, optimize surface water treatment plant operations and seeks to have its surface water treatment facilities perform as efficiently as possible.

Unregulated Contaminants Monitoring Rule

EPA has revised the Unregulated Contaminant Monitoring Rule (UCMR). The data generated by the UCMR will be used to evaluate and prioritize contaminants on the Drinking Water Contaminant Candidate List, a list of contaminants EPA is considering for possible new drinking water standards. This data will help to ensure that future decisions on drinking water standards are based on sound science.

A tiered approach will be utilized with the three monitoring lists to provide the maximum capability to monitor up to the statutory limit of no more than 30 contaminants in any 5-year monitoring cycle. Therefore, as List 3 contaminants are found to occur in public water systems, they may move up to List 2, and likewise, List 2 contaminants may move up to List 1, in 2004, when the UCMR is revised again. The law requires that EPA publish a new contaminant-monitoring list every 5 years. When the EPA adds contaminants to their list, they will also include a compliance date. Registrant will evaluate the impact and necessary actions as additions are made to the contaminant lists.

Fluoridation of Water Supplies

SCW is required to fluoridate water supplies for public water systems serving more than 10,000 service connections if funds have been made available to cover capital and operating costs. The CPUC is required to authorize cost recovery through rates should funds for the operation of fluoridation facilities, once installed, become unavailable in future years. Currently, funds have been made available to public agencies only. SCW has not been offered any funding and has not installed any fluoridation facilities.

Perchlorate Action Level Activities

In January 2002, DOHS reduced the action level from 18 ppb to a level of 4 ppb, based upon new reference dose for health risk information from EPA. The Governor in California recently signed into law a bill requiring DOHS to establish a MCL for perchlorate by January 1, 2004. SCW has removed eight wells from service in its Rancho Cordova system and six additional wells in various other systems since they contained perchlorate in amounts in excess of this reduced action level of 4 ppb. On December 6, 2002, the OEHHA published a revised draft perchlorate Public Health Goal of 2 to 6 ppb. This is the first step in the establishment of an MCL in California. SCW is continuing to periodically monitor all of its wells to determine that levels of perchlorate are below the action level currently in effect. Perchlorate is known to be used in oxidizing rocket fuels.

Nitrosodimethylamine (NDMA) Action Level

In February 2002, DOHS increased the action level from 2 parts per trillion (ppt) to 10 ppt. NDMA is an additional by-product from the production and use of rocket fuels.

Matters Relating to SCW's Arden-Cordova Water System

In SCW's Rancho Cordova system, four wells have been removed from service and destroyed due to contamination from perchlorate. The supply has been replaced for three of these wells. An additional three wells are currently out of service due to perchlorate levels above the reduced action level of 4 ppb, and two wells are out of service due to detectable levels of NDMA above the action level. SCW continues to monitor all of its active groundwater wells in the Rancho Cordova system for perchlorate and NDMA level. Aerojet-General Corp. (Aerojet) has, in the past, used ammonium perchlorate in oxidizing rocket fuels. NDMA is an additional by-product from the production of rocket fuels and it is believed that such contamination is also related to the activities of Aerojet. SCW has filed suit against Aerojet for contamination of SCW's ground water supply in its Rancho Cordova system.

On October 10, 2003 Registrant entered into a confidential memorandum of understanding with the Aerojet-General subsidiary of GenCorp, Inc. for the settlement of legal actions brought by SCW. The memorandum of understanding outlines the present financial terms of a settlement. A final settlement agreement incorporating the terms of the memorandum of understanding is underway and being negotiated at the date of this filing. As the parties continue to address issues related and additional to the memorandum of understanding, certain disagreements have developed. The parties continue to negotiate in an attempt to resolve those issues. However, no complete, documented agreement has been reached and it is presently impossible to predict when a final settlement of all issues will be reached.

To date, Aerojet has reimbursed SCW for constructing a pipeline to interconnect with the City of Folsom water system to provide an alternative source of water supply in SCW's Rancho-Cordova customer service area and has reimbursed SCW for costs associated with the drilling and equipping of new wells. As of September 30, 2003, Aerojet had previously reimbursed SCW \$4.5 million of the approximately \$20.6 million in costs SCW has incurred. The remainder of the costs is subject to further reimbursement pending outcome of the settlement negotiation previously discussed. Reimbursements received from Aerojet have been applied directly to reduce SCW's costs of utility plant and purchased water. For further information regarding litigation related to contamination of ground water in Sacramento County, see the section entitled "*Other Water Quality Litigation*" included in Part II, Item 3, Legal Proceedings.

Matters Relating to SCW's Culver City Water System

The compound, methyl tertiary butyl ether (MTBE), an oxygenate used in reformulated fuels, has been detected in the Charnock Basin, located in the vicinity of the City of Santa Monica and within SCW's Culver City customer service area. 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 water 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 Metropolitan Water District of Southern California (MWD) at an increased cost to replace the water supply formerly pumped from the two wells removed from service.

On September 22, 1999, the U.S. EPA and the Los Angeles Regional Water Quality Control Board ordered Shell Oil Company, Shell Oil Products Company, Equilon Enterprises LLC and others to provide replacement drinking water to both SCW and the City of Santa Monica due to MTBE contamination in the Charnock Basin. The EPA has ordered Shell Oil and others to reimburse SCW for water replacement costs. In March 2002, SCW reached a settlement agreement with the City of Santa Monica, in which SCW assigned its rights against all the potentially responsible parties, who stored, transported and dispensed gasoline containing methyl tertiary butyl ether (MTBE) in underground storage

Table of Contents

tanks, pipelines or other related infrastructure, and its water rights in the Charnock Basin to the City of Santa Monica and Santa Monica took over the prosecution against the potentially responsible parties in exchange for an assignment payment. On May 8, 2003, the CPUC issued a decision approving the settlement agreement. Pursuant to the resolution, SCW has subsequently filed a report that sets forth specific details as to SCW's plans to reinvest the net proceeds from the settlement agreement with the City of Santa Monica.

Matters Relating to SCW's Yorba Linda Water System

The compound MTBE has been detected in three wells serving SCW's Yorba Linda water system. Two of the wells are currently inactive, and to date the third well has not shown MTBE above the DOHS secondary standard of 5.0 ppb. SCW has constructed an interconnection with the Metropolitan Water District of Southern California to provide for the needed supply for this system in the event the third well experiences levels of detection in excess of the DOHS standard.

SCW has met with the Regional Water Quality Control Board, the Orange County Water District, (OCWD), the City of Anaheim, the DOHS and three potentially responsible parties (PRP's) to define the extent of the MTBE contamination plume and assess the contribution from the PRP's. The PRP's have voluntarily initiated a work plan for regional investigation. While there have not been significant disruptions to the water supply in Yorba Linda at this point in time, no assurances can be given that MTBE contamination will not increase in the future. Negotiations with the PRPs on reimbursement of costs incurred to date and recovery of potential future costs associated with MTBE contamination have resulted in an agreement in principal on these and related issues. The parties anticipate execution of a definitive settlement agreement by the end of November 2003.

Matters Relating to SCW's Los Osos Water System

The compound MTBE has been detected in a well serving SCW's Los Osos water system. For some time SCW has been working with the Regional Water Quality Control Board as well as the owner of a service station. Although the owner of the service station has attempted remediation with funds provided through the California Underground Storage Tank Fund ("CUSTF"), it appears there will be insufficient funds from the CUSTF to complete remediation sufficient to return the well to service. In order to prevent the running of the statute of limitations, on August 12, 2002 SCW filed suit in the Superior Court of the State of California for the County of San Luis Obispo against the operators and owners of the service station facility, and Chevron USA Products, Inc., the supplier. A settlement with Chevron has been reached and a filing has been made for dismissal by the Court. The impacted well may need to be removed permanently from service and the settlement with Chevron is expected to afford SCW sufficient funds to commence siting and construction of a replacement well.

Matters Relating to SCW's San Gabriel Water Systems

Volatile Organic Compounds (VOC) and perchlorate have been detected in 2 wells servicing SCW's San Gabriel System. SCW filed suit, along with two other affected water purveyors and the San Gabriel Basin Water Quality Authority (WQA), in federal court against some of those responsible for the contamination. Some of the other potential defendants settled with SCW, other water purveyors and the WQA on VOC related issues prior to the filing of the lawsuit resulting in reimbursement to SCW of the \$1 million in capital cost of VOC treatment facilities and contribution of approximately \$380,000 towards future operating and maintenance (O&M) costs of the facilities.

In response to the filing of the Federal lawsuit, the Potentially Responsible Party (PRP) defendants filed motions to dismiss the suit or strike certain portions of the suit. Following a hearing on these motions on March 31, 2003, the judge issued a ruling on April 1, 2003 granting in part and denying in part the defendant's motions. A key ruling of the court was that the water purveyors, including the

Table of Contents

Registrant, by virtue of their ownership of wells contaminated with hazardous chemicals are themselves PRPs under the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA). Registrant has, pursuant to permission of the court, amended its suit to claim certain affirmative defenses as an “innocent” party under CERCLA. Registrant is presently unable to predict the outcome of this ruling on its ability to fully recover from the PRPs future costs associated with the treatment of these wells.

On August 29, 2003, the US Environmental Protection Agency issued Unilateral Administrative Orders (UAO) against 41 parties deemed responsible for polluting the groundwater in that portion of the San Gabriel Valley from which SCW’s two impacted wells draw water. SCW was not named as a party to the UAO. The UAO requires that these parties remediate the contamination. As a result of the issuance of the UAO, these parties have begun settlement discussions regarding the Federal lawsuits with SCW, the other two affected water purveyors and WQA. Registrant is presently unable to predict the ultimate outcome of these settlement discussions.

Three other wells serving customers in SCW’s San Gabriel customer service area are also impacted by VOC contamination. A settlement with several potentially responsible parties together with federal funds administered by WQA resulted in reimbursement of 100% of the \$1.1 million in capital costs, \$205,000 of past operations and maintenance costs and 100% of future operations and maintenance costs for a period of up to 30 years for VOC treatment facilities at these wells.

Bark Beetle Infestation in SCW’s Bear Valley Electric Service Area

In a Proclamation issued on March 7, 2003 Governor Gray Davis declared a State of Emergency with respect to a severe fire risk caused by dead and dying trees plagued by drought and a major bark beetle infestation in the counties of Riverside, San Bernardino, and San Diego of the State of California. The threat is continuing and shows no sign of abating. The CPUC issued on April 3, 2003 an order requiring Southern California Edison Company, San Diego Gas & Electric Company and Bear Valley Electric to take all reasonable and necessary actions to mitigate the increased fire hazard by removing dead, dying or diseased trees from falling or contacting distribution and transmission lines within their rights of way and to ensure compliance with existing vegetation clearance statutes and regulations. The utilities, including Bear Valley Electric (BVE), are authorized to make annual advice letter filings requesting recovery of the costs of removal and mitigation. SCW has determined the scope and magnitude of the bark beetle infestation in its BVE service territory to date and has formulated a course of action to mitigate the fire potential in its rights-of-way. Estimated costs, of dead tree removal based on experiences with other utility vegetation management programs and current information gathered and assessed for the Big Bear Lake area, totals \$620,000. These costs represent only the cost of addressing the problem to date. If the drought continues, the infestation will likely spread and costs mitigation costs may increase. SCW is confident that current and future costs incurred in remediation of Bark Beetle Infestation will be recoverable in rates through the annual Advice Letter filings, as the April 2003 order issued by the CPUC contained cost recovery provisions.

Security Issues

Since the tragic events of September 11, 2001, water utilities, including Registrant, have been advised to increase security at key facilities in order to avoid contamination of water supplies and other disruptions of service. In compliance with “*The Public Health Security and Bioterrorism Preparedness Act of 2002*” (HR 3448), Registrant has continued to implement measures to increase security, which includes a vulnerability assessment of its large systems. In addition to large system assessments, all systems operated by Registrant were assessed to identify potential areas requiring enhancements. These assessments resulted in a prioritized listing of recommended facility upgrades to enhance the safety of water system operations. Costs associated with capital improvements identified as a result of the assessment process, of approximately \$15 million, have been included in an application filed with the CPUC in October 2002.

Water Supply

SCW's Water Supply

For the three months ended September 30, 2003, SCW supplied a total of 27,826,000 ccf of water. Of this amount, approximately 50.2% came from pumped sources and 46.1% was purchased from others, principally the Metropolitan Water District of Southern California (MWD). SCW supplied 27,971,000 ccf of water for the same period of 2002, 51.9% of which came from pumped sources, 44.6% was purchased. The Bureau of Reclamation (the Bureau) supplied the remaining amount under a no-cost contract.

For the nine months ended September 30, 2003, SCW supplied a total of 65,672,000 ccf of water 53.3% of which came from pumped sources, 43.2% was purchased. During the nine months ended September 30, 2002, SCW produced 68,777,000 ccf of water. Of this amount 55.5% came from pumped sources, 41.9% was purchased and the remainder was provided by the Bureau.

For the twelve months ended September 30, 2003, SCW supplied a total of 84,805,000 ccf of water. Of this amount, approximately 54.0% came from pumped sources and 42.4% was purchased from others. For the twelve months ended September 30, 2002, SCW supplied 87,521,000 ccf of water, 57.0% of which came from pumped sources, 40.7% was purchased, and the Bureau supplied the remainder.

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. Registrant has 58 connections to the water distribution facilities of MWD and other municipal water agencies. MWD imports water from two principal sources: the Colorado River and the SWP. Available water supplies from the Colorado River and the SWP have historically been sufficient to meet most of MWD's requirements.

On October 17, 2003 Federal government, State government, and four Southern California water agency officials, including the MWD, met to sign the Quantification Settlement Agreement (QSA) which divides up California's share of the Colorado River. Under the QSA, MWD will have access (as in the past) to Colorado River water and up to 1.6 million acre feet of additional water from the state that the Imperial Irrigation District proposes to conserve and sell to the state. With the signing of this agreement California once again has access to excess Colorado River water for the next 13 years. However for the near term, excess water may not be available due to the recent drought in the Colorado watershed. MWD has also publicly stated that it is stepping up a number of efforts including desalination, conservation, recycling, transfer and storage, to increase water supplies.

SCW's water supply and revenues are significantly affected, both in the short-run and the long run, by changes in meteorological conditions. The 2003 water year, October 2002 to September 2003, has been a better water year than the 2002 water year. California experienced the third wettest April in 80 years of recorded history. April 2003 precipitation was 203% of normal. Overall for the water year California had 112% of normal precipitation. At the end of September California reservoirs were at 81% of normal. Statewide the seasonal runoff was 45,536,000 acre feet, which was 101% of average, as opposed to only 33,030,000 acre feet, 73% of average, last year. The National Oceanic and Atmospheric Association predicts that slightly warmer-than-average conditions are likely to persist for the next several months. The National Weather Service outlook for this winter is also warmer than normal temperatures with below normal precipitation levels for the West.

Although overall groundwater conditions remain at adequate levels, certain of SCW's groundwater supplies have been affected to varying degrees by various forms of contamination which, in some cases, has caused SCW to increase its reliance on purchased water in its supply mix. For further information, see Part II, Item 1 in Legal Proceedings.

Table of Contents

A sudden and unexplained drop in groundwater water supply severely impacted SCW's Wrightwood customer service area in the third quarter of 2002. In response to this emergency situation, SCW undertook a number of steps to provide water service, including trucking water into the area from nearby sources, bringing a formerly shut down well into service, taking steps to increase capacity at existing wells and expediting the drilling and equipping of a new well. SCW experienced increased operating costs associated with the trucking of water of approximately \$1.4 million (approximately \$1.26 million was incurred in 2002 and \$166,000 in the first quarter of 2003). Due to the actions of SCW and conservation efforts of consumers, the situation has stabilized and the water hauling ceased at end of January 2003. Management is unable to predict the extent to which additional costs may be incurred or the extent to which additional problems may be encountered. Additional wells and filtration equipment have been installed during the past 12 months and, along with voluntary conservation by the community, water supplies have been sustained throughout 2003. The cause of the unexplained and sudden drop in groundwater supply has not been identified, but it may be drought-related.

CCWC's Water Supply

Arizona precipitation level for the water year were between 70% and 89% of normal with the Colorado River area getting 82%. However this was a marked improvement over 2002 when precipitation was almost nonexistent. Of the four major reservoirs in Arizona only the San Carlos reservoir is extremely low at 10% of average. The Lake Pleasant and Verde River Reservoir System are well above normal at 191% and 179% respectively. For the water year the Colorado River inflow into Lake Mead was 48% of normal as compared to 23% for 2002. However, in spite of the increase flow, the long drought has brought the Colorado River storage to only 29,932,700 acre feet as compared to 33,702,300 acre feet at this time last year.

The Arizona Water Banking Authority (AWBA) was created to store Arizona's unused Colorado River water entitlement in western, central and southern Arizona to develop long-term storage credits to: (i) firm existing water supplies for municipal and industrial users during Colorado River shortages or Central Arizona Project (CAP) service interruptions; (ii) help meet the water management objectives of the Arizona Groundwater Code; and (iii) assist in the settlement of American Indian water rights claims. The AWBA successfully banked up to Arizona's full allocation of Colorado River entitlement in 2002, and expects the same result in 2003 as a hedge against drought conditions. Further, the first curtailment of CAP deliveries in the event of shortage would occur to non-Indian agricultural users. Such users accounted for 36% of CAP deliveries in 2002, creating a buffer for users such as CCWC. Though it is difficult to predict drought conditions with certainty, the activities of AWBA, and the priority for users of CAP, such as CCWC, provides an improved outlook for CCWC supplies.

CCWC obtains its water supply from three operating wells and from Colorado River water delivered by the CAP. The majority of CCWC's water supply is obtained from its CAP allocation and well water is used for peaking capacity in excess of treatment plant capability, during treatment plant shutdown, and to keep the well system in optimal operating condition.

CCWC has an Assured Water Supply designation, by decision and order of the Arizona Department of Water Resources, providing in part that, subject to its requirements, CCWC currently has a sufficient supply of ground water and CAP water which is physically, continuously and legally available to satisfy current and committed demands of its customers, plus at least two years of predicted demands, for 100 years. Notwithstanding such a designation, CCWC's water supply may be subject to interruption or reduction, in particular owing to interruption or reduction of CAP water. In the event of interruption or reduction of CAP water, CCWC can currently rely on its well water supplies for short-term periods. However, in any event, the quantity of water CCWC supplies to some or all of its customers may be interrupted or curtailed, pursuant to the provisions of its tariffs. CCWC has the physical capability to deliver water far in excess of that which is currently accounted for in CCWC's assured water supply account.

Table of Contents

CCWC has received a letter from the Arizona Department of Water Resources (ADWR) stating that the current and committed demand for water in CCWC's service area has exceeded CCWC's supply of water in their proven assured water supply account by 400 acre-feet per year. ADWR's letter requires CCWC to make up this accounting deficit by securing additional water supplies and/or providing information to ADWR that would allow ADWR to issue a new decision that CCWC's current and committed demands are within the proven available supplies in CCWC's assured water supply account.

Although CCWC had quickly lined up 1,000 acre-feet of CAP supply, the ADWR determined that the supply offered was not assured for 100 years. To meet the ADWR requirements, CCWC is reviewing the following options: (i) proving up the sufficiency of ADWR's calculations through a hydro-geological study, (ii) developing a method for developers in CCWC's service area to secure their own certificates of assured supply, (iii) securing recharge credits from the Fountain Hills Sanitary District, and (iv) contracting with agencies and neighboring utilities to purchase needed supply.

The ADWR letter is part of a routine administrative review of all water providers. ADWR's review will have no impact on CCWC's ability to deliver water to its existing customers. In cooperation with the Town of Fountain Hills and with ADWR's consent, CCWC will continue to review and approve subdivision plats within its service area but will temporarily suspend the plats' recordation until CCWC secures a new decision from ADWR that CCWC's current and committed demands are within the proven available supplies in CCWC's assured water supply account.

CCWC is working with ADWR to secure additional water supplies, including possibly excess Central Arizona Project (CAP) capacity, to make up the accounting deficit identified in ADWR's letter.

Risk Factor Summary

You should carefully read the risks described below and other information in this Form 10-Q in order to understand certain of the risks of our business.

Our liquidity and earnings could be adversely affected by changes in water supply costs

Prior to November 29, 2001, we recovered certain water supply costs through a balancing account mechanism. Water supply costs include the cost of purchased water and power and groundwater production assessments. Changes in the unit costs did not directly affect earnings. The balancing account was not, however, designed to insulate our earnings against changes in supply mix. As a result, we were not permitted to recover increased costs due to increased use of purchased water, which is generally more expensive than groundwater, through the balancing account mechanism. Increased costs of this nature were only recoverable, on a prospective basis, through the filing of a general rate case.

On November 29, 2001, the CPUC ordered us to suspend the use of the current water balancing account, and instead started a memorandum account for each offsettable expense of purchased water, purchased power and pump tax for our water service areas. Changes in water supply costs compared to the authorized amount, as well as any future authorized offset increases may directly affect our earnings. SCW's earnings were reduced by \$0.04, \$0.11 and \$0.22 per share, respectively, for the three, nine and twelve months ended September 30, 2003 as a result of this change in the methodology for recovering water supply costs. In June 2003, we received the CPUC's authorization to increase our rates to recover the pre November 29, 2001 balance in our supply costs balancing account.

In a decision issued on June 19, 2003, the CPUC concluded that our recovery of deferred water supply costs for providing water service will be reduced if we are earning more than our authorized rate of return. Pursuant to the resolution, we filed advice letters, on September 12, 2003, seeking recovery for under-collected balance of \$2.6 million for the period of November 29, 2001 through December 31, 2002. Future recovery of the under-collected balances is subject to the earning tests and the CPUC's review of

the reasonableness of the cost. For more information, see the section entitled “*Accounting for Supply Costs*” included in Part I, Item 2 in Management’s Discussion and Analysis of Financial Condition and Results of Operation

Our liquidity, and in certain circumstances, earnings, could be adversely affected by increases in electricity prices in California

Under California law, we are permitted to file for a rate increase to recover electric power costs not being recovered in current rates. Increases in electric power costs generally have no direct impact on profit margins, unless recovery of these costs is disallowed, but do affect cash flows and can therefore impact the amount of our capital resources. Electric power costs increased substantially in California during the fall of 2000 until the summer of 2001. On July 17, 2002, the FERC extended and modified the mitigation measures that were set to expire on September 30, 2002, citing delays in construction of new generation resources in California and throughout the West, delays in adopting a new market design and market rules by the Cal ISO, transmission line constraints, constraints on natural gas pipeline capacity and continuing dysfunctions in the power market. It remains unclear how long the FERC will leave its mitigation measures in place. The premature termination of such mitigation measures could result in a substantial increase in spot market prices and the prices of long-term contracts for power and capacity. In addition, a number of market reforms are under consideration at FERC. Certain of these reforms, if adopted, could result in significantly increased electric supply reserve requirements that have the potential for further cost increases.

On July 17, 2002, the CPUC approved a settlement authorizing us to include \$0.077 per kilowatt-hour (KWh) in rates to recover electric power costs at our Bear Valley Electric operation. If our actual annual costs exceed this amount, we cannot recover the excess and the amount will be expensed against income. If our actual annual energy costs are less than \$0.077 per KWh, we can use this difference to collect amounts previously included in the balancing account. The CPUC also has authorized SCW to collect a surcharge from its customers of 2.2¢ per Kwh for a period of up to ten years to enable SCW to recover the under-collection in its balancing account arising out of the energy crisis. SCW anticipates that the 2.2¢ surcharge on its electricity sales during the ten year period will be sufficient to enable SCW to recover the amount of this under-collection, with interest, during this ten year period.

The purchased power agreements with PWCC enable SCW to purchase a contractual volume of power at \$74.65 per megawatt hour (MWh). SCW also buys additional energy from the spot market to meet peak demand and sell surplus power to the spot market from time to time. SCW should be able to recover these costs up to the annual recovery cap of \$77, unless the CPUC determines that the costs incurred by SCW for purchasing power are not reasonable. The CPUC has not yet reviewed the purchased power agreements with PWCC or SCW’s spot market practices for reasonableness.

Significant claims have been asserted against us in water quality litigation

SCW and others have been sued in twenty-two water quality related lawsuits alleging personal injury and property damage as a result of the delivery of water that was allegedly contaminated. Nineteen of the lawsuits involve plaintiffs who received water from two groundwater basins in Los Angeles County. The other lawsuits involve plaintiffs in Sacramento County.

Table of Contents

In March 1998, the CPUC issued an Order Instituting Investigation as a result of water quality lawsuits being filed against water utilities in California. On November 2, 2000, the CPUC issued a final order concluding that (i) the CPUC has jurisdiction to regulate the service of water utilities with respect to the health and safety of that service; (ii) DOHS requirements governing drinking water quality adequately protect the public health and safety; and (iii) regulated water utilities, including SCW, have satisfactorily complied with past and present drinking water quality requirements.

On February 5, 2002, the California Supreme Court ruled that water utilities regulated by the CPUC may only be sued for damages based on allegations and ultimate proof that the utility failed to comply with federal and state safe drinking water requirements. As a result, plaintiffs may proceed on their claims against SCW to the extent that these claims are based on violations of federal and state law.

Persons that are potentially responsible for causing the contamination of groundwater supplies have also been increasingly asserting claims against water distributors on a variety of theories and have thus far successfully brought them within the class of potentially responsible parties thereby increasing the costs of seeking recovery from the potentially responsible parties and the risks associated with seeking recovery of these costs.

Our operating costs have increased and are expected to continue to increase as a result of groundwater contamination

Our operations have been impacted by groundwater contamination in certain of our service territories. We have taken a number of steps to address this contamination, including the removal of wells from service, the construction of water treatment facilities and securing alternative sources of supply from other areas not affected by the contamination.

In some cases, potentially responsible parties have reimbursed us for our costs. In other cases, we have taken legal action against parties that we believe to be potentially responsible for the contamination. To date, the CPUC has also permitted SCW to establish memorandum accounts for recovery of these types of costs, but actual recovery of these costs from ratepayers has been limited to filing only with a General Rate Case, generally every 3 years.

Environmental regulation has increased, and is expected to continue to increase our operating costs

SCW and CCWC 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 maximum contaminant levels
- Approved regulations requiring increased surface-water treatment to decrease the risk of microbial contamination; these regulations affect SCW's five surface water treatment plants and two CCWC plants
- Additional regulation of disinfection/disinfection byproducts
- Additional regulations requiring disinfection of certain groundwater systems
- Regulation of arsenic and radon
- Changes in the action level and the proposed adoption of maximum contamination levels for perchlorate and other by products of the production of rocket fuel

Table of Contents

SCW and CCWC may be able to recover costs incurred to comply with these regulations through the ratemaking process. We may also be able to recover certain of these costs under our contractual arrangements with municipalities. In certain circumstances, we may be able to recover costs from parties responsible or potentially responsible for contamination, either voluntarily or through specific court action.

The adequacy of our water supplies depends upon a variety of factors beyond our control

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

- Rainfall
- Availability of Colorado River water and imported water from northern California
- The amount of water stored in reservoirs and groundwater basins
- The amount of water used by our customers and others
- Water quality
- Legal limitations on use

Population growth and increases in the amount of water used have increased limitations on use to prevent over-drafting of groundwater basins. The importation of water from the Colorado River, one of SCW's important sources of supply, is expected to decrease in future years due to the requirements of the Central Arizona Project ("CAP") and disputes affecting the amount of water that the Metropolitan Water District of Southern California is entitled to take from the Colorado River. We have also taken wells out of service due to groundwater contamination. MWD is expected to increase its efforts to secure additional supplies from conservation, desalination and water exchanges with the agricultural water users.

CCWC obtains its water supply from operating wells and from the Colorado River through the CAP. CCWC's water supply may be subject to interruption or reduction if there is an interruption or reduction in CAP water.

Water shortages may affect us in a variety of 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 from third parties that may be responsible, or potentially responsible, for groundwater contamination.

Our earnings are greatly affected by weather during different seasons

The demand for water and electricity varies by season. Therefore, the results of operations for one period may not indicate results to be expected in another period. For instance, most water consumption occurs during the third quarter of each year when weather tends to be hot and dry. On warm days, use of water by residential and commercial customers may be significantly greater than on cold days because of the increased use of water for outdoor landscaping. Likewise the demand for electricity in our Big Bear service area is greatly affected by winter snows. An increase in winter snows reduces the use of snow making machines at ski resorts in the Big Bear area and, as a result reduces electric revenues. Likewise,

unseasonably warm weather during a skiing season may result in temperatures too high for snowmaking conditions also reducing electric revenues.

Variability of weather from normal temperatures or changes in snow or rainfall can materially impact results of operations. As a result, weather has been and will continue to be one of the dominant factors in our financial performance.

Our business is heavily regulated and, as a result, decisions by regulatory agencies and changes in laws and regulations can significantly affect our business

Our revenues depend substantially on the rates that we are permitted to charge our customers and our ability to recover our costs in these rates, including the ability to recover the costs of purchased water, groundwater assessments and electric power costs in rates. We have filed for increased water rates to recover operating costs from customers in all our water regions as well as for costs associated with general office activities. In addition, we will be seeking CPUC authorization to recover in rates for constructing an 8.4 MW natural gas-fueled generator facility to meet increasing demand in our Bear Valley customer service area.

The CPUC's resolution ordering SCW to suspend the use of the current water balancing account, and instead to start a memorandum account for its supply costs has and will directly impact our earnings since the recovery of deferred water supply costs is reduced if we are earning an amount in excess of our authorized rate of return. We have also been adversely affected by electric restructuring in California and the limitations that have been placed on our ability to recover these costs in rates.

Our costs have increased as a result of increasing environmental regulation, requirements to increase security at our water facilities and requirements to mitigate fire hazard risks in our Bear Valley Electric service area arising out of the drought and a major bark beetle infestation.

Our business requires significant capital expenditures

The utility business is capital intensive. On an annual basis, we spend significant sums for additions to or replacement of property, plant and equipment. During calendar years 2002, 2001 and 2000, we spent \$40,655,000, \$47,570,000, and \$46,091,000, respectively, for these purposes. Our budgeted capital expenditures for calendar year 2003 for these purposes are approximately \$84,637,000. There is no capital expenditure for environmental control facilities budgeted for 2003.

We obtain funds for these capital projects from operations, contributions by developers and others and advances from developers (which must be repaid). We also periodically borrow money or issue equity for these purposes. In addition, we secured a syndicated bank facility that we can use for these purposes. We cannot assure you that these sources will continue to be adequate or that the cost of funds will remain at levels permitting us to earn a reasonable rate of return.

New Accounting Pronouncements

We are subject to newly issued as well as changes in existing requirements issued by the Financial Accounting Standard Board. Differences in financial reporting between periods could occur unless and until the CPUC and the ACC approve such changes for conformity through regulatory proceedings. See *Note 6* of Notes to Consolidated Financial Statements.

Condemnation Actions

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, where doing so is in the public interest. In addition, however, the laws of the State of California also provide: (1) that the owner of the utility property may contest whether the condemnation is actually in the public interest; and (2) that the owner is entitled to receive the fair market value of its property if the property is ultimately taken. Although the City of Claremont, California located in SCW's Region III has not initiated the formal condemnation process pursuant to California law, the City has authorized the hiring of a consultant to perform an appraisal of the value of Registrant's water system serving that city. SCW intends to vigorously defend itself against any condemnation action if initiated by the City.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Registrant has certain block-forward purchase power contracts that qualify as derivative instruments under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*. A derivative financial instrument or other contract derives its value from another investment or designated benchmark. SCW is a party to various block-forward purchase power contracts. Power purchase contracts with Mirant and PWCC executed in 2001 qualify for the exception provided under SFAS No. 133 for activities that are considered normal purchases and normal sales. These contracts are reflected in the statements of income at the time of contract settlement. Contracts with PWCC executed in September 2002, however, do not qualify for the normal purchases and normal sales exception and, as a result, have been recognized at fair market value on the balance sheet as of September 30, 2003. This resulted in a pre-tax unrealized loss of \$420,000 and a pre-tax unrealized gain of \$854,000, respectively, for the three and nine months ended September 30, 2003. On a quarterly basis, the related asset or liability will be adjusted to reflect the fair market value at the end of each quarter. As this contract is settled, the realized gains or losses will be recorded and the unrealized gains or losses will be reversed.

Under the terms of its power purchase contracts with Mirant and PWCC, SCW is required to post security, at the request of the seller, if SCW is in default under the terms of the applicable contract. In addition, SCW's liquidity, and in certain circumstances, earnings could be adversely affected by increases in electricity prices in California. For further information, see the section entitled *"Critical Accounting Policies"* and *"Electric Energy Situation in California"* included in Part I, Item 2 in Management's Discussion and Analysis of Financial Condition and Results of Operation.

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

Item 4. Controls and Procedures

Registrant has established disclosure controls and procedures that are designed to provide reasonable assurance that information required to be disclosed in our periodic reports filed or submitted under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. In accordance with Exchange Act Rules 13a-15 and 15d-15, Registrant carried out an evaluation, under the supervision and with the participation of management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures were effective as of September 30, 2003 to provide reasonable assurance that information required to be disclosed in the reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

As noted earlier, Registrant is reviewing certain of its existing capital project contracting policies and procedures. However, there has been no change in the internal controls over financial reporting that occurred during the three months ended September 30, 2003 that has materially affected, or is reasonably likely to materially affect, the internal controls over financial reporting other than the weakness described in "*Controls and Procedures*" included in Part III, Item 14 of Registrant's Form 10K filed for the year ended December 31, 2002, which Registrant is in the process of correcting. Certain corrective actions, including the employment of qualified managerial staff, have already been taken.

PART II

Item 1. Legal Proceedings

Water Quality-Related Litigation

SCW is a defendant in twenty-two lawsuits involving claims pertaining to water quality. Nineteen of the lawsuits involve customer service areas located in Los Angeles County that have been filed in Los Angeles Superior Court: Robert Arenas, et al. v. Suburban Water Systems, Inc., et al., Case No. KC037559, Anthony John Bell, et al. v. City of Pomona, et al., Case No. KC038796, Adler, et al. v. Southern California Water Company, et al., Case No. BC169892, Santamaria, et al. v. Suburban Water Systems, et al., Case No. KC025995, Georgianna Dominguez et al. v. Southern California Water Company, et al., Case No. GC021657, Anderson, et al. v. Suburban Water Company, et al., Case No. KC028524, Abarca, et al. v. City of Pomona, et al., Case No. K027795, Celi, et al. v. San Gabriel Valley Water Company, Case No. GC020622, Boswell et al. v. Suburban Water Systems, et al., Case No. KC027318, Demciuc et al. v. Suburban Water Systems, et al., Case No. KC028732, Antoinette Adejare, et al. v. City of Pomona, et al., Case No. KC031096, Almelia Brooks, et al. v. Suburban Water System, et al., Case No. KC032915, Lori Alexander, et al. v. Suburban Water Systems, et al., Case No. KC031130, David Arnold, et al. v. City of Pomona, et al., Case No. KC034636, Gilda Ambrose-Dubre, et al. v. City of Pomona, et al., Case No. KC032906, Melissa Garrity Alvarado, et al. v. Suburban Water Systems et al., Case No. KC034953, Charles Alexander, et al. v. City of Pomona, et al., Case No. KC035526, Criner, et al. v. San Gabriel Valley Water Company, et al., Case No. GC021658, and Donerson, et al. v. City of Pomona, et al., Case No. KC035987. The lawsuits filed in Los Angeles County Superior Court are based on the allegations that SCW and the other defendants have provided and continue to provide plaintiffs with contaminated water from its wells, several of which are located in an area of the San Gabriel Valley that has been designated a federal superfund site, that the maintenance of this contaminated well water has resulted in contamination of the soil, subsurface soil and surrounding air with solvents and other substances, and that plaintiffs have been injured and their property damaged as a result. Three of the lawsuits involve a customer service area located in Sacramento County that have been filed in Sacramento County Superior Court: Nathaniel Allen, Jr. v. Aerojet-General Corporation, et al., Case No. 97AS06295, Daphne Adams, et al. v. Aerojet-General Corporation, et al., Case No. 98AS01025, and Wallace Andrew Pennington et al. v. Aerojet-General Corporation, et al., Case No. 00AS02622. The lawsuits filed in Sacramento County Superior Court are based on the allegations that SCW and other defendants have delivered water to plaintiffs that are contaminated with a number of chemicals, including trichloroethylene, perchloroethylene, carbon tetrachloride, perchlorate, Freon-113, hexavalent chromium and other unnamed chemicals and that plaintiffs have been injured and their property damaged as a result.

On September 1, 1999, the Court of Appeals in San Francisco held that the CPUC had preemptive jurisdiction over regulated public utilities with respect to water quality matters and ordered dismissal of a series of these lawsuits. On October 11, 1999, one group of plaintiffs appealed this decision to the California Supreme Court. On February 4, 2002, the California Supreme Court concluded that (i) the CPUC had preemptive jurisdiction over claims seeking injunctive relief and claims based on the theory that a public utility regulated by the CPUC provided unsafe drinking water even though it had complied with federal and state drinking water standards, but (ii) the CPUC did not have preemptive jurisdiction over damage claims based on allegations of violations of federal and state drinking water standards by public utilities regulated by the CPUC. As a result, damage claims based on allegations of violations of federal and state drinking water standards may proceed while the other claims must be dismissed.

In light of the breadth of plaintiff's claims, the lack of factual information regarding plaintiffs' claims and injuries, if any, the impact of the California Supreme Court decision on plaintiffs' claims and the fact that investigation is presently underway, SCW is unable at this time to determine what, if any, potential liability it may have with respect to these claims. Based upon the information currently available

to it, Registrant believes that these claims are without merit and intends to vigorously defend against these claims.

SCW is subject to self-insured retention provisions in its applicable insurance policies and has either expensed the self-insured amounts or has reserved against payment of these amounts as appropriate. SCW's various insurance carriers have, to date, provided reimbursement for costs incurred above the self-insured amounts for defense against these lawsuits, subject to a reservation of rights.

Order Instituting Investigation (OII)

In March 1998, the CPUC issued an OII to regulated water utilities in the state of California, including SCW. The purpose of the OII was to determine whether existing standards and policies regarding drinking water quality adequately protect the public health and whether those standards and policies were being uniformly complied with by those water utilities. On November 2, 2000, a final decision from the CPUC concluded that the CPUC has the jurisdiction to regulate the service of water utilities with respect to the health and safety of that service; that the California Department of Health Services requirements governing drinking water quality adequately protect the public health and safety; and that, based on an extensive review of 25 years of water quality records, regulated water utilities, including SCW, have satisfactorily complied with past and present drinking water quality requirements, except for one small unrelated water utility in Northern California.

The CPUC had previously authorized establishment of memorandum accounts to capture expenses related to the OII. Under the memorandum account procedure, SCW may recover litigation costs from ratepayers to the extent authorized by the CPUC. As of September 30, 2003, SCW had incurred a net cost of \$890,000 related to the OII, for which a reserve of the same amount was established. SCW filed for recovery of these amounts, through a special condition surcharge, with the CPUC in its application filing for its Region III and general office functions. See the section entitled "*Regulatory Matters*" in Part I, Item 2 in Management's Discussion and Analysis of Financial Conditions and Results of Operation.

Other Water Quality Litigation

On October 25, 1999, SCW filed a lawsuit against the State of California and its State Water Resources Control Board, Central Valley Regional Water Quality Control Board, and Department of Toxic Substances Control (collectively, the State) alleging that the State had substantially participated in a project to inject chemical pollution into portions of the Sacramento County groundwater basin and that pollution is progressively destroying the groundwater supply in SCW's Rancho Cordova water system. SCW and the State have entered into a comprehensive \$2,475,000 settlement for all of SCW's claims against the State, contingent upon the court's approval of the good faith of the settlement, which SCW received in full during the third quarter of 2003.

In a separate case, also filed on October 25, 1999, SCW sued Aerojet-General Corporation (Aerojet) for causing the contamination of eastern portions of the Sacramento County groundwater basin. A cross complaint filed by Aerojet against SCW for negligence and constituting a public nuisance was dismissed by the court in October 2002. On October 10, 2003 Registrant entered into a confidential memorandum of understanding with the Aerojet-General subsidiary of GenCorp, Inc. for the settlement of legal actions brought by SCW. The memorandum of understanding outlines the present financial terms of a settlement. A final settlement agreement incorporating the terms of the memorandum of understanding is underway and being negotiated at the date of this filing. As the parties continue to address issues related and additional to the memorandum of understanding, certain disagreements have developed. The parties continue to negotiate in an attempt to resolve those issues. However, no complete, documented agreement has been reached and it is presently impossible to predict when a final settlement of all issues will be reached.

The CPUC has authorized memorandum accounts to allow for recovery, from customers, of costs incurred by SCW in prosecuting the suits filed against the State and Aerojet, less any recovery from the

Table of Contents

defendants or others. As of September 30, 2003, approximately \$14.9 million in legal related costs has been recorded as Other Deferred Charges.

The CPUC has authorized SCW to increase rates, effective April 28, 2001, for recovery over a six-year period of approximately \$1.8 million, in expenses that were incurred on or before August 31, 2000, in the Aerojet matter. Management believes these costs, net of any reimbursement or settlement result are recoverable based on past practices of the CPUC but cannot give assurance that the CPUC will ultimately allow recovery of all or any of the remaining costs through rates.

The compound MTBE has been detected in a well serving SCW's Los Osos water system. For some time SCW has been working with the Regional Water Quality Control Board as well as the owner of a service station. Although the owner of the service station has attempted remediation with funds provided through the California Underground Storage Tank Fund ("CUSTF"), it appears there will be insufficient funds from the CUSTF to complete remediation sufficient to return the well to service. In order to prevent the running of the statute of limitations, on August 12, 2002 SCW filed suit in the Superior Court of the State of California for the County of San Luis Obispo against the operators and owners of the service station facility, and Chevron USA Products, Inc., the supplier. A settlement with Chevron has been reached and a filing has been made for dismissal by the Court. The impacted well may need to be removed permanently from service and the settlement with Chevron is expected to afford SCW sufficient funds to commence siting and construction of a replacement well.

Volatile Organic Compounds (VOC) and perchlorate have been detected in two wells servicing SCW's San Gabriel System. SCW filed suit, along with two other affected water purveyors and the San Gabriel Basin Water Quality Authority (WQA), in the federal court against some of those responsible for the contamination. Some of the other potential defendants settled with SCW, other water purveyors and the WQA on VOC related issues prior to the filing of the lawsuit. In response to the filing of the Federal lawsuit, the Potentially Responsible Party (PRP) defendants filed motions to dismiss the suit or strike certain portions of the suit. The judge issued a ruling on April 1, 2003 granting in part and denying in part the defendant's motions. A key ruling of the court was that the water purveyors, including the Registrant, by virtue of their ownership of wells contaminated with hazardous chemicals are themselves PRPs under the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA). Registrant has, pursuant to permission of the court, amended its suit to claim certain affirmative defenses as an "innocent" party under CERCLA. Registrant is presently unable to predict the outcome of this ruling on its ability to fully recover from the PRPs future costs associated with the treatment of these wells.

On August 29, 2003, the US Environmental Protection Agency issued Unilateral Administrative Orders ("UAO") against 41 parties deemed responsible for polluting the groundwater in that portion of the San Gabriel Valley from which SCW's two impacted wells draw water. SCW was not named as a party to the UAO. The UAO requires that these parties remediate the contamination. As a result of the issuance of the UAO, these parties have begun settlement discussions regarding the Federal lawsuits with SCW, the other two affected water purveyors and WQA. Registrant is presently unable to predict the ultimate outcome of these settlement discussions.

Electric Service Litigation

SCW has been, in conjunction with the Southern California Edison (Edison) unit of Edison International, planning to upgrade transmission facilities to 115kv (the 115kv Project) in order to meet increased energy and demand requirements for SCW's Bear Valley Electric Service area. On December 27, 2000, SCW filed a lawsuit against Edison for declaratory relief and seeking damages for breach of contract as a result of delays in the 115kv Project, violations of good faith and fair dealing, negligent misrepresentation, intentional misrepresentation and unjust enrichment. Subsequently Edison filed a cross-complaint against SCW for breach of contract, anticipatory breach, and quantum meruit. SCW has also sought declaratory relief from Edison's claims. To date, SCW has spent approximately \$3.0 million

Table of Contents

in this matter, all of which has been expensed. SCW has attended two mediation meetings with Edison in this matter and is discussing a settlement proposal. The parties have not, however, yet reached a mutually agreeable definitive settlement of the issues.

Other Litigation

Registrant is also subject to ordinary routine litigation incidental to its business. Other than as disclosed above, no other legal proceedings are pending, which are believed to be material.

Item 2. Changes in Securities

As of September 30, 2003, earned surplus amounted to \$89,953,000.

Neither AWR nor ASUS is subject to any contractual restriction on its ability to pay dividends. SCW's maximum ability to pay dividends is restricted by certain Note Agreements. Approximately \$159.9 million was available to pay dividends by SCW to AWR, after giving effect to these restrictions, at September 30, 2003.

AWR's ability to pay dividends on its Common Shares is dependent upon the payment of dividends from SCW. The ability of AWR, ASUS and SCW to pay dividends is also restricted by California law. A California corporation may generally pay a dividend to its shareholders if (i) the amount of its retained earnings immediately prior to the payment of the dividend equals or exceeds the amount of the dividend, or (ii) the sum of its assets (exclusive of goodwill, capitalized research and development expenses and deferred charges) would be at least equal to 1-1/4 times its liabilities (not including deferred taxes, deferred income and other deferred credits).

CCWC is subject to contractual restrictions on its ability to pay dividends. CCWC's maximum ability to distribute dividends is limited to maintenance of no more than 55% debt in the capital structure for the quarter immediately preceding the distribution. The ability of CCWC to pay dividends is also restricted by Arizona law. Approximately \$4.2 million was available to pay dividends from CCWC to AWR at September 30, 2003.

There are 709,379 and 63,906 Common Shares authorized but unissued under the Dividend Reinvestment and Stock Purchase Plan (DRP) and the 401(k) Plan, respectively, at September 30, 2003. Shares reserved for the 401(k) Plan are in relation to Company matching contributions and for investment purposes by participants.

Under Registrant's 2000 Stock Incentive Plan, stock options representing a total of 405,145 Common Shares upon exercise have been granted to certain eligible employees. An additional 1,050 shares are subject to grants of restricted stock. As of September 30, 2003, a total of 748,950 Common Shares is authorized but unissued under the 2000 Stock Incentive Plan.

AWR implemented a three-for-two split of AWR's common shares payable on June 7, 2002 to holders of record on May 15, 2002. Fractional shares were paid in cash. As a result of the stock split, the total number of Common Shares outstanding increased from approximately 10.1 million to 15.1 million.

On April 5, 2002, AWR redeemed the 4% and 4-1/4% series of \$25 Preferred Shares at the redemption price \$27.00 and \$26.50 per share, respectively, plus accrued and unpaid dividends to the redemption date. Subsequently on April 19, 2002, the 5% Series was redeemed at \$25.25 per share plus accrued and unpaid dividends to the redemption date.

[Table of Contents](#)

Item 3. Defaults Upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

No items were submitted during the third quarter of the fiscal year covered by this report to a vote of security holders through the solicitation of proxies or otherwise

Item 5. Other Information

On October 28, 2003, the Board of Directors of Registrant declared a regular quarterly dividend of \$0.221 per common share. The dividend will be paid December 1, 2003 to shareholders of record as of the close of business on November 8, 2003.

Item 6. Exhibits and Reports on Form 8-K

(a) The following documents are filed as Exhibits to this report:

*10.1 American States Water Company 2000 Stock Incentive Plan (As Amended April 2003)

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* This is a compensatory plan.

(b) On July 29, 2003, Registrant furnished a Form 8-K to the Securities and Exchange Commission announcing its earnings release for the three and twelve months ended June 30, 2003, and its quarterly dividend payment.

SIGNATURE

Pursuant to the requirements of Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized and as its principal financial officer.

AMERICAN STATES WATER COMPANY
and its subsidiary
SOUTHERN CALIFORNIA WATER COMPANY

By: /s/ McClellan Harris III

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

Dated: November 14, 2003

AMERICAN STATES WATER COMPANY
2000 STOCK INCENTIVE PLAN

.
. .
. .

TABLE OF CONTENTS

	Page

1. THE PLAN.....	1
1.1 Purpose.....	1
1.2 Administration and Authorization; Power and Procedure.....	1
1.3 Participation.....	2
1.4 Shares Available for Awards; Share Limits.....	3
1.5 Grant of Awards.....	3
1.6 Award Period.....	3
1.7 Limitations on Exercise and Vesting of Awards.....	4
1.8 Acceptance of Notes to Finance Exercise.....	4
1.9 No Transferability; Limited Exception to Transfer Restrictions.....	5
2. OPTIONS.....	6
2.1 Grants.....	6
2.2 Option Price.....	6
2.3 Limitations on Grant and Terms of Incentive Stock Options.....	6
2.4 Limits on 10% Holders.....	7
2.5 Option repricing/cancellation and Regrant/Waiver.....	8
2.6 Effects of Termination of Employment; Termination of Subsidiary Status; Discretionary Provisions.....	8
3. RESTRICTED STOCK AWARDS.....	9
3.1 Grants.....	9
3.2 Restrictions.....	9
3.3 Return to the Corporation.....	10
4. OTHER PROVISIONS.....	10
4.1 Rights of Eligible Employees, Participants and Beneficiaries.....	10
4.2 Adjustments; Acceleration.....	11
4.3 Effect of Termination of Service on Awards.....	13
4.4 Compliance with Laws.....	13
4.5 Tax Matters.....	14
4.6 Plan Amendment, Termination and Suspension.....	14
4.7 Privileges of Stock Ownership.....	15

4.8	Effective Date of the Plan.....	15
4.9	Term of the Plan.....	15
4.10	Governing Law/Construction/Severability.....	15
4.11	Captions.....	16
4.12	Stock-Based Awards in Substitution for Stock Options or Awards Granted by Other Corporation.....	16
4.13	Non-Exclusivity of Plan.....	16
4.14	No Corporate Action Restriction.....	16
4.15	Other Company Benefit and Compensation Program.....	17
5.	DEFINITIONS.....	17
5.1	Definitions.....	17

AMERICAN STATES WATER COMPANY
2000 STOCK INCENTIVE PLAN
(AS AMENDED AS OF APRIL 2003)

1. THE PLAN

1.1 Purpose

The purpose of this Plan is to promote the success of the Company by providing an additional means through the grant of Awards to attract, motivate, retain and reward key employees, including officers, whether or not directors, of the Company with awards and incentives for high levels of individual performance and improved financial performance of the Company. "Corporation" means American States Water Company and "Company" means the Corporation and its Subsidiaries, collectively. These terms and other capitalized terms are defined in Article 5.

1.2 Administration and Authorization; Power and Procedure.

(a) Committee. This Plan shall be administered by and all Awards to Eligible Employees shall be authorized by the Committee. Action of the Committee with respect to the administration of this Plan shall be taken pursuant to a majority vote or by written consent of its members.

(b) Plan Awards; Interpretation; Powers of Committee. Subject to the express provisions of this Plan, the Committee shall have the authority:

(i) to determine eligibility and, from among those persons determined to be eligible, the particular Eligible Employees who will receive an Award;

(ii) to grant Awards to Eligible Employees, determine the price at which securities will be offered or awarded and the amount of securities to be offered or awarded to any of such persons, and determine the other specific terms and conditions of such Awards consistent with the express limits of this Plan, and establish the installments (if any) in which such Awards shall become exercisable or shall vest, or determine that no delayed exercisability or vesting is required, and establish the events of termination or reversion of such Awards;

(iii) to approve the forms of Award Agreements (which need not be identical either as to type of award or among Participants);

(iv) to construe and interpret this Plan and any agreements defining the rights and obligations of the Company and Participants under this Plan, further define the terms used in this Plan, and prescribe, amend

and rescind rules and regulations relating to the administration of this Plan;

(v) to cancel, modify, or waive the Corporation's rights with respect to, or modify, discontinue, suspend, or terminate any or all outstanding Awards held by Eligible Employees, subject to any required consent under Section 4.6;

(vi) to accelerate or extend the exercisability or extend the term of any or all such outstanding Awards within the maximum ten-year term of Awards under Section 1.6; and

(vii) to make all other determinations and take such other action as contemplated by this Plan or as may be necessary or advisable for the administration of this Plan and the effectuation of its purposes.

(c) Binding Determinations/Liability Limitation. Any action taken by, or inaction of, the Corporation, any Subsidiary, the Board or the Committee relating or pursuant to this Plan and within its authority hereunder or under applicable law shall be within the absolute discretion of that entity or body and shall be conclusive and binding upon all persons. Neither the Board nor any Committee, nor any member thereof or person acting at the direction thereof, shall be liable for any act, omission, interpretation, construction or determination made in good faith in connection with this Plan (or any Award made under this Plan), and all such persons shall be entitled to indemnification and reimbursement by the Company in respect of any claim, loss, damage or expense (including, without limitation, attorneys' fees) arising or resulting therefrom to the fullest extent permitted by law and/or under any directors and officers liability insurance coverage that may be in effect from time to time.

(d) Reliance on Experts. In making any determination or in taking or not taking any action under this Plan, the Committee or the Board, as the case may be, may obtain and may rely upon the advice of experts, including professional advisors to the Corporation. No director, officer or agent of the Company shall be liable for any such action or determination taken or made or omitted in good faith.

(e) Delegation. The Committee may delegate ministerial, non-discretionary functions to individuals who are officers or employees of the Company.

1.3 Participation

Awards may be granted by the Committee only to those persons that the Committee determines to be Eligible Employees. An Eligible Employee who has been granted an Award may, if otherwise eligible, be granted additional Awards if the Committee shall so determine.

1.4 Shares Available for Awards; Share Limits.

(a) Shares Available. Subject to the provisions of Section 4.2, the capital stock that may be delivered under this Plan shall be shares of the Corporation's authorized but unissued Common Stock. The shares may be delivered for any lawful consideration.

(b) Share Limits. The maximum number of shares of Common Stock that may be delivered pursuant to Awards granted to Eligible Employees under this Plan shall not exceed 750,000 shares (the "Share Limit"). The maximum number of shares of Common Stock that may be delivered pursuant to options qualified as Incentive Stock Options granted under this Plan is 187,500 shares. The maximum number of shares subject to those options that are granted during any calendar year to any individual shall be limited to 50,000 and the maximum individual limit on the number of shares in the aggregate subject to all Awards that during any calendar year are granted under this Plan shall be 50,000. Each of the four foregoing numerical limits shall be subject to adjustment as contemplated by this Section 1.4 and Section 4.2.

(c) Share Reservation; Replenishment and Reissue of Unvested Awards. No Award may be granted under this Plan unless, on the date of grant, the sum of (i) the maximum number of shares issuable at any time pursuant to such Award, plus (ii) the number of shares that have previously been issued pursuant to Awards granted under this Plan, other than reacquired shares available for reissue consistent with any applicable legal limitations, plus (iii) the maximum number of shares that may be issued at any time after such date of grant pursuant to Awards that are outstanding on such date, does not exceed the Share Limit. Shares that are subject to or underlie Awards which expire or for any reason are cancelled or terminated, are forfeited, fail to vest, or for any other reason are not paid or delivered under this Plan, as well as reacquired shares, shall again, except to the extent prohibited by law, be available for subsequent Awards under the Plan. Except as limited by law, if an Award is or may be settled only in cash, such Award need not be counted against any of the limits under this Section 1.4.

1.5 Grant of Awards.

Subject to the express provisions of this Plan, the Committee shall determine the number of shares of Common Stock subject to each Award and the price (if any) to be paid for the shares or the Award. Each Award shall be evidenced by an Award Agreement signed by the Corporation and, if required by the Committee, by the Participant. The Award Agreement shall set forth the material terms and conditions of the Award established by the Committee consistent with the specific provisions of this Plan.

1.6 Award Period.

Each Award and all executory rights or obligations under the related Award Agreement shall expire on such date (if any) as shall be determined by the

Committee, but in the case of Options or other rights to acquire Common Stock not later than ten (10) years after the Award Date.

1.7 Limitations on Exercise and Vesting of Awards.

(a) Provisions for Exercise. Unless the Committee otherwise expressly provides, no Award shall be exercisable or shall vest until at least six months after the initial Award Date, and once exercisable an Award shall remain exercisable until the expiration or earlier termination of the Award.

(b) Procedure. Any exercisable Award shall be deemed to be exercised when the Secretary of the Corporation receives written notice of such exercise from the Participant, together with any required payment made in accordance with Section 2.2.

(c) Fractional Shares/Minimum Issue. Fractional share interests shall be disregarded, but may be accumulated. The Committee, however, may determine in the case of Eligible Employees that cash, other securities, or other property will be paid or transferred in lieu of any fractional share interests. No fewer than 100 shares may be purchased on exercise of any Award at one time unless the number purchased is the total number at the time available for purchase under the Award.

1.8 Acceptance of Notes to Finance Exercise.

The Corporation may, with the Committee's approval, accept one or more notes from any Eligible Employee in connection with the exercise or receipt of any outstanding Award; provided that any such note shall be subject to the following terms and conditions:

(a) The principal of the note shall not exceed the amount required to be paid to the Corporation upon the exercise or receipt of one or more Awards under the Plan and the note shall be delivered directly to the Corporation in consideration of such exercise or receipt.

(b) The initial term of the note shall be determined by the Committee; provided that the term of the note, including extensions, shall not exceed a period of five years.

(c) The note shall provide for full recourse to the Participant and shall bear interest at a rate determined by the Committee but not less than the interest rate necessary to avoid the imputation of interest under the Code.

(d) If the employment of the Participant terminates, the unpaid principal balance of the note shall become due and payable on the 10th business day after such termination; provided, however, that if a sale of such shares would cause such Participant to incur liability under Section 16(b) of the Exchange Act, the unpaid balance shall become due and payable on the 10th business day after the first day on which a sale of such shares could have been made without incurring such liability assuming for these

purposes that there are no other transactions (or deemed transactions in securities of this Corporation) by the Participant subsequent to such termination.

(e) If required by the Committee or by applicable law, the note shall be secured by a pledge of any shares or rights financed thereby in compliance with applicable law.

(f) The terms, repayment provisions, and collateral release provisions of the note and the pledge securing the note shall conform with applicable rules and regulations of the Federal Reserve Board as then in effect.

1.9 No Transferability; Limited Exception to Transfer Restrictions.

(a) Limit On Exercise and Transfer. Unless otherwise expressly provided in (or pursuant to) this Section 1.9, by applicable law and by the Award Agreement, as the same may be amended, (i) all Awards are non-transferable and shall not be subject in any manner to sale, transfer, anticipation, alienation, assignment, pledge, encumbrance or charge; Awards shall be exercised only by the Participant; and (ii) amounts payable or shares issuable pursuant to an Award shall be delivered only to (or for the account of) the Participant.

(b) Exceptions. The Committee may permit Awards to be exercised by and paid only to certain persons or entities related to the Participant, including but not limited to members of the Participant's immediate family, or trusts or other entities whose beneficiaries or beneficial owners are members of the Participant's immediate family, pursuant to such conditions and procedures as the Committee may establish. Any permitted transfer shall be subject to the condition that the Committee receive evidence satisfactory to it that the transfer is being made for essentially estate and/or tax planning purposes on a gratuitous or donative basis and without consideration (other than nominal consideration or in exchange for an interest in a qualified transferee). Notwithstanding the foregoing or anything to contrary in Section 1.9(c), ISOs and Restricted Stock Awards shall be subject to any and all additional transfer restrictions under the Code.

(c) Further Exceptions to Limits On Transfer. The exercise and transfer restrictions in Section 1.9(a) shall not apply to:

(i) transfers to the Corporation,

(ii) the designation of a beneficiary to receive benefits in the event of the Participant's death or, if the Participant has died, transfers to or exercise by the Participant's beneficiary, or, in the absence of a validly designated beneficiary, transfers by will or the laws of descent and distribution,

(iii) transfers pursuant to a QDRO order if approved or ratified by the Committee,

(iv) if the Participant has suffered a disability, permitted transfers or exercises on behalf of the Participant by his or her legal representative, or

(v) the authorization by the Committee of "cashless exercise" procedures with third parties who provide financing for the purpose of (or who otherwise facilitate) the exercise of Awards consistent with applicable laws and the express authorization of the Committee.

2. OPTIONS.

2.1 Grants.

One or more Options may be granted under this Article to any Eligible Employee. Each Option granted shall be designated in the applicable Award Agreement, by the Committee as either an Incentive Stock Option, subject to Section 2.3, or a Non-Qualified Stock Option.

2.2 Option Price.

(a) Pricing Limits. The purchase price per share of the Common Stock covered by each Option shall be determined by the Committee at the time of the Award, but shall not be less than 100% (110% in the case of an ISO granted to a Participant described in Section 2.4) of the Fair Market Value of the Common Stock on the date of grant.

(b) Payment Provisions. The purchase price of any shares purchased on exercise of an Option granted under this Article shall be paid in full at the time of each purchase in one or a combination of the following methods: (i) in cash or by electronic funds transfer; (ii) by check payable to the order of the Corporation; (iii) if authorized by the Committee or specified in the applicable Award Agreement, by a promissory note of the Participant consistent with the requirements of Section 1.8; (iv) by notice and third party payment in such manner as may be authorized by the Committee; or (v) by the delivery of shares of Common Stock of the Corporation already owned by the Participant, provided, however, that the Committee may in its absolute discretion limit the Participant's ability to exercise an Award by delivering such shares, and provided further that any shares delivered which were initially acquired upon exercise of a stock option must have been owned by the Participant at least six months as of the date of delivery. Shares of Common Stock used to satisfy the exercise price of an Option shall be valued at their Fair Market Value on the date of exercise.

2.3 Limitations on Grant and Terms of Incentive Stock Options.

(a) \$100,000 Limit. To the extent that the aggregate "Fair Market Value" of stock with respect to which incentive stock options first become exercisable by a Participant in any calendar year exceeds \$100,000, taking into account both Common Stock subject to Incentive Stock Options under this Plan and stock subject to incentive stock options under all other plans of the Company, such options shall be treated as

Nonqualified Stock Options. For this purpose, the "Fair Market Value" of the stock subject to options shall be determined as of the date the options were awarded. In reducing the number of options treated as incentive stock options to meet the \$100,000 limit, the most recently granted options shall be reduced first. To the extent a reduction of simultaneously granted options is necessary to meet the \$100,000 limit, the Committee may, in the manner and to the extent permitted by law, designate which shares of Common Stock are to be treated as shares acquired pursuant to the exercise of an Incentive Stock Option.

(b) Option Period. Each Option and all rights thereunder shall expire no later than 10 years after the Award Date.

(c) Other Code Limits. Incentive Stock Options may only be granted to Eligible Employees of the Corporation or a Subsidiary that satisfies the other eligibility requirements of the Code. There shall be imposed in any Award Agreement relating to Incentive Stock Options such other terms and conditions as from time to time are required in order that the Option be an "incentive stock option" as that term is defined in Section 422 of the Code.

2.4 Limits on 10% Holders.

No Incentive Stock Option may be granted to any person who, at the time the Option is granted, owns (or is deemed to own under Section 424(d) of the Code) shares of outstanding Common Stock possessing more than 10% of the total combined voting power of all classes of stock of the Corporation, unless the exercise price of such Option is at least 110% of the Fair Market Value of the stock subject to the Option and such Option by its terms is not exercisable after the expiration of five years from the date such Option is granted.

2.5 Option Repricing/Cancellation and Regrant/Waiver of Restrictions.

Subject to Section 1.4 and Section 4.6 and the specific limitations on Awards contained in this Plan, the Committee from time to time may authorize, generally or in specific cases only, for the benefit of any Eligible Employee any adjustment in the exercise or purchase price, the vesting schedule, the number of shares subject to, the restrictions upon or the term of, an Award granted under this Article by cancellation of an outstanding Award and a subsequent regranting of an Award, by amendment, by substitution of an outstanding Award, by waiver or by other legally valid means. Such amendment or other action may result in, among other changes, an exercise or purchase price which is higher or lower than the exercise or purchase price of the original or prior Award, provide for a greater or lesser number of shares subject to the Award, or provide for a longer or shorter vesting or exercise period; provided, however, that, except for adjustments contemplated by Section 4.2, any such amendment that results in the reduction of the exercise or purchase price below the exercise price or purchase price of the original or prior Award shall be subject to prior shareholder approval.

2.6 Effects of Termination of Employment; Termination of Subsidiary Status; Discretionary Provisions.

(a) Options - Resignation or Dismissal. If the Participant's employment by the Company terminates for any reason (the date of such termination being referred to as the "Severance Date") other than Retirement, Total Disability or death, or for Cause (as determined in the discretion of the Committee), the Participant shall have, unless otherwise provided in the Award Agreement and subject to earlier termination pursuant to or as contemplated by Section 1.6 or 4.2, three months after the Severance Date to exercise any Option to the extent it shall have become exercisable on the Severance Date. In the case of a termination for Cause, the Option shall terminate on the Severance Date. In other cases, the Option, to the extent not exercisable on the Severance Date, shall terminate.

(b) Options - Death or Disability. If the Participant's employment by the Company terminates as a result of Total Disability or death, the Participant, Participant's Personal Representative or his or her Beneficiary, as the case may be, shall have, unless otherwise provided in the Award Agreement and subject to earlier termination pursuant to or as contemplated by Section 1.6 or 4.2, until 12 months after the Severance Date to exercise any Option to the extent it shall have become exercisable by the Severance Date. Any Option to the extent not exercisable on the Severance Date shall terminate.

(c) Options - Retirement. If the Participant's employment by the Company terminates as a result of Retirement, the Participant, Participant's Personal Representative or his or her Beneficiary, as the case may be, shall have, unless otherwise provided in the Award Agreement and subject to earlier termination pursuant to or as contemplated by Section 1.6 or 4.2, until 12 months after the Severance Date to exercise any Option to the extent it shall have become exercisable by the Severance Date. The Option, to the extent not exercisable on the Severance Date, shall terminate.

(d) Committee Discretion. Notwithstanding the foregoing provisions of this Section 2.6, in the event of, or in anticipation of, a termination of employment with the Company for any reason, other than discharge for Cause, the Committee may, in its discretion, increase the portion of the Participant's Award available to the Participant, or Participant's Beneficiary or Personal Representative, as the case may be, or, subject to the provisions of Section 1.6, extend the exercisability period upon such terms as the Committee shall determine and expressly set forth in or by amendment to the Award Agreement.

3. RESTRICTED STOCK AWARDS.

3.1 Grants.

The Committee may, in its discretion, grant one or more Restricted Stock Awards to any Eligible Employee. Each Restricted Stock Award Agreement shall specify the number of shares of Common Stock to be issued to the Participant, the date of such issuance, the consideration for such shares (but not less than the minimum lawful consideration under applicable state law) by the Participant, the extent (if any) to which and the time (if ever) at which the Participant shall be entitled to dividends, voting and other rights in respect of the shares prior to vesting, and the restrictions (which may be based on performance criteria, passage of time or other factors or any combination thereof) imposed on such shares and the conditions of release or lapse of such restrictions. Such restrictions shall not lapse earlier than six months after the Award Date, except to the extent the Committee may otherwise provide. Stock certificates evidencing shares of Restricted Stock pending the lapse of the restrictions ("Restricted Shares") shall bear a legend making appropriate reference to the restrictions imposed hereunder and shall be held by the Corporation or by a third party designated by the Committee until the restrictions on such shares shall have lapsed and the shares shall have vested in accordance with the provisions of the Award and Section 1.7. Upon issuance of the Restricted Stock Award, the Participant may be required to provide such further assurance and documents as the Committee may require to enforce the restrictions.

3.2 Restrictions.

(a) Pre-Vesting Restraints. Except as provided in Section 3.1 and 1.9, restricted shares comprising any Restricted Stock Award may not be sold, assigned, transferred, pledged or otherwise disposed of or encumbered, either voluntarily or involuntarily, until the restrictions on such shares have lapsed and the shares have become vested.

(b) Dividend and Voting Rights. Unless otherwise provided in the applicable Award Agreement, a Participant receiving a Restricted Stock Award shall be entitled to cash dividend and voting rights for all shares issued even though they are not vested, provided that such rights shall terminate immediately as to any Restricted Shares which cease to be eligible for vesting.

(c) Cash Payments. If the Participant shall have paid or received cash (including any dividends) in connection with the Restricted Stock Award, the Award Agreement shall specify whether and to what extent such cash shall be returned (with or without an earnings factor) as to any restricted shares which cease to be eligible for vesting.

3.3 Return to the Corporation.

Unless the Committee otherwise expressly provides, Restricted Shares that remain subject to restrictions at the time of termination of employment or are subject to other conditions to vesting that have not been satisfied by the time specified in the applicable Award Agreement shall not vest and shall be returned to the Corporation in such manner and on such terms as the Committee shall therein provide.

4. OTHER PROVISIONS

4.1 Rights of Eligible Employees, Participants and Beneficiaries.

(a) Employment Status. Status as an Eligible Employee shall not be construed as a commitment that any Award will be made under this Plan to an Eligible Employee or to Eligible Employees generally.

(b) No Employment Contract. Nothing contained in this Plan (or in any other documents under this Plan or in any Award) shall confer upon any Eligible Employee or Participant any right to continue in the employ or other service of the Company, constitute any contract or agreement of employment or other service or affect an employee's status as an employee at will, nor shall interfere in any way with the right of the Company to change a person's compensation or other benefits, or to terminate his or her employment or other service, with or without cause. Nothing in this Section, however, is intended to adversely affect any express independent right of such person under a separate employment or service contract other than an Award Agreement.

(c) Plan Not Funded. Awards payable under this Plan shall be payable in shares or from the general assets of the Corporation, and (except as provided in Section 1.4(c)) no special or separate reserve, fund or deposit shall be made to assure payment of such Awards. No Participant, Beneficiary or other person shall have any right, title or interest in any fund or in any specific asset (including shares of Common Stock, except as expressly otherwise provided) of the Company by reason of any Award hereunder. Neither the provisions of this Plan (or of any related documents), nor the creation or adoption of this Plan, nor any action taken pursuant to the provisions of this Plan shall create, or be construed to create, a trust of any kind or a fiduciary relationship between the Company and any Participant, Beneficiary or other person. To the extent that a Participant, Beneficiary or other person acquires a right to receive payment pursuant to any Award hereunder, such right shall be no greater than the right of any unsecured general creditor of the Company.

4.2 Adjustments; Acceleration.

(a) Adjustments. Upon or in contemplation of any reclassification, recapitalization, stock split (including a stock split in the form of a stock dividend) or reverse stock split; any merger, combination, consolidation, or other reorganization; any spin-off, split-up, or similar extraordinary dividend distribution ("spin-off") in respect of the Common Stock (whether in the form of securities or property); any exchange of Common Stock or other securities of the Corporation, or any similar, unusual or extraordinary corporate transaction in respect of the Common Stock; or a sale of all or substantially all the assets of the Corporation as an entirety ("asset sale"); then the Committee shall, in such manner, to such extent (if any) and at such time as it deems appropriate and equitable in the circumstances:

(1) proportionately adjust any or all of (a) the number and type of shares of Common Stock (or other securities) that thereafter may be made the subject of Awards (including the specific maxima and numbers of shares set forth elsewhere in this Plan), (b) the number, amount and type of shares of Common Stock (or other securities or property) subject to any or all outstanding Awards, (c) the grant, purchase, or exercise price of any or all outstanding Awards, (d) the securities, cash or other property deliverable upon exercise of any outstanding Awards, or (e) (subject to limitations under Section 4.10(c)) the performance standards appropriate to any outstanding Awards, or

(2) make provision for a cash payment or for the assumption, substitution or exchange of any or all outstanding share-based Awards or the cash, securities or property deliverable to the holder of any or all outstanding share-based Awards, based upon the distribution or consideration payable to holders of the Common Stock upon or in respect of such event.

The Committee may adopt such valuation methodologies for outstanding Awards as it deems reasonable in the event of a cash or property settlement and, in the case of Options, but without limitation on other methodologies, may base such settlement solely upon the excess if any of the amount payable upon or in respect of such event over the exercise or strike price of the Award.

In each case, with respect to Awards of Incentive Stock Options, no adjustment shall be made in a manner that would cause the Plan to violate Section 422 or 424(a) of the Code or any successor provisions without the written consent of holders materially adversely affected thereby.

In any of such events, the Committee may take such action prior to such event to the extent that the Committee deems the action necessary to permit the Participant to realize the benefits intended to be conveyed with respect to the underlying shares in the same manner as is or will be available to shareholders generally.

(b) Possible Early Termination of Accelerated Awards. If any Option or other right to acquire Common Stock under this Plan has been fully accelerated as required or permitted by Section 4.2(c) but is not exercised prior to (1) a dissolution of the Company, or (2) an event described in Section 4.2(a) that the Company does not survive, or (3) the consummation of an event described in Section 4.2(a) involving a Change of Control Event approved by the Board, such Option or right shall terminate, subject to any provision that has been expressly made by the Board or the Committee, through a plan of reorganization or otherwise, for the survival, substitution, assumption, exchange or other settlement of such Option or right.

(c) Acceleration of Awards Upon Change in Control. Unless prior to a Change in Control Event the Committee determines that, upon its occurrence, benefits under any or all Awards shall not be accelerated or determines that only certain or limited benefits under any or all Awards shall be accelerated and the extent to which they shall be accelerated, and/or establishes a different time in respect of such Event for such acceleration, then upon the occurrence of a Change in Control Event:

(1) each Option shall become immediately exercisable, and

(2) Restricted Stock shall immediately vest free of restrictions.

Any discretion with respect to these events shall be limited to the extent required by applicable accounting requirements in the case of a transaction intended to be accounted for as a pooling of interests transaction.

The Committee may override the limitations on acceleration in this Section 4.2(c) by express provision in the Award Agreement and may accord any Eligible Employee a right to refuse any acceleration, whether pursuant to the Award Agreement or otherwise, in such circumstances as the Committee may approve. Any acceleration of Awards shall comply with applicable legal requirements and, if necessary to accomplish the purposes of the acceleration or if the circumstances require, may be deemed by the Committee to occur (subject to Section 4.2(d) a limited period of time not greater than 30 days before the event. Without limiting the generality of the foregoing, the Committee may deem an acceleration to occur immediately prior to the applicable event and/or reinstate the original terms of an Award if an event giving rise to an acceleration does not occur.

(d) Possible Rescission of Acceleration. If the vesting of an Award has been accelerated expressly in anticipation of an event or upon shareholder approval of an event and the Committee or the Board later determines that the event will not occur, the Committee may rescind the effect of the acceleration as to any then outstanding and unexercised or otherwise unvested Awards.

(e) Acceleration Upon Termination of Service Following a Change in Control.

(1) Termination After Change in Control. If any Participant's employment is terminated by the Company upon or within one year after a

Change in Control Event, and the termination is not the result of death, Total Disability, Retirement or a termination for Cause, then, subject to the other provisions of this Section 4.2 (including without limitation Section 4.2(b) and Section 4.4), all outstanding Options and other Awards held by the Participant shall be deemed fully vested immediately prior to the Severance Date, irrespective of the vesting provisions of the Participant's Award Agreement, unless the Award Agreement specifies a different result in the case of a Change in Control Event.

(2) No Extension Beyond Expiration.

Notwithstanding the foregoing, in no event shall an Award be reinstated or extended beyond its final expiration date.

4.3 Effect of Termination of Service on Awards.

(a) General. The Committee shall establish the effect of a termination of employment on the rights and benefits under each Award under this Plan and in so doing may make distinctions based upon the cause of termination.

(b) Events Not Deemed Terminations of Service. Unless Company policy or the Committee otherwise provides, the employment relationship shall not be considered terminated in the case of (i) sick leave, (ii) military leave, or (iii) any other leave of absence authorized by the Company or the Committee; provided that unless reemployment upon the expiration of such leave is guaranteed by contract or law, such leave is for a period of not more than 90 days. In the case of any Eligible Employee on an approved leave of absence, continued vesting of the Award while on leave from the employ of the Company shall be suspended, unless the Committee otherwise provides or applicable law otherwise requires. In no event shall an Award be exercised after the expiration of the term set forth in the Award Agreement.

(c) Effect of Change of Subsidiary Status. For purposes of this Plan and any Award, if an entity ceases to be a Subsidiary a termination of employment shall be deemed to have occurred with respect to each Eligible Employee in respect of the Subsidiary who does not continue as an Eligible Employee in respect of another entity within the Company.

4.4 Compliance with Laws.

This Plan, the granting and vesting of Awards under this Plan, the offer, issuance and delivery of shares of Common Stock, the acceptance of promissory notes and/or the payment of money under this Plan or under Awards are subject to compliance with all applicable federal and state laws, rules and regulations (including but not limited to state and federal securities law and federal margin requirements) and to such approvals by any listing, regulatory or governmental authority as may, in the opinion of counsel for the Company, be necessary or advisable in connection therewith. In addition, any securities delivered under this Plan may be subject to any special restrictions that the Committee may require to preserve a pooling of interests under generally accepted

accounting principles. The person acquiring any securities under this Plan will, if requested by the Company, provide such assurances and representations to the Company as the Committee may deem necessary or desirable to assure compliance with all applicable legal and accounting requirements.

4.5 Tax Matters.

(a) Provision for Tax Withholding or Offset. Upon any exercise, vesting, or payment of any Award or upon the disposition of shares of Common Stock acquired pursuant to the exercise of an Incentive Stock Option prior to satisfaction of the holding period requirements of Section 422 of the Code, the Company shall have the right at its option to (i) require the Participant (or Personal Representative or Beneficiary, as the case may be) to pay or provide for payment of the minimum amount of any taxes which the Company may be required to withhold with respect to such Award event or payment or (ii) deduct from any amount payable in cash the minimum amount of any taxes which the Company may be required to withhold with respect to such cash payment. In any case where a tax is required to be withheld in connection with the delivery of shares of Common Stock under this Plan, the Committee may in its sole discretion (subject to Section 4.4) grant (either at the time of the Award or thereafter) to the Participant the right to elect, pursuant to such rules and subject to such conditions as the Committee may establish, to have the Corporation reduce the number of shares to be delivered by (or otherwise reacquire) the appropriate number of shares valued at their Fair Market Value, to satisfy such minimum withholding obligation, determined in each case as of the trading day next preceding the applicable date of exercise, vesting or payment. Shares in no event shall be withheld in excess of the minimum number required for tax withholding under these provisions.

4.6 Plan Amendment, Termination and Suspension.

(a) Board Authorization. The Board may, at any time, terminate or, from time to time, amend, modify or suspend this Plan, in whole or in part. No Awards may be granted during any suspension of this Plan or after termination of this Plan, but the Committee shall retain jurisdiction as to Awards then outstanding in accordance with the terms of this Plan.

(b) Shareholder Approval. To the extent then required under Sections 162, 422 or 424 of the Code or any other applicable law, or by the provisions of Section 2.5 of the Plan, or deemed necessary or advisable by the Board, any amendment to this Plan shall be subject to shareholder approval.

(c) Amendments to Awards. Without limiting any other express authority of the Committee under (but subject to) the express limits of this Plan, the Committee by agreement or resolution may waive conditions of or limitations on Awards to Participants that the Committee in the prior exercise of its discretion has imposed, without the consent of a Participant, and (subject to the requirements of Section 1.2(b)) may make other changes to the terms and conditions of Awards that do not affect in any

manner materially adverse to the Participant, the Participant's rights and benefits under an Award.

(d) Limitations on Amendments to Plan and Awards. No amendment, suspension or termination of this Plan or change of or affecting any outstanding Award shall, without written consent of the Participant, affect in any manner materially adverse to the Participant any rights or benefits of the Participant or obligations of the Company under any Award granted under this Plan prior to the effective date of such change. Changes contemplated by Section 4.2 shall not be deemed to constitute changes or amendments for purposes of this Section 4.6.

4.7 Privileges of Stock Ownership.

Except as otherwise expressly authorized by the Committee or this Plan, a Participant shall not be entitled to any privilege of stock ownership as to any shares of Common Stock not actually delivered to and held of record by the Participant. No adjustment will be made for dividends or other rights as a shareholder for which a record date is prior to such date of delivery.

4.8 Effective Date of the Plan.

This Plan is effective as of January 27, 2000 the date of approval by the Board. The Plan shall be submitted for and subject to shareholder approval.

4.9 Term of the Plan.

No Award will be granted under this Plan after January 26, 2010 (the "termination date"). Unless otherwise expressly provided in this Plan or in an applicable Award Agreement, any Award granted prior to the termination date may extend beyond such date, and all authority of the Committee with respect to Awards hereunder, including the authority to amend an Award, shall continue during any suspension of this Plan and in respect of Awards outstanding on the termination date.

4.10 Governing Law/Construction/Severability.

(a) Choice of Law. This Plan, the Awards, all documents evidencing Awards and all other related documents shall be governed by, and construed in accordance with the laws of the State of California.

(b) Severability. If a court of competent jurisdiction holds any provision invalid and unenforceable, the remaining provisions of this Plan shall continue in effect.

(c) Plan Construction.

(1) Rule 16b-3. It is the intent of the Corporation that the Awards and transactions permitted by Awards be interpreted in a manner that, in the case of Participants who are or may be subject to Section 16 of the Exchange Act, satisfies the applicable requirements for exemptions

under Rule 16b-3. The exemption will not be available if the authorization of actions by any Committee of the Board with respect to such Awards does not satisfy the applicable conditions of Rule 16b-3. Notwithstanding the foregoing, the Corporation shall have no liability to any Participant for Section 16 consequences of Awards or events under Awards.

(2) Section 162(m). It is the further intent of the Company that (to the extent the Company or Awards under this Plan may be or become subject to limitations on deductibility under Section 162(m) of the Code), Options granted with an exercise or base price not less than Fair Market Value on the date of grant will qualify as performance-based compensation or otherwise be exempt from deductibility limitations under Section 162(m) of the Code, to the extent that the authorization of the Award (or the payment thereof, as the case may be) satisfies any applicable administrative requirements thereof.

4.11 Captions.

Captions and headings are given to the sections and subsections of this Plan solely as a convenience to facilitate reference. Such headings shall not be deemed in any way material or relevant to the construction or interpretation of this Plan or any provision thereof.

4.12 Stock-Based Awards in Substitution for Stock Options or Awards Granted by Other Corporation.

Awards may be granted to Eligible Employees under this Plan in substitution for employee stock options, stock appreciation rights, restricted stock or other stock-based awards granted by other entities to persons who are or who will become Eligible Employees in respect of the Company, in connection with a distribution, merger or other reorganization by or with the granting entity or an affiliated entity, or the acquisition by the Company, directly or indirectly, or all or a substantial part of the stock or assets of the employing entity.

4.13 Non-Exclusivity of Plan.

Nothing in this Plan shall limit or be deemed to limit the authority of the Board or the Committee to grant awards or authorize any other compensation, with or without reference to the Common Stock, under any other plan or authority.

4.14 No Corporate Action Restriction.

The existence of the Plan, the Award Agreements and the Awards granted hereunder shall not limit, affect or restrict in any way the right or power of the Board or the shareholders of the Corporation to make or authorize: (a) any adjustment, recapitalization, reorganization or other change in the Corporation's or any Subsidiary's capital structure or its business, (b) any merger, amalgamation, consolidation or change

in the ownership of the Corporation or any subsidiary, (c) any issue of bonds, debentures, capital, preferred or prior preference stock ahead of or affecting the Corporation's or any Subsidiary's capital stock or the rights thereof, (d) any dissolution or liquidation of the Corporation or any Subsidiary, (e) any sale or transfer of all or any part of the Corporation or any Subsidiary's assets or business, or (f) any other corporate act or proceeding by the Corporation or any Subsidiary. No participant, beneficiary or any other person shall have any claim under any Award or Award Agreement against any member of the Board or the Committee, or the Corporation or any employees, officers or agents of the Corporation or any Subsidiary, as a result of any such action.

4.15 Other Company Benefit and Compensation Program.

Payments and other benefits received by a Participant under an Award made pursuant to this Plan shall not be deemed a part of a Participant's compensation for purposes of the determination of benefits under any other employee welfare or benefit plans or arrangements, if any, provided by the Corporation or any Subsidiary, except where the Committee or the Board expressly otherwise provides or authorizes in writing. Awards under this Plan may be made in addition to, in combination with, as alternatives to or in payment of grants, awards or commitments under any other plans or arrangements of the Company or the Subsidiaries.

5. DEFINITIONS.

5.1 Definitions.

(a) "Award" means an award of any Option or Restricted Stock, or any combination thereof, whether alternative or cumulative, authorized by and granted under this Plan.

(b) "Award Agreement" means any writing setting forth the terms of an Award that has been authorized by the Committee.

(c) "Award Date" means the date upon which the Committee took the action granting an Award or such later date as the Committee designates as the Award Date at the time of the Award.

(d) "Award Period" means the period beginning on an Award Date and ending on the expiration date of such Award.

(e) "Beneficiary" means the person, persons, trust or trusts designated by a Participant or, in the absence of a designation, entitled by will or the laws of descent and distribution, to receive the benefits specified in the Award Agreement and under this Plan in the event of a Participant's death, and shall mean the Participant's executor or administrator if no other Beneficiary is designated and able to act under the circumstances.

(f) "Board" means the Board of Directors of the Corporation.

(g) "Cause" with respect to a Participant means (unless otherwise expressly provided in the applicable Award Agreement or another applicable contract with the Participant) a termination of employment based upon a finding by the Company, acting in good faith and based on its reasonable belief at the time, that the Participant:

(1) has failed to render services to the Company where such failure amounts to gross negligence or misconduct of the Participant's responsibility and duties; or

(2) has committed an act of fraud or been dishonest against the Company or any affiliate of the Company; or

(3) has been convicted of a felony or other crime involving moral turpitude.

A termination for Cause shall be deemed to occur (subject to reinstatement upon a contrary final determination by the Committee) on the date on which the Company first delivers written notice to the Participant of a finding of termination for Cause.

(h) "Change in Control Event" means any of the following events

(1) the dissolution or liquidation of either the Company, unless its business is continued by another entity in which holders of the Company's voting securities immediately before the event own, either directly or indirectly, more than 50% of the continuing entity's voting securities immediately after the event;

(2) any sale, lease, exchange or other transfer (in one or a series of transactions) of all or substantially all of the assets of either the Company, unless its business is continued by another entity in which holders of the Company's voting securities immediately before the event own, either directly or indirectly, more than 50% of the continuing entity's voting securities immediately after the event;

(3) any reorganization or merger of the Company, unless the holders of the Company's voting securities immediately before the event own, either directly or indirectly, more than 50% of the continuing or surviving entity's voting securities immediately after the event;

(4) an acquisition by any person, entity or group acting in concert of more than 50% of the voting securities of the Company, unless the holders of the Company's voting securities immediately before the event own, either directly or indirectly, more than 50% of the acquirer's voting securities immediately after the acquisition; or

(5) a change of one-half or more of the members of the Board of Directors of the Company within a twelve-month period, unless the election or nomination for election by shareholders of new directors within

such period constituting a majority of the applicable Board was approved by the vote of at least two-thirds of the directors then still in office who were in office at the beginning of the twelve-month period.

(i) "Code" means the Internal Revenue Code of 1986, as amended from time to time.

(j) "Commission" means the Securities and Exchange Commission.

(k) "Committee" means the Board or one or more committees appointed by the Board to administer all or certain aspects of this Plan, each committee to be comprised solely of one or more directors or such number as may be required under applicable law.

(l) "Common Stock" means the Common Stock of the Corporation and such other securities or property as may become the subject of Awards, or become subject to Awards, pursuant to an adjustment made under Section 4.2 of this Plan.

(m) "Company" means, collectively, the Corporation and its Subsidiaries.

(n) "Corporation" means American States Water Company, a California corporation, and its successors.

(o) "Eligible Employee" means an officer (whether or not a director) or key employee of the Company, including participants in the American States Water Company Annual Incentive Plan.

(p) "Exchange Act" means the Securities Exchange Act of 1934, as amended from time to time.

(q) "Fair Market Value" on any date means (1) if the stock is listed or admitted to trade on a national securities exchange, the closing price of the stock on the Composite Tape, as published in the Western Edition of The Wall Street Journal, of the principal national securities exchange on which the stock is so listed or admitted to trade, on such date, or, if there is no trading of the stock on such date, then the closing price of the stock as quoted on such Composite Tape on the next preceding date on which there was trading in such shares; (2) if the stock is not listed or admitted to trade on a national securities exchange, the last price for the stock on such date, as furnished by the National Association of Securities Dealers, Inc. ("NASD") through the NASDAQ National Market Reporting System or a similar organization if the NASD is no longer reporting such information; (3) if the stock is not listed or admitted to trade on a national securities exchange and is not reported on the National Market Reporting System, the mean between the bid and asked price for the stock on such date, as furnished by the NASD or a similar organization; or (4) if the stock is not listed or admitted to trade on a national securities exchange, is not reported on the National Market Reporting System and if bid and asked prices for the stock are not furnished by the NASD or a similar organization, the value as established by the Committee at such time for purposes of this Plan.

(r) "Incentive Stock Option" means an Option which is intended, as evidenced by its designation, as an incentive stock option within the meaning of Section 422 of the Code, the award of which contains such provisions (including but not limited to the receipt of shareholder approval of this Plan, if the Award is made prior to such approval) and is made under such circumstances and to such persons as may be necessary to comply with that section.

(s) "Nonqualified Stock Option" means an Option that is designated as a Nonqualified Stock Option and shall include any Option intended as an Incentive Stock Option that fails to meet the applicable legal requirements thereof. Any Option granted hereunder that is not designated as an incentive stock option shall be deemed to be designated a nonqualified stock option under this Plan and not an incentive stock option under the Code.

(t) "Option" means an option to purchase Common Stock granted under this Plan. The Committee shall designate any Option granted to an Eligible Employee as a Nonqualified Stock Option or an Incentive Stock Option.

(u) "Participant" means an Eligible Employee who has been granted an Award under this Plan.

(v) "Personal Representative" means the person or persons who, upon the disability or incompetence of a Participant, shall have acquired on behalf of the Participant, by legal proceeding or otherwise, the power to exercise the rights or receive benefits under this Plan and who shall have become the legal representative of the Participant.

(w) "Plan" means this 2000 Stock Incentive Plan, as it may be amended from time to time.

(x) "QDRO" means a qualified domestic relations order.

(y) "Restricted Shares" or "Restricted Stock" means shares of Common Stock awarded to a Participant under this Plan, subject to payment of such consideration, if any, and such conditions on vesting (which may include, among others, the passage of time, specified performance objectives or other factors) and such transfer and other restrictions as are established in or pursuant to this Plan and the related Award Agreement, for so long as such shares remain unvested under the terms of the applicable Award Agreement.

(z) "Retirement" means retirement from active service as an employee or officer of the Company on or after attaining age 65.

(aa) "Rule 16b-3" means Rule 16b-3 as promulgated by the Commission pursuant to the Exchange Act, as amended from time to time.

(bb) "Section 16 Person" means a person subject to Section 16(a) of the Exchange Act.

(cc) "Securities Act" means the Securities Act of 1933, as amended from time to time.

(dd) "Subsidiary" means any corporation or other entity a majority of whose outstanding voting stock or voting power is beneficially owned directly or indirectly by the Corporation.

(ee) "Total Disability" means a "permanent and total disability" within the meaning of Section 22(e)(3) of the Code and such other disabilities, infirmities, afflictions or conditions as the Committee by rule may include.

Exhibit 31.2

***Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
(18 U.S.C. Section 1350)***

I, McClellan Harris III, Chief Financial Officer, certify that:

- 1) I have reviewed this quarterly report on Form 10-Q for the period ended September 30, 2003 of American States Water Company and of Southern California Water Company (both referred to as “the Registrant”);
- 2) Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
- 3) Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;
- 4) The Registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the Registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) evaluated the effectiveness of the Registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - c) disclosed in this report any change in the Registrant’s internal control over financial reporting that occurred during the Registrant’s most recent fiscal quarter (the Registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant’s internal control over financial reporting.
- 5) The Registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant’s auditors and the audit committee of Registrant’s board of directors (or persons performing the equivalent function):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant’s ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant’s internal controls over financial reporting.

Dated: November 14, 2003

By: /s/ McCLELLAN HARRIS III

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

Exhibit 32.1

***Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
(18 U.S.C. Section 1350)***

I, Floyd E. Wicks, Chief Executive Officer of American States Water Company and Southern California Water Company (the "Registrant"), do hereby certify, pursuant to § 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350), that, to my knowledge:

- (1) the Quarterly Report on Form 10-Q of the Registrant for the quarter ended September 30, 2003, as filed with the Securities and Exchange Commission (the "Report"), fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Registrant.

/s/ Floyd E. Wicks

Floyd E. Wicks
Chief Executive Officer

Date: November 14, 2003

Exhibit 32.2

***Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
(18 U.S.C. Section 1350)***

I, McClellan Harris III, Chief Financial Officer of American States Water Company and Southern California Water Company (the "Registrant"), do hereby certify, pursuant to § 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350), that, to my knowledge:

- (1) the Quarterly Report on Form 10-Q of the Registrant for the quarter ended September 30, 2003, as filed with the Securities and Exchange Commission (the "Report"), fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Registrant.

/s/ McClellan Harris III

McClellan Harris III
Chief Financial Officer

Date: November 14, 2003