



full...





service.



Turn on your faucet. Even contending with severe drought in California, even facing more stringent water quality requirements, we reliably deliver clean, safe water for our customers. To fulfill this need, we've built one of the industry's strongest water portfolios, and are rebuilding our infrastructure mile by mile, pipe by pipe. Through aggressive conservation programs, we are also better managing our resources today so we can fully deliver tomorrow.

Dial your phone. No matter the problem, no matter what time of day or night our customers need help, we answer the call. Our service personnel, including our highly trained and experienced staff of engineers, certified water distribution operators, water and wastewater utility technicians and electric workers, address the full extent of any issue and respond in the shortest time possible. By tirelessly working to improve our company's efficiencies, we strive to keep our cost of service affordable to our customers.

Invest in your community. Over the last two years, Golden State Water Company (our utility subsidiary) spent \$160 million on upgrading its water and electric infrastructure and American States Utility Services (our contracted services subsidiary) spent \$142 million constructing and renewing water and wastewater systems for the nine military bases we serve. In 2015, Golden State Water Company alone expects to spend \$85-\$95 million of capital expenditures, including \$7 million for its electric division, Bear Valley Electric Service. That means new pipes and power lines, but it also means new construction jobs—and that is just one more way that we are fully investing in our communities.

Rely on us fully. No matter how you know us, whether as Golden State Water Company, Bear Valley Electric Service or American States Utility Services, we are a service company first. Because delivering fully takes more than delivering water and power.

It's delivering service in the fullest sense of the word.



## Letter to Our Shareholders,

Full is a good thing if you are in the business of providing water and other services as we are. Full, of course, is what we strive for in filling our proverbial glass. But for the people, businesses, and communities that rely on us daily, delivering fully isn't as simple as turning on the faucet or flipping a switch. That task of delivering exceptional customer service and real shareholder value takes a strategic plan and efficient operations that we continued to implement in 2014.

**Financial Results** Indeed, 2014 was another successful year for American States Water Company, as we strengthened our balance sheet through generating a high level of cash flow from operations, achieved a higher total return on our common stock than an index of the eight other publicly-traded water utilities in the U.S. and the S&P 500, and once again increased our dividend. We understand how important continued strong financial performance is to the Company and our customers as it allows us to successfully compete for capital at a lower cost to invest in our systems and maintain the reliability our customers expect. We earned \$1.57 per fully diluted share in 2014 and we achieved a consolidated return on equity for the year of 12.2%. Our consolidated performance reflects excellent financial results by our two first-tier subsidiaries: Golden State Water Company (GSWC), our regulated water and electric utility, and American States Utility Services, Inc. (ASUS), our contracted services business.

### 2014 Key Developments

- GSWC continued its focus on cost containment during 2014. The success of this initiative over the last few years is evidenced by a decrease in non-supply cost related operating expenses for 2014 compared to 2013, despite higher depreciation expenses and property taxes.<sup>1</sup> GSWC has continued to control staffing levels. Total employment at GSWC declined by approximately 4% in 2014 and has decreased by approximately 7% since 2010.
- In July, the water segment of GSWC filed its general rate case (GRC) for rates to customers for 2016–2018. While we have requested a capital expenditure budget of \$90 million for each year of the three-year period to ensure we continue to provide reliable service to our customers, our request represents a slight decrease in rates to customers on a total company basis. Under the California Public Utilities Commission's (CPUC's) rate case plan, water utilities are required to file rate applications every three years.
- ASUS continued to play a significant role for the Company, contributing \$0.31 per share, or approximately 20% of consolidated earnings and 22% of overall revenues and earning a higher return on investment than our well-performing regulated utilities.

<sup>1</sup> A one-time memo account recovery in 2013 and surcharges billed for the recovery of various costs previously incurred were excluded for this comparison.

- Because of our earnings growth in recent years and a dividend payout ratio that was lower than our peers, our board of directors approved a 5.2% increase in the quarterly dividend.
- The board also approved a share repurchase program, authorizing the Company to repurchase up to 1.25 million shares, or 3.2% of our outstanding common shares, through June 30, 2016. The program will enable the consolidated company to reduce its equity ratio (as a percent of total capitalization) to a level that is more in line on a weighted basis with appropriate capital structures for GSWC and ASUS. The Company repurchased 545,000 shares on the open market during 2014 as part of this program.
- During the year, GSWC received authorization from the CPUC to serve a new development in Sutter County near Sacramento, California. The development could add an additional 17,000 water customers at final build out, though this is expected to take many years.
- In July, Standard & Poor's Ratings Services raised its rating outlook to Positive from Stable for both American States Water and GSWC, as well as affirming the A+ credit ratings for both companies, which allows us to borrow at low rates to fund our capital and operational needs.
- ASUS favorably resolved its price redeterminations at Fort Bragg, Fort Jackson and Andrews Air Force Base during the third quarter, resulting in contract modifications which provided an increase in operation and maintenance management fee revenues, including retroactive amounts totaling \$1.7 million related to prior years. The contract modifications also provided additional renewal and replacement funding, which will be recognized in construction revenues when the work is performed.
- GSWC's electric utility segment received a final decision in its GRC for new rates for 2013–2016. The CPUC's final decision, which was retroactive to January 2013, did not have a significant impact on GSWC's 2014 financial statements. The decision provides for an authorized return on equity of 9.95% and also allows GSWC to invest \$19.5 million in capital projects for the years 2013–2016.
- We received special recognition from a study detailing the presence of women at the very top of the 400 largest publicly held corporations headquartered in California. We ranked fifth with approximately 43% of positions held by women among the board of directors and five highest-compensated executives, a testament to our workplace diversity and the opportunities provided at the Company.
- GSWC received The Black Business Association's *Utility Company of the Year Award*, given to the utility that has been most supportive of the growth and development of the Association and providing equal opportunities for diverse suppliers including women, minority and disabled veteran business enterprises.

**Working to Provide Above Market Returns to Shareholders Over the Long-Term** Our common stock achieved a total shareholder return (TSR) of 34.7% for 2014, higher than the S&P 500's TSR for 2014 of 13.7%. Over the past three years, the Company has achieved a compound annual return of 33.0% compared to a 20.4% return for the S&P 500 for this same period.

**60th Consecutive Year of Dividend Increases** 2014 marked the 60th consecutive year of increases in our annual dividend, placing us in an exclusive group of companies on the New York Stock Exchange who have achieved that result. Earnings from ASUS have grown significantly over the past five years and have contributed to our recent increases in the annual dividend. Our goal is to increase our dividend at a compound annual growth rate of 5 percent or more over the long term. We believe American States Water is well-positioned for future dividend growth. Our 2014 dividend-to-earnings payout ratio was approximately 54.3%, based on our current annualized dividend of \$0.852 per share. This is below the average payout ratio for the U.S. water utility industry and, along with growth in our future earnings, allows us the opportunity to increase the dividend in the future.

**GSWC: A Strategy that Works** GSWC continues to be our flagship subsidiary, as it is responsible for our water and electric utility operations. During 2014, it accounted for approximately 78% of American States' consolidated revenues and net income. The key tenets of GSWC's strategy continue to include: (i) delivering outstanding customer service; (ii) driving operational efficiency to minimize costs to our customers; (iii) making prudent capital additions and infrastructure investments; (iv) maintaining a strong water supply portfolio; (v) establishing a rate structure that provides the right customer incentives for conservation of precious resources and (vi) purchasing goods and services from diverse vendors.

**Delivering Outstanding Customer Service** GSWC has been in business for 85 years because we put customers first. We operate a call center 24 hours a day, 7 days per week, and 365 days per year while many other water providers do not. We think it is critical that if a customer has a problem with their water or electric service, they be able to contact us any time of day. In recent years, the Company has focused on improving our communication with customers, including electronic newsletters, improving the GSWC website, and providing more timely updates on capital projects and issues of interest to our stakeholders. We do not play politics with customer service – deferred maintenance and cutting corners puts customers, water supply and water quality at risk.

We would not have our well-earned reputation for customer service without the dedication of our employees. They know they have a very important job to do, which is to protect the communities we serve by delivering safe water and high-quality customer service. We will continue our commitment to attract and retain the talented employees needed to manage a very complex business.

**Driving Operational Efficiency to Minimize Costs to Our Customers** We continually look for ways to improve efficiency and manage our operating expenses to mitigate future rate increases. We understand that this is part of our commitment to customers and we have continually executed plans to stabilize costs and mitigate expense volatility. For instance, over the past few years we have redeemed long-term notes totaling \$45 million prior to their maturities due to the opportunity to borrow at lower interest rates. The Company's defined benefit pension plan was closed to new hires and a defined contribution retirement plan was implemented instead, which will lower costs over the long-term. Certain functions that had previously been done in-house were outsourced at reduced costs because the outside vendors had economies of scale that we could not match. We have recently centralized our procurement activities to allow us to more effectively purchase materials and services. In addition, we have reduced staff by about 7% since 2010 and continue to adjust while balancing customer service and cost. We are committed to continuously evaluating our processes to maximize efficiency and we're always cognizant of the importance of keeping customer rates affordable. As an example, as we developed our recent water general rate case filed in July 2014, we were able to pass along the cost savings to customers while continuing to invest in our systems.

**Making Prudent Capital Additions and Infrastructure Investments** Our capital investment program is a critical factor in delivering consistent, high-quality service to our customers. Water is an essential part of life and customers expect to receive safe, reliable uninterrupted service. GSWC continues to expend capital on infrastructure to ensure reliability and service to our customers in the best way possible. We expect to spend \$85-\$95 million in 2015. GSWC recovers its capital expenditures from customers through depreciation expense and a return on its rate base. Over the past five years, GSWC's net utility plant has increased from \$819.0 million at the end of 2009 to almost \$1 billion at the end of 2014.

**Maintaining a Strong Water Supply Portfolio** GSWC owns 73,000 acre-feet of adjudicated groundwater rights and a significant number of unadjudicated groundwater rights. In addition, GSWC owns 11,300 acre-feet of surface water rights. We remain intent on preserving the ever-increasing value of these water rights, particularly given the drought in California. We also maintain a strong conservation program to encourage customers to use less of this precious resource, and we look to innovative strategies, such as groundwater storage and new supplies, to ensure a robust water supply portfolio for the future.

Facing severe drought conditions in California, we are closely monitoring our water supplies. Our long-term plans involve increasing the diversity of our suppliers. As a result, GSWC continues to assess additional water supply opportunities to expand and firm up its water supply portfolio for service to customers.

**Establishing a Rate Structure That Provides the Right Incentives for Conservation** With the CPUC's encouragement, GSWC has implemented a tiered-structure in its water and electric rates to promote conservation. The tiered water rates were established to meet the State of California's goal of a 20% reduction in water use by 2020. As part of the implementation of these tiered rates, both the water and electric utility business segments were authorized by the CPUC to establish revenue adjustment mechanisms to decouple revenues from sales to ensure conservation would not compromise reliable operations and necessary capital investments. Due to the implementation of the tiered rate design and public awareness of the need for Californians to conserve, GSWC's water sales in 2014 were approximately 19.5% lower than water sales in 2007, the last full year before implementation of the tiered rates. As a result, GSWC was able to meet more of its customers' demand from its own water sources, decreasing dependency on expensive, purchased water.

Water conservation has not been our only commitment to protecting our environment. We have also secured the purchase of green energy as part of our supply portfolio to serve GSWC's electric customers. We have a ten year agreement for renewable resources allowing our electric segment to meet the renewables portfolio standard requirements of the CPUC.

**Purchasing Goods and Services from Diverse Vendors** GSWC has been committed to providing opportunities and forming partnerships within the diverse communities we serve. We continue to follow the guidelines established by the CPUC to increase the inclusion of Women, Minority and Disabled Veteran Business Enterprises (WMDVBE) in procurement opportunities at GSWC. We have increased our percentage of spend with WMDVBE vendors from 7.5% in 2004, when we started our Supplier Diversity Program, to 23.1% in 2014. This significant progress is a direct result of our commitment to diversity at all levels of the Company.

**ASUS: Solid Results for 2014 and an Exciting Future** ASUS performs operations, maintenance and capital construction activities on water and wastewater systems at eight military bases, and the wastewater system only at a ninth base, under fifty-year contracts with the U.S. government. This subsidiary had another solid year in 2014, generating operating revenues of \$104.7 million, pre-tax operating income of \$19.4 million, and contributing \$0.31 per share to consolidated earnings. ASUS provides American States Water with opportunities to improve companywide returns, grow the Company and diversify risk, and contribute to funding the overall dividend to shareholders. ASUS has also given us the opportunity to proudly serve the men and women in our nation's military.

Our strategy for ASUS is to increase the size and scope of our contracted services operations through: (i) further developing opportunities on the bases we currently serve and (ii) actively pursuing bases still to be privatized.

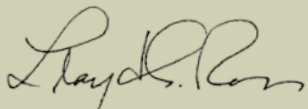
**Further Developing Opportunities on the Bases We Currently Serve** Like GSWC, ASUS is focused on providing excellent customer service and we continue to enhance our relationship with the U.S. government. We are proud that we receive high marks from the U.S. government for our customer service and that we continue to exceed our customer's requirements for small business utilization.

During 2014, ASUS spent \$65.4 million of construction cost in expanding and improving water and wastewater infrastructure on various military bases. Unlike GSWC, which earns a return on infrastructure investment, ASUS earns a profit on its construction activities. We substantially completed a number of projects in 2014 across ASUS and specifically at the Fort Bragg military base, including: (i) a \$58 million water and wastewater pipeline replacement project; (ii) a backflow preventer and meter project totaling \$23 million and (iii) a \$16.5 million water and wastewater infrastructure project required to serve a new growth area of Fort Bragg. There are also ongoing, smaller-scale projects at all military bases and we expect construction activities will continue to make a significant contribution to ASUS's earnings in 2015.

To be successful long-term, ASUS needs to be able to charge prices that reflect our current costs of serving the bases, plus a mark-up for profit. Under the military privatization program, a water or wastewater supplier has generally been allowed to file for a price increase two years after implementing a contract and every three years thereafter. These price increases are referred to as price redeterminations. A detailed description of our pending price redeterminations can be found on pages 51-52 of the 2014 SEC form 10-K.

**Actively Pursuing Bases Still to be Privatized** We are also aggressively responding to solicitations from the U.S. government on military bases where the water and wastewater utilities are in the process of being privatized to increase ASUS's footprint in utility privatization and to continue to be recognized as one of the premier providers of water and wastewater services. We have made several key hires so that we are able to respond to requests for proposals from the U.S. government timely and cost effectively. We anticipate continued expansion of privatizations by the U.S. government over the next five years and expect ASUS to be successful in growing its business as a result.

On behalf of everyone at American States Water Company and its subsidiaries, thank you for your continued trust and support.



Lloyd E. Ross  
Chairman of the Board



Robert J. Sprowls  
President and CEO

# 10-year statistical review

(dollars in thousands, except for per share and per customer amounts)

	2014	2013	2012
<b>Financial Information for Continuing Operations</b>			
<b>Revenues by Segment from Continuing Operations</b>			
Water Revenue	\$ 326,672	\$ 320,131	\$ 305,898
Electric Revenue	34,387	38,409	37,033
Contracted Services Revenue	104,732	113,537	123,977
Total Operating Revenues	465,791	472,077	466,908
Net Income	\$ 61,058	\$ 62,686	\$ 54,148
Diluted Earnings per Common Share	1.57	1.61	1.41
Total Assets	\$ 1,378,298	\$ 1,310,183	\$ 1,280,943
Net Utility Plant	1,003,520	981,477	917,791
Capital Additions	72,553	97,379	68,104
Long-term Debt	325,798	326,079	332,463
Investment per Customer	5,334	5,176	4,874
<b>Financial Information for Discontinued Operations</b>			
Water Revenues	\$ -	\$ -	\$ -
Net Income (loss)	-	-	-
Diluted Earnings (loss) per Common Share	-	-	-
<b>Financial Information for Consolidated Operations</b>			
Total Operating Revenues	\$ 465,791	\$ 472,077	\$ 466,908
Net Income	61,058	62,686	54,148
Diluted Earnings per Common Share	1.57	1.61	1.41
Dividends Declared per Common Share	0.831	0.760	0.635
Book Value per Common Share	13.24	12.72	11.82
<b>Operating Information for Continuing Operations</b>			
<b>Water Sold by Classification (mg)</b>			
Residential and Commercial	43,539	45,308	44,786
Industrial	434	437	422
Fire Service and Other	5,121	5,112	5,189
Total Water	49,094	50,858	50,397
Total Electric Sales (mwh)	126,850	134,129	130,784
<b>Water Production by Source (mg)</b>			
Purchased	18,430	19,291	19,077
Pumped - Electric and Gas	30,486	32,663	32,035
Gravity and Surface	2,881	2,972	3,049
Total Supply	51,797	54,926	54,161
<b>Customers by Classification*</b>			
Residential and Commercial	250,035	249,051	247,648
Industrial	345	342	351
Fire Service and Other	7,811	7,709	7,658
Total Water	258,191	257,102	255,657
Electric	23,716	23,615	23,379
Total Company	281,907	280,717	279,036
Miles of Main in Service	2,792	2,789	2,786
Number of Employees as of December 31	709	723	725

mg = millions of gallons      mwh = mega-watt hours

\* In addition, as of December 31, 2014 the Company had six contracts with the U.S. government for its contracted services business.



	2011	2010	2009	2008	2007	2006	2005
\$	300,450	\$ 291,617	\$ 266,114	\$ 241,435	\$ 231,235	\$ 216,171	\$ 198,845
	36,275	35,799	28,920	28,422	28,573	29,266	27,222
	83,188	72,360	59,132	42,358	34,914	16,449	5,213
	419,913	399,776	354,166	312,215	294,722	261,886	231,280
\$	42,010	\$ 31,091	\$ 29,374	\$ 25,996	\$ 27,121	\$ 21,857	\$ 25,061
	1.11	0.83	0.81	0.75	0.78	0.63	0.74
\$	1,238,362	\$ 1,192,035	\$ 1,113,293	\$ 1,061,287	\$ 964,675	\$ 936,955	\$ 873,135
	896,500	854,956	822,027	780,148	733,105	712,384	675,516
	80,281	79,050	77,459	77,018	49,867	66,599	71,184
	340,395	299,839	300,221	260,561	260,941	261,248	261,540
	4,689	4,422	4,227	3,987	3,716	3,551	3,344
\$	3,492	\$ 8,745	\$ 7,722	\$ 7,472	\$ 7,704	\$ 7,755	\$ 7,019
	3,849	2,106	157	(3,991)	909	1,224	1,705
	0.10	0.06	0.01	(0.12)	0.03	0.04	0.05
\$	423,405	\$ 408,521	\$ 361,888	\$ 319,687	\$ 302,426	\$ 269,641	\$ 238,299
	45,859	33,197	29,531	22,005	28,030	23,081	26,766
	1.21	0.89	0.82	0.63	0.81	0.67	0.79
	0.550	0.520	0.505	0.500	0.478	0.455	0.450
	10.88	10.13	9.70	8.98	8.77	8.32	7.86
	43,220	44,057	48,169	51,679	54,531	53,175	52,254
	420	429	442	483	622	711	776
	4,439	4,526	4,924	5,625	5,817	5,380	4,536
	48,079	49,012	53,535	57,787	60,970	59,266	57,566
	134,216	132,167	136,365	137,358	140,441	141,235	134,066
	18,077	19,005	21,504	25,244	26,506	27,521	29,027
	30,805	30,583	33,562	34,431	35,874	34,896	32,734
	3,116	3,264	3,162	3,232	3,216	1,890	1,801
	51,998	52,852	58,228	62,907	65,596	64,307	63,562
	247,838	247,607	247,275	246,891	247,270	246,910	245,950
	350	352	356	363	374	368	370
	7,747	7,603	7,367	7,228	6,902	6,692	6,525
	255,935	255,562	254,998	254,482	254,546	253,970	252,845
	23,508	23,257	23,234	23,172	23,273	23,248	22,966
	279,443	278,819	278,232	277,654	277,819	277,218	275,811
	2,780	2,782	2,753	2,727	2,724	2,720	2,707
	732	707	692	658	557	543	532

# American States Water Company Locations

Customers

## 1. GOLDEN STATE WATER COMPANY

### Northern District

Arden/Rancho Cordova	16,331
Bay Point	5,011
Clearlake	2,177

### Coastal District

Los Osos	3,267
Ojai	2,897
Santa Maria	13,650
Simi Valley	13,368

### Central District

Central Basin East	20,102
Central Basin West	20,209
Culver City	9,642

### Southwest District

Southwest	52,263
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### Foothill District

Claremont	11,123
San Dimas	16,081
San Gabriel	12,363

### Mountain/Desert District

Victorville/Apple Valley	2,927
Barstow	8,960
Calipatria	1,178
Morongo Valley	969
Wrightwood	2,732

### Orange County District

Los Alamitos	27,456
Placentia	15,485

**BEAR VALLEY ELECTRIC SERVICE** 23,716

**TOTAL** **281,907**



## 2. AMERICAN STATES UTILITY SERVICES, INC.

American States Utility Services, Inc., contracts with the U.S. government and private entities to provide operation and maintenance and capital construction and improvements (collectively, “services”) of potable water and wastewater systems as identified below:



### 3. TEXAS / NEW MEXICO

Fort Bliss Water Services Company provides services to the United States Army at the Fort Bliss military installation in El Paso, Texas. The service area also includes Dona Ana, MacGregor, and Myers Range Camps located in New Mexico.

### 4. MARYLAND

Terrapin Utility Services, Inc. provides services to the United States Air Force at Andrews Air Force Base in Maryland.

### 5. VIRGINIA

Old Dominion Utility Services, Inc provides services to the United States Army at Fort Eustis and Story in Virginia. In addition, ODUS provides services for the wastewater system at Fort Lee, Virginia for the United States Army.

### 6. NORTH CAROLINA

Old North Utility Services, Inc. provides services to the United States Army at Fort Bragg in North Carolina.

### 7. SOUTH CAROLINA

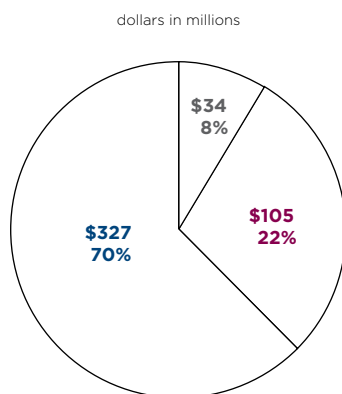
Palmetto State Utility Services, Inc. provides services to the United States Army at Fort Jackson in South Carolina.

# Financial Highlights

(in thousands, except per share amounts)

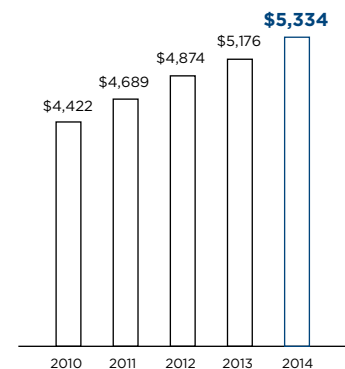
	2014	2013	Variance	% Change
<b>Income Statement Information</b>				
Total Operating Revenue	\$ 465,791	\$ 472,077	\$ (6,286)	-1.3%
Total Operating Expense	346,746	353,005	(6,259)	-1.8%
Operating Income	119,045	119,072	(27)	0.0%
Interest Charges (net)	20,690	21,708	(1,018)	-4.7%
Net Income from Operations	61,058	62,686	(1,628)	-2.6%
Basic Earnings Per Common Share	1.57	1.61	(0.04)	-2.5%
Dividends Declared per Common Share	0.831	0.760	0.07	9.3%
Average Number of Shares Outstanding	38,658	38,639	19	0.0%
Average Number of Diluted Shares Outstanding	38,880	38,869	11	0.0%
Fully Diluted Earnings per Common Share	\$ 1.57	\$ 1.61	\$ (0.04)	-2.5%
<b>Balance Sheet Information</b>				
Total Assets	\$ 1,378,298	\$ 1,310,183	\$ 68,115	5.2%
Net Utility Plant	1,003,520	981,477	22,043	2.2%
Common Shareholders' Equity	506,801	492,404	14,397	2.9%
Long-Term Debt	325,798	326,079	(281)	-0.1%
Total Capitalization	832,599	818,483	14,116	1.7%
Book Value per Common Share	\$ 13.24	\$ 12.72	\$ 0.52	4.1%

## 2014 Revenues By Segment



- Golden State Water Company-Water Utility
- Golden State Water Company-Electric Utility
- American States Utility Services, Inc.

## Investment Per Customer



# Form 10-K





SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

FOR ANNUAL AND TRANSITION REPORTS
PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

(Mark One)

[X] Annual Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2014 or
[ ] Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from to

Table with 3 columns: Commission File Number, Registrant, State of Incorporation Address, Zip Code and Telephone Number, and IRS Employer Identification No. Rows include American States Water Company and Golden State Water Company.

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

Table with 2 columns: Title of Each Class and Name of Each Exchange on Which Registered. Row: American States Water Company Common Shares, New York Stock Exchange.

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

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

American States Water Company Yes [X] No [ ]
Golden State Water Company Yes [ ] No [X]

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

American States Water Company Yes [ ] No [X]
Golden State Water Company Yes [ ] No [X]

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 Yes [X] No [ ]
Golden State Water Company Yes [X] No [ ]

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

American States Water Company Yes [X] No [ ]
Golden State Water Company Yes [X] No [ ]

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

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

American States Water Company
Large accelerated filer [X] Accelerated filer [ ] Non-accelerated filer [ ] Smaller reporting company [ ]

Golden State Water Company
Large accelerated filer [ ] Accelerated filer [ ] Non-accelerated filer [X] Smaller reporting company [ ]

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act)

American States Water Company Yes [ ] No [X]
Golden State Water Company Yes [ ] No [X]

The aggregate market value of all voting Common Shares held by non-affiliates of American States Water Company was approximately \$1,288,725,000 and \$1,517,357,000 on June 30, 2014 and February 23, 2015, respectively. The closing price per Common Share of American States Water Company on February 23, 2015, as quoted in The Wall Street Journal website, was \$39.70. As of February 23, 2015, the number of Common Shares of American States Water Company outstanding was 38,220,567. As of that same date, American States Water Company owned all 146 outstanding Common Shares of Golden State Water Company. The aggregate market value of all voting stock held by non-affiliates of Golden State Water Company was zero on June 30, 2014 and February 23, 2015.

Golden State Water Company meets the conditions set forth in General Instruction I(1)(a) and (b) of Form 10-K and is therefore filing this Form, in part, with the reduced disclosure format for Golden State Water Company.

Documents Incorporated by Reference:

Portions of the Proxy Statement of American States Water Company will be subsequently filed with the Securities and Exchange Commission as to Part III, Item Nos. 10, 11, 13 and 14 and portions of Item 12, in each case as specifically referenced herein.

**AMERICAN STATES WATER COMPANY  
and  
GOLDEN STATE WATER COMPANY**

**FORM 10-K**

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## PART I

### **Item 1. Business**

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

AWR makes its periodic reports, Form 10-Q and Form 10-K, and current reports, Form 8-K, available free of charge through its website, [www.aswater.com](http://www.aswater.com), as soon as material is electronically filed with or furnished to the Securities and Exchange Commission (“SEC”). Such reports are also available on the SEC’s internet website at <http://www.sec.gov>. AWR also makes available free of charge its code of business conduct and ethics, its corporate governance guidelines and the charters of its Board of Directors, Nominating and Governance Committee, Compensation Committee, and Audit and Finance Committee through its website or by calling (800) 999-4033. AWR and GSWC have filed the certification of officers required by Section 302 of the Sarbanes-Oxley Act as Exhibits 31.1 and 31.2 to its Form 10-K for the year ended December 31, 2014.

### **General**

AWR is the parent company of GSWC and American States Utility Services, Inc. (“ASUS”) and its subsidiaries (Fort Bliss Water Services Company (“FBWS”), Terrapin Utility Services, Inc. (“TUS”), Old Dominion Utility Services, Inc. (“ODUS”), Palmetto State Utility Services, Inc. (“PSUS”) and Old North Utility Services, Inc. (“ONUS”). AWR was incorporated as a California corporation in 1998 as a holding company. AWR has three reportable segments: water, electric and contracted services. Within the segments, AWR has two principal business units, water and electric service utility operations, conducted through GSWC, and contracted services conducted through ASUS and its subsidiaries. FBWS, TUS, ODUS, PSUS and ONUS may be referred to herein individually as a “Military Utility Privatization Subsidiary” or collectively as the “Military Utility Privatization Subsidiaries.”

GSWC is a California public utility company engaged principally in the purchase, production and distribution of water in 75 communities in 10 counties in the State of California. GSWC is regulated by the California Public Utilities Commission (“CPUC”). It was incorporated as a California corporation on December 31, 1929. GSWC also provides electric service to the City of Big Bear Lake and surrounding areas in San Bernardino County, California through its Bear Valley Electric Service (“BVES”) division.

GSWC served 258,191 water customers and 23,716 electric customers at December 31, 2014, or a total of 281,907 customers, compared with 257,102 water customers and 23,615 electric customers at December 31, 2013, or a total of 280,717 customers. GSWC’s utility operations exhibit seasonal trends. Although GSWC’s water utility operations have a diversified customer base, residential and commercial customers account for the majority of GSWC’s water sales and revenues. Revenues derived from commercial and residential water customers accounted for approximately 90% of total water revenues for the years ended December 31, 2014, 2013 and 2012.

ASUS, through its wholly-owned subsidiaries, has contracted with the U.S. government to provide water and/or wastewater services at various military installations. ASUS operates, maintains and performs construction activities on water and/or wastewater systems at various United States military bases pursuant to 50-year firm, fixed-price with prospective price-redetermination contracts. Each of the contracts with the U.S. government may be subject to termination, in whole or in part, prior to the end of the 50-year term for convenience of the U.S. government or as a result of default or nonperformance by the subsidiary performing the contract. The contract price for each of these contracts is subject to redetermination every three years following the initial two years of the contract. Prices are also subject to equitable adjustment based upon changes in circumstances, changes in laws and/or regulations and changes in wages and fringe benefits to the extent provided in the contract. AWR guarantees performance of ASUS’s military privatization contracts.

Pursuant to the terms of these contracts, the Military Utility Privatization Subsidiaries operate, as of the effective date of their respective contracts, the following water and wastewater systems:

- FBWS - water and wastewater systems at Fort Bliss located near El Paso, Texas and extending into southeastern New Mexico effective October 1, 2004;
- TUS - water and wastewater systems at Andrews Air Force Base in Maryland effective February 1, 2006;

- ODUS - wastewater system at Fort Lee in Virginia effective February 23, 2006 and the water and wastewater systems at Fort Eustis and Fort Story in Virginia (“TRADOC”) effective April 3, 2006;
- PSUS - water and wastewater systems at Fort Jackson in South Carolina effective February 16, 2008; and
- ONUS - water and wastewater systems at Fort Bragg, Pope Army Airfield and Camp Mackall, North Carolina effective March 1, 2008.

Certain financial information for each of AWR’s business segments - water distribution, electric distribution, and contracted services - is set forth in Note 16 to the Notes to Consolidated Financial Statements of American States Water Company and its subsidiaries. AWR’s water and electric distribution segments are not dependent upon a single or only a few customers. The U.S. government is the primary customer for ASUS’s contracted services. ASUS, from time to time, performs work at military bases for other prime contractors of the U.S. government.

The revenue from AWR’s segments is seasonal. The impact of seasonality on these AWR businesses is discussed in more detail in Item 1A — “*Risk Factors*.”

Environmental matters and compliance with such laws and regulations are discussed in detail in Item 7 — “*Management’s Discussion and Analysis of Financial Condition and Results of Operation*” under the section titled “Environmental Matters.”

### **Competition**

The businesses of GSWC are substantially free from direct and indirect competition with other public utilities, municipalities and other public agencies within their existing service territories. However, GSWC may be subject to eminent domain proceedings in which government agencies, under state law, may acquire GSWC’s water systems if doing so is necessary and in the public’s interest. GSWC competes with governmental agencies and other investor-owned utilities in connection with offering service to new real estate developments on the basis of financial terms, availability of water and ability to commence providing service on a timely basis. AWR’s other subsidiary, ASUS, actively competes for business with other investor-owned utilities, other third party providers of water and/or wastewater services and governmental entities primarily on the basis of price and quality of service.

### **AWR Workforce**

AWR and its subsidiaries had a total of 707 employees as of February 19, 2015. GSWC had 552 employees as of February 19, 2015. Sixteen employees in GSWC’s Bear Valley Electric Service (“BVES”) customer service area are covered by a collective bargaining agreement with the International Brotherhood of Electrical Workers, which expires in December 2017. Sixty-three employees in GSWC’s Region II are covered by a collective bargaining agreement with the Utility Workers Union of America, which expired in 2014. GSWC is currently in negotiations with this union on a new labor agreement. GSWC has no other unionized employees.

ASUS had 155 employees as of February 19, 2015. Fifteen of the employees at FBWS are covered by a collective bargaining agreement with the International Union of Operating Engineers. This agreement expires in 2017.

### **Forward-Looking Information**

This Form 10-K and the documents incorporated herein contain forward-looking statements intended to qualify for the “safe harbor” from liability established by the Private Securities Litigation Reform Act of 1995. Forward-looking statements are based on current estimates, expectations and projections about future events and assumptions regarding these events and include statements regarding management’s goals, beliefs, plans or current expectations, taking into account the information currently available to management. Forward-looking statements are not statements of historical facts. For example, when we use words such as “anticipate,” “believe,” “plan,” “estimate,” “expect,” “intend,” “may” and other words that convey uncertainty of future events or outcomes, we are making forward-looking statements. We are not able to predict all the factors that may affect future results. We caution you that any forward-looking statements made by us are not guarantees of future performance and actual results may differ materially from those in our forward-looking statements. Some of the factors that could cause future results to differ materially from those expressed or implied by our forward-looking statements, or from historical results, include, but are not limited to:

- The outcome of pending and future regulatory, legislative or other proceedings, investigations or audits, including decisions in our general rate cases and the results of independent audits of our construction contracting procurement practices or other independent audits of our costs

- Changes in the policies and procedures of the CPUC
- Timeliness of CPUC action on rates
- Availability of water supplies, which may be adversely affected by the California drought, changes in weather patterns in the West, contamination and court decisions or other governmental actions restricting the use of water from the Colorado River, the California State Water Project, and/or pumping of groundwater
- Our ability to efficiently manage GSWC capital expenditures and operating and maintenance expenses within CPUC authorized levels and timely recovery of our costs through rates
- The impact of increasing opposition to GSWC rate increases on our ability to recover our costs through rates
- The impact of condemnation actions on the size of our customer base
- Our ability to forecast the costs of maintaining GSWC's aging water and electric infrastructure
- Our ability to recover increases in permitting costs and in costs associated with negotiating and complying with the terms of our franchise agreements with cities and counties and other demands made upon us by the cities and counties in which GSWC operates
- Changes in accounting valuations and estimates, including changes resulting from our assessment of anticipated recovery of regulatory assets, liabilities and revenues subject to refund or regulatory disallowances
- Changes in environmental laws and water and wastewater quality requirements and increases in costs associated with complying with these laws and requirements
- Our ability to obtain adequate, reliable and cost-effective supplies of chemicals, electricity, fuel, water and other raw materials that are needed for our water and wastewater operations
- Our ability to recover the costs associated with the contamination of GSWC's groundwater supplies from parties responsible for the contamination or through the ratemaking process, and the time and expense incurred by us in obtaining recovery of such costs
- Adequacy of our electric division's power supplies and the extent to which we can manage and respond to the volatility of electric and natural gas prices
- Our electric operation's ability to comply with the CPUC's renewable energy procurement requirements
- Changes in GSWC long-term customer demand due to changes in customer usage patterns as a result of conservation efforts, regulatory changes affecting demand such as new landscaping or irrigation requirements, recycling of water by the customer or purchase of recycled water supplied by other parties, unanticipated population growth or decline, changes in climate conditions, general economic and financial market conditions and cost increases
- Changes in accounting treatment for regulated utilities
- Changes in estimates used in ASUS's revenue recognition under the percentage of completion method of accounting for construction activities at our contracted services business
- Termination, in whole or in part, of one or more of our Military Utility Privatization Subsidiaries' contracts to provide water and/or wastewater services at military bases for the convenience of the U.S. government or for default
- Termination of contracts and suspension or debarment for a period of time from contracting with the government due to violations of federal law or regulations in connection with military utility privatization activities
- Failure of the U.S. government to make timely payments to ASUS for water and/or wastewater services at military bases as a result of fiscal uncertainties over the funding of the U.S. government
- Delays in obtaining redetermination of prices or equitable adjustments to our prices on one or more of our contracts to provide water and/or wastewater services at military bases

- Disallowance of costs on any of our contracts to provide water and/or wastewater services at military bases as a result of audits, cost reviews or investigations by contracting agencies
- Inaccurate assumptions used in preparing bids in our contracted services business
- Failure of the wastewater systems that we operate on military bases resulting in untreated wastewater or contaminants spilling into nearby properties, streams or rivers
- Failure to comply with the terms of our military privatization contracts
- Failure of any of our subcontractors to perform services for us in accordance with the terms of our military privatization contracts
- Issues with the implementation, maintenance and/or upgrading of our information technology systems
- General economic conditions which may impact our ability to recover infrastructure investments and operating costs from customers
- Explosions, fires, accidents, mechanical breakdowns, the disruption of information technology and telecommunication systems, human error and similar events that may occur while operating and maintaining water and electric systems in California or operating and maintaining water and wastewater systems on military bases under varying geographic conditions
- The impact of storms, earthquakes, floods, mudslides, drought, wildfires, disease and similar natural disasters, or acts of terrorism or vandalism, that affect customer demand or that damage or disrupt facilities, operations or information technology systems owned by us, our customers or third parties on whom we rely
- Potential costs, lost revenues, or other consequences resulting from misappropriation of assets or sensitive information, corruption of data, or operational disruption in connection with a cyber-attack or other cyber incident
- Restrictive covenants in our debt instruments or changes to our credit ratings on current or future debt that may increase our financing costs or affect our ability to borrow or make payments on our debt
- Our ability to access capital markets and other sources of credit in a timely manner on acceptable terms

Please consider our forward-looking statements in light of these risks as you read this Form 10-K. We qualify all of our forward-looking statements by these cautionary statements.

## **Item 1A — Risk Factors**

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

### ***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 at GSWC depend substantially on the rates and fees we charge our customers and the ability to recover our costs on a timely basis, including the ability to recover the costs of purchased water, groundwater assessments, electric power, natural gas, chemicals, water treatment, security at water facilities and preventative maintenance and emergency repairs. Any delays by the CPUC in granting rate relief to cover increased operating and capital costs at our public utilities or delays in obtaining approval of our requests at ASUS for equitable adjustments or price redeterminations for contracted services from the U.S. government may adversely affect our financial performance. We may file for interim rates in California in situations where there may be delays in granting final rate relief during a general rate case proceeding. If the CPUC approves lower rates, the CPUC will require us to refund to customers the difference between the interim rates and the rates approved by the CPUC. Similarly, if the CPUC approves rates that are higher than the interim rates, the CPUC may authorize us to recover the difference between the interim rates and the final rates. Interim rates may also be granted by the U.S. government, should there be delays in the price redetermination process.

Regulatory decisions may also impact prospective revenues and earnings, affect the timing of the recognition of revenues and expenses, may overturn past decisions used in determining our revenues and expenses and could result in impairment charges and customer refunds. Management continually evaluates the anticipated recovery of regulatory assets, liabilities and revenues subject to refund and provides for allowances and/or reserves as deemed necessary. In the event that our assessment of the probability of recovery through the ratemaking process is incorrect, we will adjust the associated regulatory asset or liability to reflect the change in our assessment or any regulatory disallowances. A change in our evaluation of the probability of recovery of regulatory assets or a regulatory disallowance of all or a portion of our costs could have a material adverse effect on our financial results.

We are also, in some cases, required to estimate future expenses and in others, we are required to incur the expense before recovering costs. As a result, our revenues and earnings may fluctuate depending on the accuracy of our estimates, the timing of our investments or expenses or other factors. If expenses increase significantly over a short period of time, we may experience delays in recovery of these expenses, the inability to recover carrying costs for these expenses and increased risks of regulatory disallowances or write-offs.

Regulatory agencies may also change their rules and policies which may adversely affect our profitability and cash flows. Changes in policies of the U.S. government may also adversely affect one or more of our Military Utility Privatization Subsidiaries. In certain circumstances, the U.S. government may be unwilling or unable to appropriate funds to pay costs mandated by changes in rules and policies of federal or state regulatory agencies. The U.S. government may disagree with the increases that we request and may delay approval of requests for equitable adjustment or redetermination of prices which could adversely affect our anticipated rates of return.

We may also be subject to fines or penalties if a regulatory agency determines that we have failed to comply with laws, regulations or orders applicable to our businesses, unless we appeal this determination, or our appeal of an adverse determination is denied. Regulatory agencies may also disallow certain costs if audit findings determine that we have failed to comply with our policies and procedures for procurement or other practices.

### ***Our costs involved in maintaining water quality and complying with environmental regulation have increased and are expected to continue to increase***

Our capital and operating costs at GSWC can increase substantially as a result of increases in environmental regulation arising from increases in the cost of disposing of residuals from our water treatment plants, upgrading and building new water treatment plants, compliance monitoring activities and securing alternative supplies when necessary. GSWC may be able to recover these costs through the ratemaking process. We may also be able to recover these costs under settlement and contractual arrangements.

### ***We may sustain losses that exceed or are excluded from our insurance coverage or for which we are not insured***

We are, from time to time, parties to legal or regulatory proceedings. These proceedings may pertain to regulatory investigations, employment matters or other disputes. Management periodically reviews its assessment of the probable outcome of these proceedings, the costs and expenses reasonably expected to be incurred, and the availability and extent of insurance coverage. On the basis of this review, management establishes reserves for such matters. We may, however, from

time to time be required to pay fines, penalties or damages that exceed our insurance coverage and/or reserves if our estimate of the probable outcome of such proceedings proves to be inaccurate.

We maintain insurance coverage as part of our overall legal and risk management strategy to minimize our potential liabilities. However, our insurance policies contain exclusions and other limitations that may not cover our potential liabilities. Generally, our insurance policies cover property, worker's compensation, employer's liability, general liability and automobile liability. Each policy includes deductibles or self-insured retentions and policy limits for covered claims. As a result, we may sustain losses that exceed or that are excluded from our insurance coverage or for which we are not insured.

### **Additional Risks Associated with our Public Utility Operations**

#### ***Our operating costs may increase as a result of groundwater contamination***

Our operations can be impacted by groundwater contamination in certain service territories. Historically, we have taken a number of steps to address contamination, including the removal of wells from service, decreasing the amount of groundwater pumped from wells in order to slow the movement of plumes of contaminated water, constructing water treatment facilities and securing alternative sources of supply from other areas not affected by the contamination. In emergency situations, we have supplied our customers with bottled water until the emergency situation has been resolved.

Our ability to recover these types of costs depends upon a variety of factors, including approval of rate increases, the willingness of potentially responsible parties to settle litigation and otherwise address the contamination and the extent and magnitude of the contamination. We may recover costs from certain third parties that may be responsible, or potentially responsible, for groundwater contamination. However, we often experience delays in obtaining recovery of these costs and incur additional costs associated with seeking recovery from responsible or potentially responsible parties which may adversely impact our liquidity. In some events we may be unable to recover all of these costs from third parties due to the inability to identify the potentially responsible parties, the lack of financial resources of responsible parties or the high litigation costs associated with obtaining recovery from responsible or potentially responsible parties.

We can give no assurance regarding the adequacy of any such recovery to offset the costs associated with contamination or the cost of recovery of any legal costs. To date, the CPUC has permitted us to establish memorandum accounts for potential recovery of these types of costs when they arise.

Management believes that rate recovery, proper insurance coverage and reserves are in place to appropriately manage these types of contamination issues. However, such issues, if ultimately resolved unfavorably to us, could, in the aggregate, have a material adverse effect on our results of operations and financial condition.

#### ***The adequacy of our water supplies depends upon weather and a variety of other uncontrollable factors***

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

- Rainfall, basin replenishment, flood control, snow pack levels in California and the West, reservoir levels and availability of reservoir storage;
- Availability of Colorado River water and imported water from the State Water Project;
- The amount of usable water stored in reservoirs and groundwater basins;
- The amount of water used by our customers and others;
- Water quality;
- Legal limitations on production, diversion, storage, conveyance and use; and
- Climate change.

The extended California drought and changes in weather patterns in the West, population growth and changes in customer usage patterns in California have caused increased stress on surface water supplies and groundwater basins. In addition, low or no allocations of water from the State Water Project, low reservoir levels and court-ordered pumping restrictions on water obtained from the Sacramento-San Joaquin Delta decrease or eliminate the amount of water Metropolitan Water District of Southern California, or MWD, and other state water contractors are able to import from northern California. We have implemented tiered rates and other practices in order to encourage water conservation. We are also acting to secure additional supplies from desalination and water transfers. It is unlikely, however, that any of these efforts will enable us to address the near term impacts of the extended drought in California. Moreover, we cannot predict the extent to which these efforts to reduce stress on our water supplies will be successful or sustainable, or the extent to which these efforts will enable us to continue to satisfy all of the water needs of our customers.

Water shortages at GSWC may:

- adversely affect our supply mix, for instance, by causing increased reliance upon more expensive water sources;
- adversely affect our operating costs, for instance, by increasing the cost of producing water from more highly contaminated aquifers or requiring us to transport water over longer distances, truck water to water systems or adopt other emergency measures to enable us to continue to provide water service to our customers;
- result in an increase in our capital expenditures over the long-term, for example by requiring future construction of pipelines to connect to alternative sources of supply, new wells to replace those that are no longer in service or are otherwise inadequate to meet the needs of our customers and reservoirs and other facilities to conserve or reclaim water;
- adversely affect the volume of water sold as a result of such factors as mandatory or voluntary conservation efforts by customers, changes in customer conservation patterns, recycling of water by customers and imposition of new regulations impacting such things as landscaping and irrigation patterns;
- adversely affect aesthetic water quality if we are unable to flush our water systems as frequently due to water shortages or drought restrictions; and
- result in customer dissatisfaction and harm to our reputation if water service is reduced, interrupted or otherwise adversely affected as a result of the California drought, water contamination or other causes.

***Our liquidity may be adversely affected by changes in water supply costs***

We obtain our water supplies for GSWC from a variety of sources. For example, water is pumped from aquifers within our service areas to meet a portion of the demands of our customers. Our source of supply varies among our water systems. Certain systems obtain all of their supply from wells; some systems purchase all of the supply from wholesale suppliers; and other systems obtain the supply from a combination of wells and wholesale suppliers. When water produced from wells is insufficient to meet customer demand or when such production is interrupted, we have purchased water from other suppliers. As a result, our cost of providing, distributing and treating water for our customers' use can vary significantly.

Furthermore, imported water wholesalers, such as MWD may not always have an adequate supply of water to sell to us. Wholesale water suppliers may increase their prices for water delivered to us based on factors that affect their operating costs. Purchased water rate increases are beyond our control.

GSWC has implemented a modified supply cost balancing account ("MCBA") to track and recover costs from supply mix changes and rate changes by wholesale suppliers, as authorized by the CPUC. However, cash flows from operations can be significantly affected as much of the surcharges or surcredits we recognize in the MCBA account are collected from or refunded to customers primarily through surcharges generally over a twelve to eighteen month period.

***Our liquidity and earnings may be adversely affected by maintenance costs***

Some of our infrastructure in California is more than 50 years old. We have experienced leaks and mechanical problems in some of these older systems. In addition, well and pump maintenance expenses are affected by labor and material costs and more stringent water discharge requirements. These costs can increase substantially and unexpectedly.

We include estimated increases in maintenance costs for future years in each general rate case filed by GSWC for possible recovery. We may not recover overages from those estimates in rates.

***Our liquidity and earnings may be adversely affected by our conservation efforts***

Our water utility business is heavily dependent upon revenue generated from rates charged to our residential customers for the volume of water used. The rates we charge for water are regulated by the CPUC and may not be adequately adjusted to reflect changes in demand. Declining usage also negatively impacts our long-term operating revenues if we are unable to secure rate increases or if growth in the residential customer base does not occur to the extent necessary to offset the per customer residential usage decline.

Conservation by all customer classes at GSWC is a top priority. However, customer conservation will result in lower volumes of water sold. We may experience a decline in per residential customer water usage due to factors such as:

- conservation efforts to reduce costs;
- drought conditions resulting in additional water conservation;
- the use of more efficient household fixtures and appliances by residential consumers to save water;
- voluntary or mandatory changes in landscaping and irrigation patterns; and
- recycling of water by our customers.

These types of changes may result in permanent decreases in demand even if our water supplies are sufficient to meet higher levels of demand after the current drought ends. In addition, governmental restrictions on water usage during drought conditions may result in a decreased demand for our water, even if our water reserves are sufficient to serve our customers during these drought conditions.

We implemented a CPUC-approved water revenue adjustment mechanism ("WRAM") at GSWC which has the effect of reducing the adverse impact of our customers' conservation efforts on revenues. However, cash flows from operations can be significantly affected as much of the surcharges or surcredits we recognize in these accounts are collected from or refunded to customers primarily through surcharges generally over a twelve, eighteen or thirty-six month period. Regardless of whether we may surcharge our customers during a conservation period, they may use less water even after a drought has passed because of conservation patterns developed during the drought.

***Our earnings may be affected, to some extent, by weather during different seasons***

The demand for water and electricity varies by season. For instance, there can be a higher level of water consumption during the third quarter of each year when weather in California tends to be hot and dry. During unusually wet weather, our customers generally use less water. The CPUC-approved WRAM helps mitigate fluctuations in revenues due to changes in water consumption by our customers in California.

The demand for electricity in our electric customer service area is greatly affected by winter snows. An increase in winter snows reduces the use of snowmaking machines at ski resorts in the Big Bear area and, as a result, reduces our electric revenues. Likewise, unseasonably warm weather during a skiing season may result in temperatures too high for snowmaking conditions, which also reduces our electric revenues. GSWC has implemented a CPUC-approved base revenue requirement adjustment mechanism for our electric business which helps mitigate fluctuations in the revenues of our electric business due to changes in the amount of electricity used by GSWC's electric customers.

***Our liquidity may be adversely affected by increases in electricity and natural gas prices in California***

We generally purchase most of the electric energy sold to customers in our electric customer service area from others under purchased power contracts. In addition to purchased power contracts, we purchase additional energy from the spot market to meet peak demand and following expiration of power purchase contracts if there are delays in obtaining CPUC authorization of new power purchase contracts. We may sell surplus power to the spot market during times of reduced energy demand. As a result, our cash flow may be affected by the increases in spot market prices of electricity purchased and decreases in spot market prices for electricity sold. However, GSWC has implemented supply cost balancing accounts, as approved by the CPUC, to alleviate any fluctuation to supply costs. We also operate a natural gas-fueled 8.4 megawatt generator in our electric service area.

Unexpected generator downtime or a failure to perform by any of the counterparties to our electric and natural gas purchase contracts could further increase our exposure to fluctuating natural gas and electric prices.

Changes in electricity prices also affect the unrealized gains and losses on our block forward purchased power contracts that qualify as derivative instruments as we adjust the asset or liability on these contracts to reflect the fair market value of the contracts at the end of each month. The CPUC has authorized us to establish a memorandum account to track the changes in the fair market value of our purchased power contracts. As a result, unrealized gains and losses on these types of purchased power contracts do not impact earnings.

***We may not be able to procure sufficient renewable energy resources to comply with CPUC rules***

We are required to procure a portion of our electricity from renewable energy resources to meet the CPUC's renewable procurement requirements. We have an agreement with a third party to purchase renewable energy credits which we believe allows us to meet these requirements through 2023. In the event that the third party fails to perform in accordance with the terms of the agreement, we may not be able to obtain sufficient resources to meet the renewable procurement requirements. We may be subject to fines and penalties by the CPUC if the CPUC determines that we are not in compliance with the renewable resource procurement rules.

***Our assets are subject to condemnation***

Municipalities and other government subdivisions may, in certain circumstances, seek to acquire certain of our assets through eminent domain proceedings. It is generally our practice to contest these proceedings which may be costly and may divert the attention of management from the operation of our business. If a municipality or other government subdivision succeeds in acquiring our assets, there is a risk that we will not receive adequate compensation for the assets acquired or be able to recover all charges associated with the condemnation of these assets. In addition, we would no longer be entitled to any portion of revenue generated from the use of such assets going forward.



### ***Our costs of obtaining and complying with the terms of franchise agreements are increasing***

Cities and counties in which GSWC operates have granted GSWC a franchise to construct, maintain and use pipes and appurtenances in public streets and rights of way. The costs of obtaining, renewing and complying with the terms of these franchise agreements have been increasing as cities and counties attempt to regulate GSWC's operations within the boundaries of the city or unincorporated area of the counties in which GSWC operates. Cities and counties have also been attempting to impose new fees on GSWC's operations, including pipeline abandonment fees and road cut or other types of capital improvement fees. At the same time, there is increasing opposition from consumer groups to rate increases that may be necessary to compensate GSWC for the increased costs of local government regulation. These trends may adversely affect GSWC's ability to recover its costs of providing water service in rates and to efficiently manage capital expenditures and operating and maintenance expenses within CPUC authorized levels.

### **Additional Risks Associated with our Contracted Services**

We derive revenues from contract operations primarily from the operation and maintenance of water and/or wastewater systems at military bases and the construction of water and wastewater infrastructure on these bases (including renewal and replacement of these systems). As a result, these operations are subject to risks that are different than those of our public utility operations.

#### ***Our 50-year contracts for servicing military bases create certain risks that are different from our public utility operations***

We have entered into contracts to provide water and/or wastewater services at military bases pursuant to 50-year contracts, subject to termination, in whole or in part, for the convenience of the U.S. government. In addition, the U.S. government may stop work under the terms of one or more of the contracts, delay performance of our obligations under the contracts or modify the contracts at its convenience.

Our contract pricing was based on a number of assumptions, including assumptions about prices and availability of labor, equipment and materials. We may be unable to recover all costs if any of these assumptions are inaccurate or if all costs incurred in connection with performing the work were not considered. Our contracts are also subject to periodic price adjustments at the time of price redetermination or in connection with requests for equitable adjustment or other changes permitted by the terms of the contracts. The contract price for each of these contracts is subject to redetermination every three years following the initial two years of the contracts. Prices are also subject to equitable adjustment based upon changes in circumstances, laws or regulations and service requirement changes with respect to wages and fringe benefits to the extent provided in each of the contracts.

We are required to record all costs under these types of contracts as they are incurred. As a result, we may record losses associated with unanticipated conditions, higher than anticipated infrastructure levels and emergency work at the time such expenses occur. We recognize additional revenue for such work as, and to the extent that, our price redeterminations and/or requests for equitable adjustments are approved. Delays in obtaining approval of price redeterminations and/or equitable adjustments can negatively impact our results of operations and cash flows.

Certain payments under these contracts are subject to appropriations by Congress. We may experience delays in receiving payment or delays in redetermination of prices or other price adjustments due to canceled or delayed appropriations specific to our projects or reductions in government spending for the military generally or military base operations specifically. Appropriations and the timing of payment may be influenced by, among other things, the state of the economy, competing political priorities, budget constraints, the timing and amount of tax receipts and the overall level of government expenditures for the military generally or military base operations specifically.

Management also reviews goodwill for impairment at least annually. ASUS has \$1.1 million of goodwill which may be at risk for potential impairment if requested price redeterminations and/or equitable adjustments are not granted.

#### ***Risks associated with the collection of wastewater are different, in some respects, from that of our water distribution operations***

The wastewater collection system operations of our subsidiaries providing wastewater services on military bases are subject to substantial regulation and involve significant environmental risks. If collection or sewage systems fail, overflow or do not operate properly, untreated wastewater or other contaminants could spill onto nearby properties or into nearby streams and rivers, causing damage to persons or property, injury to aquatic life and/or economic damages. The cost of addressing such damages may not be recoverable. This risk is most acute during periods of substantial rainfall or flooding, which are common causes of sewer overflows and system failures. Liabilities resulting from such damage could adversely and materially affect our business, results of operations and financial condition. In the event that we are deemed liable for any damage caused by overflows, our losses might not be recoverable under our contracts with the U.S. government, covered by insurance policies or we may find it difficult to secure insurance for this business in the future at acceptable rates.

***Our contracts for the construction of infrastructure improvements on military bases create risks that are different, in some respects, from that of our operations and maintenance activities***

We have entered into contract modifications with the U.S. government and agreements with third parties for the construction of new water and/or wastewater infrastructure at the military bases on which we operate. Most of these contracts are firm fixed-price contracts. Under firm fixed-price contracts, we will benefit from cost savings, but are generally unable (except for changes in scope or circumstances approved by the U.S. government or third party) to recover any cost overruns to the approved contract price. Under most circumstances, the U.S. government or third party has approved increased cost change orders due to changes in scope of work performed.

We generally recognize revenues from these types of contracts using the percentage-of-completion method of accounting. This accounting practice results in our recognizing contract revenues and earnings ratably over the contract term in proportion to contract costs incurred or the physical completion of the construction projects. The earnings or losses recognized on individual contracts are based on periodic estimates of contract revenues, costs and profitability as the construction projects progress.

We establish prices for these types of firm fixed-price contracts and the overall 50-year contracts taken as a whole, based, in part, on cost estimates that are subject to a number of assumptions, including assumptions regarding future economic conditions. If these estimates prove inaccurate or circumstances change, cost overruns could have a material adverse effect on our contracted business operations and results of operations.

***We may be adversely affected by disputes with the U.S. government regarding our performance of contracted services on military bases***

We are routinely audited by the Defense Contract Auditing Agency (“DCAA”) for compliance with federal acquisition regulations, cost accounting standards and other laws regulations and standards that are not applicable to the operations of GSWC. During the course of these audits, the DCAA may question our incurred project costs or the manner in which we have accounted for such costs and recommend to our U.S. government corporate administrative contracting officer that such costs be disallowed.

If there is a dispute with the U.S. government regarding performance under these contracts or the amounts owed to us, the U.S. government may delay, reject or withhold payment, delay price redeterminations or assert its right to offset damages against amounts owed to us. If we are unable to collect amounts owed to us on a timely basis or the U.S. government asserts its offset rights, profits and cash flows could be adversely affected.

If we fail to comply with the terms of one or more of our U.S. government contracts, other agreements with the U.S. government or U.S. government regulations and statutes, we could also be suspended or barred from future U.S. government contracts for a period of time and be subject to possible damages, fines and penalties and damage to our reputation in the water and wastewater industry.

***We depend, to some extent, upon subcontractors to assist us in the performance of contracted services on military bases***

We rely, to some extent, on subcontractors to assist us in the operation and maintenance of the water and wastewater systems at military bases. The failure of any of these subcontractors to perform services for us in accordance with the terms of our contracts with the U.S. government could result in the termination of our contract to provide water and/or wastewater services at the affected base(s), a loss of revenues or increases in costs to correct a subcontractor’s performance failures.

We are also required to make a good faith effort to achieve our small business subcontracting plan goals pursuant to U.S. government regulation. If we fail to use good faith efforts to meet these goals, the U.S. government may assess damages against us either at the end of each price redetermination period or at the end of the contract. The U.S. government has the right to offset claimed damages against any amounts owed to us.

We also rely on third-party manufacturers as well as third-party subcontractors to complete our construction projects. To the extent that we cannot engage subcontractors or acquire equipment or materials, our ability to complete a project in a timely fashion or at a profit may be impaired. If the amount of costs we incur for these projects exceeds the amount we have estimated in our bid, we could experience reduced profits or losses in the performance of these contracts. In addition, if a subcontractor or manufacturer is unable to deliver its services, equipment or materials according to the negotiated terms for any reason, including the deterioration of its financial condition, we may be required to purchase the services, equipment or materials from another source at a higher price. This may reduce the profit to be realized or result in a loss on a project for which the services, equipment or materials were needed.

If these subcontractors fail to perform services to be provided to us or fail to provide us with the proper equipment or materials, we may be penalized for their failure to perform; however, our contracts with these subcontractors include certain

protective provisions, which may include the assessment of liquidated damages. We mitigate these risks by requiring many of our subcontractors to obtain performance bonds and to compensate us for any penalties we may be required to pay as a result of their failure to perform.

***Our earnings may be affected, to some extent, by weather during different seasons***

Seasonal weather conditions, such as hurricanes, heavy rainfall or significant winter storms, occasionally cause temporary office closures and/or result in temporary halts to construction activity at military bases. To the extent that our construction activities are impeded by these events, we will experience a delay in recognizing revenues from these construction projects.

***We continue to incur costs associated with the expansion of our contract activities***

We continue to incur additional costs in connection with the attempted expansion of our contract operations associated with the preparation of bids for new contracts for contract operations on prospective and existing military bases. Our ability to recover these costs and to earn a profit on our contract operations will depend upon the extent to which we are successful in obtaining new contracts and recovering these costs and other costs from new contract revenues.

**Other Risks**

***Our business requires significant capital expenditures***

The utility business is capital intensive. We spend significant sums of money for additions to, or replacement of, our property, plant and equipment at our water and electric utilities. We obtain funds for these capital projects from operations, contributions by developers and others and advances from developers (which are repaid over a period of time at no interest). We also periodically borrow money or issue equity for these purposes. In addition, we have a syndicated bank credit facility that is partially used for these purposes. We cannot provide assurance 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.

Our subsidiaries providing water and wastewater services on military bases also expect to incur significant capital expenditures. To the extent that the U.S. government does not reimburse us for these expenditures as the work is performed or completed, the U.S. government will repay us over time.

***We may be adversely impacted by economic conditions***

Access to external financing on reasonable terms depends, in part, on conditions in the debt and equity markets. When business and market conditions deteriorate, we may no longer have access to the capital markets on reasonable terms. Our ability to obtain funds is dependent upon our ability to access the capital markets by issuing debt or equity to third parties or obtaining funds from our revolving credit facility. In the event of financial turmoil affecting the banking system and financial markets, consolidation of the financial services industry, significant financial service institution failures or our inability to renew or replace our existing revolving credit facility on attractive terms, it may become necessary for us to seek funds from other sources on less attractive terms.

***Market conditions and demographic changes may adversely impact the value of our benefit plan assets and liabilities***

Market factors can affect assumptions we use in determining funding requirements with respect to our pension and postretirement plans. For example, a relatively modest change in our assumptions regarding discount rates can materially affect our calculation of funding requirements. To the extent that market data compels us to reduce the discount rate used in our assumptions, our benefit obligations could materially increase, which could adversely affect our financial position and our cash flow position. Further, changes in demographics, such as increases in life expectancy assumptions may also increase the funding requirements of our obligations related to the pension and other postretirement benefit plans.

Market conditions also affects the values of the assets that are held in trust to satisfy significant future obligations under our pension and postretirement benefit plans. These assets are subject to market fluctuations, which may cause investment returns to fall below our projected rates of return. A decline in the market value of our pension and postretirement benefit plan assets will increase the funding requirements under our pension and postretirement benefit plans if future returns on these assets are insufficient to offset the decline in value. Future increases in pension and other postretirement costs as a result of the reduced value of plan assets may not be fully recoverable in rates, and our results of operations and financial position could be negatively affected. These risks are mitigated to some extent by the two-way pension balancing account authorized by the CPUC which permits us to track differences between forecasted annual expense adopted in rates and actual expenses for future recovery or refund to customers.

***Payment of our debt may be accelerated if we fail to comply with restrictive covenants in our debt agreements***

Our failure to comply with restrictive covenants in our debt agreements could result in an event of default. If the default is not cured or waived, we may be required to repay or refinance this debt before it becomes due. Even if we are able to obtain waivers from our creditors, we may only be able to do so on unfavorable terms.

***The price of our Common Shares may be volatile and may be affected by market conditions beyond our control***

The trading price of our Common Shares may fluctuate in the future because of the volatility of the stock market and a variety of other factors, many of which are beyond our control. Factors that could cause fluctuations in the trading price of our Common Shares include: regulatory developments; general economic conditions and trends; price and volume fluctuations in the overall stock market from time to time; actual or anticipated changes or fluctuations in our results of operations; actual or anticipated changes in the expectations of investors or securities analysts; actual or anticipated developments in other utilities' businesses or the competitive landscape generally; litigation involving us or our industry; and major catastrophic events or sales of large blocks of our stock.

***We (AWR) are a holding company that depends on cash flow from our subsidiaries to meet our financial obligations and to pay dividends on our Common Shares***

As a holding company, our subsidiaries conduct substantially all operations and our only significant assets are investments in our subsidiaries. This means that we are dependent on distributions of funds from our subsidiaries to meet our debt service obligations and to pay dividends on our Common Shares.

Our subsidiaries are separate and distinct legal entities and generally have no obligation to pay any amounts due on our credit facility. Our subsidiaries only pay dividends if and when declared by the subsidiary board. Moreover, GSWC is obligated to give first priority to its own capital requirements and to maintain a capital structure consistent with that determined to be reasonable by the CPUC in its most recent decision on capital structure, in order that customers not be adversely affected by the holding company structure. Furthermore, our right to receive cash or other assets in the unlikely event of liquidation or reorganization of any of our subsidiaries is generally subject to the prior claims of creditors of that subsidiary. If we are unable to obtain funds from a subsidiary in a timely manner, we may be unable to meet our financial obligations, make additional investments or pay dividends.

***Failure to attract, retain, train, motivate, develop and transition key employees could adversely affect our business***

In order to be successful, we must attract, retain, train, motivate, and develop key employees, including those in managerial, operational, financial, business development and IT support positions. Our regulated business and contracted services operations are complex. Attracting and retaining high quality staff allows us to minimize the cost of providing quality service. In order to attract and retain key employees in a competitive marketplace, we must provide a competitive compensation package and be able to effectively recruit qualified candidates. The failure to successfully hire key employees or the loss of a material number of key employees could have a significant impact on the quality of our operations in the short-term. Further, changes in our management team may be disruptive to our business, and any failure to successfully transition key new hires or promoted employees could adversely affect our business and results of operations.

***We must successfully maintain and/or upgrade our information technology systems as we are increasingly dependent on the continuous and reliable operation of these systems***

We rely on various information technology systems to manage our operations. Such systems require periodic modifications, upgrades and or replacement which subject us to inherent costs and risks including potential disruption of our internal control structure, substantial capital expenditures, additional administration and operating expenses, retention of sufficiently skilled personnel to implement and operate the new systems, and other risks and costs of delays or difficulties in transitioning to new systems or of integrating new systems into our current systems. In addition, the difficulties with implementing new technology systems may cause disruptions in our business operations and have an adverse effect on our business and operations, if not anticipated and appropriately mitigated.

We rely on our computer, information and communications technology systems in connection with the operation of our business, especially with respect to customer service and billing, accounting and, in some cases, the monitoring and operation of our treatment, storage and pumping facilities. Our computer and communications systems and operations could be damaged or interrupted by natural disasters, telecommunications, failures or acts of war or terrorism or similar events or disruptions. Any of these or other events could cause system interruption, delays and loss of critical data or delay or prevent operations and adversely affect our financial results.

***System security risks, data protection breaches and cyber-attacks could disrupt our internal operations, and any such disruption could increase our expenses, damage our reputation and adversely affect our stock price.***

There have been an increasing number of cyber-attacks on companies around the world, which have caused operational failures or compromised sensitive corporate or customer data. These attacks have occurred over the internet, through malware, viruses or attachments to e-mails or through persons inside the organization or with access to systems inside the organization. We have implemented security measures and will continue to devote significant resources to address any security vulnerabilities in an effort to prevent cyber-attacks. Despite our efforts, we cannot be assured that a cyber-attack will not cause water, wastewater or electric system problems, disrupt service to our customers, compromise important data or systems or result in unintended release of customer or employee information. Moreover, if a computer security breach affects our systems or results in the unauthorized release of sensitive data, our reputation could be materially damaged. We could also be exposed to a risk of loss or litigation and possible liability.

***Our operations are geographically concentrated in California***

Although we operate water and wastewater facilities in a number of states, our operations are concentrated in California, particularly southern California. As a result, our financial results are largely subject to political, water supply, labor, utility cost and regulatory risks, economic conditions, natural disasters and other risks affecting California.

***We operate in areas subject to natural disasters or that may be the target of terrorist activities***

We operate in areas that are prone to earthquakes, fires, mudslides, hurricanes, tornadoes and other natural disasters. While we maintain insurance policies to help reduce our financial exposure, a significant seismic event in southern California, where GSWC's operations are concentrated, or other natural disasters in any of the areas that we serve could adversely impact our ability to deliver water and electricity or provide wastewater service and adversely affect our costs of operations. With respect to GSWC, the CPUC has historically allowed utilities to establish a catastrophic event memorandum account to potentially recover these costs for our public utility operations.

Terrorists could seek to disrupt service to our customers by targeting our assets. We have invested in additional security for facilities throughout our regulated service areas to mitigate the risks of terrorist activities. We also may be prevented from providing water and/or wastewater services at the military bases we serve in times of military crisis affecting these bases.

**Item 1B — Unresolved Staff Comments**

None.

## **Item 2 - Properties**

### **Water Properties**

As of December 31, 2014, GSWC's physical properties consisted of water transmission and distribution systems which included 2,792 miles of pipeline together with services, meters and fire hydrants and approximately 425 parcels of land, generally less than 1 acre each, on which are located wells, pumping plants, reservoirs and other water utility facilities, including three surface water treatment plants. GSWC also has franchises, easements and other rights of way for the purpose of accessing wells and tanks and constructing and using pipes and appurtenances for transmitting and distributing water. All of GSWC's properties are located in California.

As of December 31, 2014, GSWC owned 239 wells, of which 192 are active operable wells equipped with pumps with an aggregate production capacity of approximately 202.3 million gallons per day. GSWC has 63 connections to the water distribution facilities of the MWD, and other municipal water agencies. GSWC's storage reservoirs and tanks have an aggregate capacity of approximately 112 million gallons. GSWC owns no dams. The following table provides, in greater detail, information regarding the water utility plant of GSWC:

<b>Pumps</b>		<b>Distribution Facilities</b>			<b>Reservoirs</b>	
<b>Well</b>	<b>Booster</b>	<b>Mains*</b>	<b>Services</b>	<b>Hydrants</b>	<b>Tanks</b>	<b>Capacity*</b>
239	381	2,792	258,281	25,332	142	111,816 (1)

\* Reservoir capacity is measured in thousands of gallons. Mains are in miles.

- (1) GSWC has additional capacity in its Bay Point system, through an exclusive capacity right to use 4.4 million gallons from a treatment plant owned by Contra Costa Water District. GSWC also has additional reservoir capacity through an exclusive right to use all of one 8 million gallon reservoir, one-half of another 8 million gallon reservoir, and one-half of a treatment plant's capacity, all owned by Three Valleys Municipal Water District.

### **Electric Properties**

GSWC's electric properties are located in the Big Bear area of San Bernardino County, California. As of December 31, 2014, GSWC owned and operated 29.6 miles of overhead 34.5 kilovolt ("kv") transmission lines, 1.4 miles of underground 34.5 kv transmission lines, 180.0 miles of 4.16 kv or 2.4 kv distribution lines, 54.0 miles of underground cable, 13 sub-stations and a natural gas-fueled 8.4 MW peaking generation facility. GSWC also has franchises, easements and other rights of way for the purpose of constructing and using poles, wires and other appurtenances for transmitting electricity.

### **Adjudicated and Other Water Rights**

GSWC owns groundwater and surface water rights in California. Groundwater rights are further subject to classification as either adjudicated or unadjudicated rights. Adjudicated rights have been subjected to comprehensive litigation in the courts, are typically quantified and are actively managed for optimization and sustainability of the resource. Surface water rights are quantified and managed by the State Water Resources Control Board, unless they originated prior to 1914. As of December 31, 2014, GSWC had adjudicated groundwater water rights and surface water rights of 73,330 and 11,335 acre feet per year, respectively. GSWC also has a number of unadjudicated groundwater rights, which have not been quantified and are not subject to predetermined limitations, but are typically measured by historical usage.

### **Office Buildings**

Registrant's general headquarters is owned and located in San Dimas, California. GSWC also owns and/or leases certain facilities that house regional, district and customer service offices. ASUS leases office facilities in California, Georgia and Virginia. TUS rents a temporary service center facility in Maryland, pending the completion of a facility expected to be constructed at that location. FBWS has a ten-year, renewable, no cost license for use of space in a U.S. government building at Fort Bliss as a service center. PSUS, ODUS and ONUS own service centers in South Carolina, Virginia and North Carolina, respectively. ONUS rents temporary support facilities.

## **Mortgage and Other Liens**

As of December 31, 2014, GSWC had no mortgage debt outstanding or liens securing indebtedness. As of December 31, 2014, neither AWR nor ASUS, or any of its subsidiaries, had any mortgage debt or liens securing indebtedness outstanding.

Under the terms of certain debt of AWR and GSWC, AWR and GSWC are prohibited from issuing any secured debt, without providing equal and ratable security to the holders of this existing debt.

## **Condemnation of Properties**

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 necessary and in the public interest. In addition, these laws provide: (i) that the owner of utility property may contest whether the condemnation is actually necessary and in the public interest, and (ii) that the owner is entitled to receive the fair market value of its property if the property is ultimately taken.

### *Claremont System:*

On November 4, 2014 voters passed a measure authorizing the City to issue up to \$135.0 million in water revenue bonds to finance the acquisition of the Claremont water system. On December 9, 2014, the City filed an eminent domain lawsuit against GSWC. GSWC intends to vigorously contest this action. GSWC serves approximately 11,000 customers in Claremont.

### *Ojai System:*

In March 2013, Casitas Municipal Water District ("CMWD") passed resolutions under the Mello-Roos Communities Facilities District Act of 1982 ("Mello-Roos Act") authorizing the establishment of a Community Facilities District and the issuance of bonds to finance the potential acquisition of GSWC's Ojai system by eminent domain. In August 2013, Ojai residents approved the levying of a special tax to satisfy the planned bond obligations. GSWC filed a petition in the Superior Court, Ventura County, which, among other things, challenged the legality of CMWD's effort to utilize the Mello-Roos Act to acquire property by eminent domain and to fund legal and expert costs of the planned condemnation. Ojai FLOW ("Friends of Locally Owned Water") members filed a motion with the Superior Court asking that all residents of GSWC's Ojai service area be certified as class defendants in GSWC's pending action. They contend that the class would later be entitled to sue GSWC for damages if GSWC's challenge is denied. Without deciding whether such a lawsuit would be permitted, the Court granted the motion for class certification. On March 13, 2014, the Court denied GSWC's petition. On April 9, 2014, GSWC filed a Notice of Appeal. GSWC is unable to predict the outcome of the appeal at this time. GSWC serves approximately 3,000 customers in Ojai.

### *Apple Valley System:*

In recent years, the Town of Apple Valley has considered a potential condemnation of the water systems serving its area, including GSWC's Apple Valley system. In August 2014, Apple Valley's Town Council issued a request for proposal for an updated feasibility study on the potential acquisition of the water systems. The feasibility study has been completed. However, the Town of Apple Valley has not taken any action against GSWC. GSWC serves approximately 2,900 customers in the Town of Apple Valley.

### *Artesia System:*

On October 13, 2014, the City of Artesia's City Council approved the funding of a feasibility study on the potential acquisition of GSWC's water system in Artesia. GSWC serves approximately 3,300 customers in Artesia.

## **Environmental Clean-Up and Remediation of Properties:**

GSWC has been involved in environmental remediation and clean-up at a plant site ("Chadron Plant") that contained an underground storage tank which was used to store gasoline for its vehicles. This tank was removed from the ground in July 1990 along with the dispenser and ancillary piping. Since then, GSWC has been involved in various remediation activities at this site. Recent analysis indicates that offsite monitoring wells may also be necessary to document effectiveness of remediation.

The Company has accrued an estimated liability which includes costs for two years of continued activities of groundwater cleanup and monitoring, future soil treatment and site closure related activities. The ultimate cost may vary as there are many unknowns in remediation of underground gasoline spills and this is an estimate based on currently available information. Management also believes it is probable that the estimated additional costs will be approved in rate base by the CPUC.

**Item 3 - Legal Proceedings**

On December 9, 2014, the City of Claremont filed an eminent domain lawsuit in the County of Los Angeles Superior Court against GSWC (*City of Claremont v. Golden State Water Company*, Case No. BC 566125), to acquire the portion of GSWC's system which serves the City of Claremont. GSWC intends to vigorously contest this action.

Registrant is subject to ordinary routine litigation incidental to its business. Management believes that the opportunity for rate recovery, 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. Management is unable to predict an estimate of the loss, if any, resulting from any pending suits or administrative proceedings.

**Item 4. Mine Safety Disclosure**

Not applicable.



## PART II

### Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

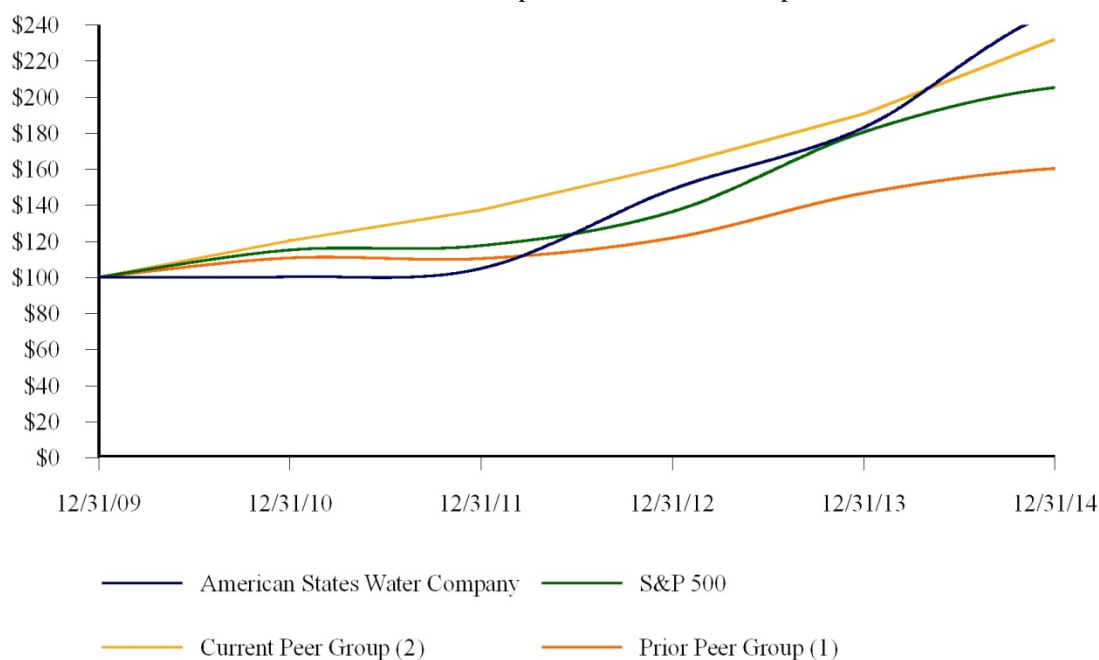
#### Stock Performance Graph

The graph below compares the cumulative 5-year total return provided shareholders on American States Water Company's Common Shares relative to the cumulative total returns of the S&P 500 index and two customized peer groups of five companies and eight companies respectively. The companies in each of the peer groups are listed in footnotes 1 and 2 below. The new peer group includes three additional water companies that were not included in the prior peer group. AWR believes that the expansion of the peer group to include larger water utilities is appropriate in light of AWR's increase in market capitalization in recent years. An investment of \$100 (with reinvestment of all dividends) is assumed to have been made in our Common Shares, and in the common stock in each index and in each of the peer groups on December 31, 2009. Relative performance is tracked through December 31, 2014.

- (1) There are five companies included in the Company's first customized peer group which are: Artesian Resources Corp, California Water Service Group, Connecticut Water Service Inc., Middlesex Water Co and SJW Corp.
- (2) The eight companies included in the Company's second customized peer group include all companies in the prior peer group and American Water Works Company Inc., Aqua America Inc., and York Water Co.

#### **COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN\***

Among American States Water Company, the S&P 500 Index,  
Prior Peer Group and Current Peer Group



\*\$100 invested on 12/31/09 in stock or index, including reinvestment of dividends.  
Fiscal year ending December 31.

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	12/09	12/10	12/11	12/12	12/13	12/14
<b>American States Water Company</b>	\$ 100.00	\$ 100.25	\$ 104.80	\$ 148.66	\$ 182.92	\$ 246.40
<b>S&amp;P 500</b>	\$ 100.00	\$ 115.06	\$ 117.49	\$ 136.30	\$ 180.44	\$ 205.14
<b>Prior Peer Group</b>	\$ 100.00	\$ 110.69	\$ 110.34	\$ 121.73	\$ 146.54	\$ 160.28
<b>Current Group</b>	\$ 100.00	\$ 120.40	\$ 137.37	\$ 161.90	\$ 190.56	\$ 231.98

*The stock price performance included in this graph is not necessarily indicative of future stock price performance.*

## **Market Information Relating to Common Shares**

Common Shares of American States Water Company are traded on the New York Stock Exchange (“NYSE”) under the symbol “AWR”. The intra-day high and low NYSE prices on the Common Shares for each quarter during the past two years, and reflecting the two-for-one stock split effective September 3, 2013, were:

	Stock Prices	
	High	Low
<b><u>2014</u></b>		
First Quarter	\$ 32.97	\$ 27.02
Second Quarter	\$ 33.27	\$ 27.82
Third Quarter	\$ 34.00	\$ 30.11
Fourth Quarter	\$ 38.74	\$ 30.26
<b><u>2013</u></b>		
First Quarter	\$ 28.88	\$ 24.01
Second Quarter	\$ 28.90	\$ 25.65
Third Quarter	\$ 33.09	\$ 25.07
Fourth Quarter	\$ 29.89	\$ 26.45

The closing price of the Common Shares of American States Water Company on the NYSE on February 23, 2015 was \$39.70.

## **Approximate Number of Holders of Common Shares**

As of February 23, 2015, there were 2,475 holders of record of the 38,220,567 outstanding Common Shares of American States Water Company. AWR owns all of the outstanding Common Shares of GSWC and ASUS. ASUS owns all of the outstanding stock of the Military Utility Privatization Subsidiaries.

## **Frequency and Amount of Any Dividends Declared and Dividend Restrictions**

For the last two years, AWR has paid dividends on its Common Shares on or about March 1, June 1, September 1 and December 1. The following table lists the amount of dividends paid on Common Shares of American States Water Company:

	2014	2013
First Quarter	\$ 0.2025	\$ 0.1775
Second Quarter	\$ 0.2025	\$ 0.1775
Third Quarter	\$ 0.2130	\$ 0.2025
Fourth Quarter	\$ 0.2130	\$ 0.2025
Total	\$ 0.8310	\$ 0.7600

AWR’s ability to pay dividends is subject to the requirement in its \$100.0 million revolving credit facility to maintain compliance with all covenants described in footnote (14) to the table in the section entitled “*Contractual Obligations, Commitments and Off Balance Sheet Arrangements*” included in Part II, Item 7 in Management’s Discussion and Analysis of Financial Condition and Results of Operation. GSWC’s maximum ability to pay dividends is restricted by certain Note Agreements to the sum of \$21.0 million plus 100% of consolidated net income from certain dates plus the aggregate net cash proceeds received from capital stock offerings or other instruments convertible into capital stock from various dates. Under the most restrictive of the Note Agreements, \$367.7 million was available from GSWC to pay dividends to AWR as of December 31, 2014. GSWC is also prohibited under the terms of senior notes from paying dividends if, after giving effect to the dividend, its total indebtedness to capitalization ratio (as defined) would be more than 0.6667 to 1. GSWC would have to issue additional debt of \$533.2 million to invoke this covenant as of December 31, 2014.

Under California law, AWR, GSWC and ASUS are each permitted to distribute dividends to its shareholders and repurchase its shares so long as the Board of Directors determines, in good faith, that either: (i) the value of the corporation's assets equals or exceeds the sum of its total liabilities immediately after the dividend, or (ii) its retained earnings equals or exceeds the amount of the distribution. Under the least restrictive of the California tests, approximately \$253.6 million was available to pay dividends to AWR's common shareholders and repurchase shares from AWR's common shareholders at December 31, 2014. Approximately \$199.6 million was available for GSWC to pay dividends to AWR at December 31, 2014. Approximately \$41.3 million was available for ASUS to pay dividends to AWR at December 31, 2014.

AWR paid \$32.1 million in dividends to shareholders for the year ended December 31, 2014, as compared to \$29.4 million for the year ended December 31, 2013. GSWC paid dividends of \$52.0 million and \$29.4 million to AWR in 2014 and 2013, respectively. ASUS did not pay dividends to AWR in 2014 or 2013. AWR paid \$17.2 million to repurchase its Common Shares in 2014.

### **Other Information**

The shareholders of AWR have approved the material features of all equity compensation plans under which AWR directly issues equity securities. AWR did not directly issue any unregistered equity securities during 2014.

The following table provides information about AWR repurchases of its Common Shares during the fourth quarter of 2014:

<b>Period</b>	<b>Total Number of Shares Purchased</b>	<b>Average Price Paid per Share</b>	<b>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</b>	<b>Maximum Number of Shares That May Yet To Be Purchased under the Plans or Programs (2)</b>
October 1 - 31, 2014	185,950	\$ 30.58	184,688	834,014
November 1 - 30, 2014	33,758	\$ 34.84	—	834,014
December 1 - 31, 2014	171,501	\$ 34.19	129,232	704,782
<b>Total</b>	<b>391,209 (1)</b>	<b>\$ 32.53</b>	<b>313,920</b>	

(1) Of this amount, 67,600 Common Shares were acquired on the open market for employees pursuant to our 401(k) Plan and 9,689 of the Common Shares were acquired on the open market for participants in AWR's Common Share Purchase and Dividend Reinvestment Plan. The remainder of the Common Shares were purchased under the stock repurchase program.

(2) On March 27, 2014, AWR's Board of Directors approved a stock repurchase program authorizing AWR to repurchase up to 1.25 million shares of AWR's Common Shares from time to time through June 30, 2016.

**Item 6. Selected Financial Data****AMERICAN STATES WATER COMPANY (AWR):**

(in thousands, except per share amounts)

	2014	2013	2012	2011	2010 (3)
<b>Income Statement Information:</b>					
Total Operating Revenues	\$ 465,791	\$ 472,077	\$ 466,908	\$ 419,913	\$ 399,776
Total Operating Expenses	346,746	353,005	355,814	324,809	325,957
Operating Income	119,045	119,072	111,094	95,104	73,819
Interest Expense	21,617	22,415	22,765	23,681	21,636
Interest Income	927	707	1,333	859	2,406
Income from Continuing Operations	\$ 61,058	\$ 62,686	\$ 54,148	\$ 42,010	\$ 31,091
Income from Discontinued Operations, net of tax (2)	\$ —	\$ —	\$ —	\$ 3,849	\$ 2,106

**Basic Earnings per Common Share (1):**

Income from Continuing Operations	\$ 1.57	\$ 1.61	\$ 1.42	\$ 1.12	\$ 0.84
Income from Discontinued Operations (2)	—	—	—	0.10	0.06
Total	<u>\$ 1.57</u>	<u>\$ 1.61</u>	<u>\$ 1.42</u>	<u>\$ 1.22</u>	<u>\$ 0.90</u>

**Fully Diluted Earnings per Common Share (1):**

Income from Continuing Operations	\$ 1.57	\$ 1.61	\$ 1.41	\$ 1.11	\$ 0.83
Income from Discontinued Operations (2)	—	—	—	0.10	0.06
Total	<u>\$ 1.57</u>	<u>\$ 1.61</u>	<u>\$ 1.41</u>	<u>\$ 1.21</u>	<u>\$ 0.89</u>

Average Shares Outstanding	38,658	38,639	37,998	37,386	37,170
Average number of Diluted Shares Outstanding	38,880	38,869	38,262	37,674	37,472
Dividends Declared per Common Share	\$ 0.831	\$ 0.760	\$ 0.635	\$ 0.550	\$ 0.520

**Balance Sheet Information:**

Total Assets	\$ 1,378,298	\$ 1,310,183	\$ 1,280,943	\$ 1,238,362	\$ 1,192,035
Common Shareholders' Equity	506,801	492,404	454,579	408,666	377,541
Long-Term Debt	325,798	326,079	332,463	340,395	299,839
Total Capitalization	\$ 832,599	\$ 818,483	\$ 787,042	\$ 749,061	\$ 677,380

**GOLDEN STATE WATER COMPANY (GSWC):**

(in thousands)

	2014	2013	2012	2011	2010 (3)
<b>Income Statement Information:</b>					
Total Operating Revenues	\$ 361,059	\$ 358,540	\$ 342,931	\$ 336,725	\$ 327,416
Total Operating Expenses	261,317	256,197	256,326	253,047	263,615
Operating Income	99,742	102,343	86,605	83,678	63,801
Interest Expense	21,524	22,287	22,609	23,292	21,215
Interest Income	894	615	1,293	801	1,914
Net Income	\$ 47,857	\$ 48,642	\$ 39,220	\$ 34,822	\$ 25,110
<b>Balance Sheet Information:</b>					
Total Assets	\$ 1,282,374	\$ 1,233,381	\$ 1,214,052	\$ 1,173,383	\$ 1,078,478
Common Shareholder's Equity	435,190	437,613	416,257	384,806	358,295
Long-Term Debt	325,798	326,079	332,463	340,395	299,839
Total Capitalization	\$ 760,988	\$ 763,692	\$ 748,720	\$ 725,201	\$ 658,134

- (1) On September 3, 2013, a two-for-one stock split became effective. The number of shares outstanding, and basic and diluted earnings per share ("EPS") have been restated for all periods presented above to reflect the stock split.
- (2) In May 2011, AWR completed its sale of Chaparral City Water Company ("CCWC") and recorded a gain on the sale (net of taxes and transaction costs) of approximately \$2.2 million, or \$0.06 per share. The results of CCWC for all periods included have been presented as a discontinued operation.
- (3) In 2010, results include a \$16.6 million charge related to the impairment of assets and loss contingencies in connection with regulatory matters.

## **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation**

The following discussion and analysis provides information on AWR's consolidated operations and assets and where necessary, includes specific references to AWR's individual segments and/or other subsidiaries: GSWC and ASUS and its subsidiaries. Included in the following analysis is a discussion of water and electric gross margins. Water and electric gross margins are computed by taking total revenues, less total supply costs. Registrant uses these gross margins and related percentages as an important measure in evaluating its operating results. Registrant believes this measure is a useful internal benchmark in evaluating the performance of GSWC.

The discussions and tables included in the following analysis also present Registrant's operations in terms of earnings per share by business segment. Registrant believes that the disclosure of earnings per share by business segment provides investors with clarity surrounding the performance of our differing services. Registrant reviews these measurements regularly and compares them to historical periods and to our operating budget. However, these measures, which are not presented in accordance with Generally Accepted Accounting Principles ("GAAP"), may not be comparable to similarly titled measures used by other entities and should not be considered as an alternative to operating income or earnings per share, which are determined in accordance with GAAP. A reconciliation of water and electric gross margins to the most directly comparable GAAP measures are included in the table under the section titled "*Operating Expenses: Supply Costs.*" Reconciliations to AWR's diluted earnings per share are included in the discussions under the sections titled "*Summary Results by Segment.*"

### **Overview**

GSWC's revenues, operating income and cash flows are earned primarily through delivering potable water to homes and businesses in California and the delivery of electricity in the Big Bear area of San Bernardino County, California. Rates charged to GSWC customers are determined by the CPUC. These rates are intended to allow recovery of operating costs and a reasonable rate of return on capital. Factors affecting the financial performance of GSWC are described under Forward-Looking Information and Risk Factors and include: the process and timing of setting rates charged to customers; the ability to recover, and the process for recovering in rates, the costs of distributing water and electricity and overhead costs; pressures on water supply caused by the drought in California, changing weather patterns in the West, population growth, more stringent water quality standards and water supply from a variety of causes; fines, penalties and disallowances by the CPUC arising from failures to comply with regulatory requirements; the impact of increased water quality standards and environmental regulations on the cost of operations and capital expenditures; changes in long-term customer demand due to changes in usage patterns as a result of conservation efforts, mandatory regulatory changes impacting the use of water, such as new landscaping or irrigation requirements, recycling of water by the customer and purchases of recycled water by customers from other third parties; capital expenditures needed to upgrade water systems and increased costs and risks associated with litigation relating to water quality and water supply, including suits initiated by GSWC to protect its water supply and condemnation actions initiated by municipalities. GSWC plans to continue to seek additional rate increases in future years from the CPUC to recover operating and supply costs and receive reasonable returns on invested capital. Capital expenditures in future years at GSWC are expected to remain at much higher levels than depreciation expense. When necessary, GSWC obtains funds from external sources in the capital markets and through bank borrowings.

On June 26, 2014, the CPUC approved a Certificate of Public Convenience and Necessity application granting GSWC the authority to provide water utility services to an area to be developed near Sacramento, in Sutter County, California, called Sutter Pointe. With the CPUC's approval, GSWC will create a water service district to supply the Sutter Pointe development, approximately 17,000 residential customers, with groundwater and surface water from the Sacramento River. The decision also sets a cap on the revenue requirement per Sutter Pointe customer during the first two rate cycles. As part of the agreement, GSWC will also request approval from the CPUC to acquire the water system that currently serves the community of Robbins in Sutter County. In August 2014, the Office of Ratepayer Advocates filed an application for rehearing on the application. At this time, management cannot predict if a rehearing will be granted or the outcome of any rehearing if granted.

In July 2014, GSWC filed a general rate case for all of its water regions and the general office. The application will determine rates for the years 2016, 2017 and 2018. GSWC's requested capital budgets in the application average approximately \$90 million a year for the three year period. The 2016 adopted water gross margin is expected to decrease by approximately \$700,000 as compared to the currently adopted levels due, in part, to a decrease in annual depreciation expense resulting from an updated depreciation study.

In February 2012, BVES filed its general rate case ("GRC") for new rates in years 2013 through 2016. On May 7, 2014, GSWC filed a settlement agreement with the CPUC covering all matters in the case. On November 6, 2014, the CPUC approved the settlement agreement retroactive to January 1, 2013. This decision did not have a significant impact on GSWC's 2014 financial results.

ASUS's revenues, operating income and cash flows are earned by providing water and/or wastewater services, including the operation, maintenance, renewal and replacement of the water and/or wastewater systems, at various military installations pursuant to 50-year firm, fixed-price contracts. The contract price for each of these contracts is subject to prospective price redeterminations. Additional revenues generated by contract operations are primarily dependent on new construction activities under contract modifications with the U.S. government or agreements with other third party prime contractors. As a result, ASUS is subject to risks that are different than those of GSWC. Factors affecting the financial performance of our Military Utility Privatization Subsidiaries are described under Forward-Looking Information and under Risk Factors and include delays in receiving payments from and the redetermination and equitable adjustment of prices under the contracts with the U.S. government; fines, penalties or disallowance of costs by the U.S. government; and termination of contracts and suspension or debarment for a period of time from contracting with the government due to violations of federal law and regulations in connection with military utility privatization activities. Our financial performance is also dependent upon our ability to accurately estimate our costs in bidding on firm fixed-price construction contracts and the costs of seeking new contracts for the operation and maintenance and renewal and replacement of water and/or wastewater services at military bases and for additional construction work at existing bases. ASUS is actively pursuing utility privatization contracts of other military bases to expand the contracted services segment.

In September 2014, ASUS received retroactive contract modifications from the U.S. government for price redeterminations and other matters related to the operations at Fort Bragg, Fort Jackson and Andrews Air Force Base. As a result, included in earnings for the year ended December 31, 2014 was approximately \$1.7 million in retroactive revenues for years prior to 2014, or \$0.03 per share, related to these contract modifications.

### Summary Results by Segment

The table below sets forth diluted earnings per share by business segment for AWR's operations:

	Diluted Earnings per Share			
	Year Ended			
	12/31/2014	12/31/2013	CHANGE	
Water	\$ 1.16	\$ 1.19	\$ (0.03)	
Electric	0.07	0.06	0.01	
Contracted services	0.31	0.30	0.01	
AWR (parent)	0.03	0.06	(0.03)	
Totals from operations, as reported	\$ 1.57	\$ 1.61	\$ (0.04)	

For the year ended December 31, 2014, fully diluted earnings per share for the water segment decreased by \$0.03 per share to \$1.16 per share, as compared to \$1.19 per share for 2013. In May 2013, the CPUC issued a final decision on GSWC's water general rate case which approved, among other things, recovery of \$3.1 million of previously incurred costs. The approval of these items increased earnings for the year ended December 31, 2013 by \$0.05 per share, with no similar increase in 2014. Excluding this \$0.05 per share impact, diluted earnings from the water segment increased by \$0.02 per share for the year ended December 31, 2014 as compared to the same period in 2013. Impacting the comparability of the two periods were the following items:

- An increase in the water gross margin of \$0.05 per share, primarily resulting from second-year rate increases and additional revenues approved by the CPUC for advice letter capital projects. There was also a decrease of approximately \$580,000 in revenues with a corresponding decrease in operating expenses representing lower surcharges billed to customers to recover previously incurred costs. These surcharges had no impact on net earnings.
- Excluding supply costs, the one-time recovery of previously incurred costs and the impact of the surcharges discussed above, there was an increase in operating expenses of approximately \$2.1 million, or \$0.03 per share, due primarily to increases in outside service costs, depreciation expense and property taxes. These increases were partially offset by lower planned maintenance.
- A decrease in interest expense and other non-operating expenses (net of interest income), increasing earnings by \$0.01 per share due primarily to the refinance of certain long-term notes with notes at a lower interest rate as well as other debt maturing during the fourth quarter of 2013 and 2014.
- An increase in the effective income tax rate for the water segment during the year ended December 31, 2014 as compared to 2013, which decreased earnings by approximately \$0.01 per share. The change in the tax rate is primarily due to changes between book and taxable income from items that are treated as flow-through adjustments in accordance with regulatory requirements as well as changes in permanent items.

For the year ended December 31, 2014, diluted earnings from the electric segment increased by \$0.01 per share as compared to 2013 due primarily to an overall decrease in operating expenses and a lower electric effective income tax rate. The decrease in expenses in 2014 was partially offset by the recovery of legal and outside services costs in connection with the CPUC's renewables portfolio standard approved by the CPUC in May 2013. As a result, in the second quarter of 2013, GSWC recorded an \$834,000 reduction in legal and outside services costs, increasing earnings by \$0.01 per share. There was no similar reduction in 2014. The final decision on BVES's general rate case approved by the CPUC in November 2014 did not have a significant impact on BVES's earnings for 2014.

For the year ended December 31, 2014, diluted earnings from contracted services were \$0.31 per share, compared to \$0.30 per share for the same period in 2013. Impacting the comparability of the two periods were the following items:

- An increase in management fees as a result of successful resolutions of various price redeterminations received during the third quarter of 2014, increasing earnings by \$0.05 per share for 2014. Included in this increase were retroactive amounts totaling \$1.7 million, or \$0.03 per share, related to prior years.
- An increase of \$0.02 per share due to the recording of additional revenues during the close-out of a large pipe replacement construction project at Fort Bragg. ONUS began work on this large project in 2010, which was completed and closed-out during the fourth quarter of 2014.
- An overall decrease in construction activity reducing earnings by \$0.03 per share due to significant work on several projects being substantially completed during 2013, with less work performed during 2014.
- A decrease of \$0.03 per share as compared to 2013 as a result of cumulative tax deductions taken in 2013 related to certain construction activities for years 2013 and prior. There was no similar cumulative amount deducted for 2014.

Diluted earnings from AWR (parent) decreased \$0.03 per share as compared to the same period in 2013 due primarily to a cumulative tax benefit recorded during the third quarter of 2013 for deductions related to an employee benefit program, with no similar cumulative benefit recorded in 2014.

The following discussion and analysis for the years ended December 31, 2014, 2013 and 2012 provides information on AWR's consolidated operations and assets and, where necessary, includes specific references to AWR's individual segments and/or other subsidiaries: GSWC and ASUS and its subsidiaries.

**Consolidated Results of Operations — Years Ended December 31, 2014 and 2013 (amounts in thousands, except per share amounts):**

	Year Ended 12/31/2014	Year Ended 12/31/2013	\$ CHANGE	% CHANGE
<b>OPERATING REVENUES</b>				
Water	\$ 326,672	\$ 320,131	\$ 6,541	2.0%
Electric	34,387	38,409	(4,022)	-10.5%
Contracted services	104,732	113,537	(8,805)	-7.8%
Total operating revenues	<u>465,791</u>	<u>472,077</u>	<u>(6,286)</u>	-1.3%
<b>OPERATING EXPENSES</b>				
Water purchased	57,790	58,930	(1,140)	-1.9%
Power purchased for pumping	10,700	9,518	1,182	12.4%
Groundwater production assessment	16,450	15,541	909	5.8%
Power purchased for resale	9,649	13,392	(3,743)	-27.9%
Supply cost balancing accounts	6,346	214	6,132	*
Other operation	28,288	27,767	521	1.9%
Administrative and general	78,323	77,291	1,032	1.3%
Depreciation and amortization	41,073	40,090	983	2.5%
Maintenance	16,092	17,772	(1,680)	-9.5%
Property and other taxes	16,722	15,865	857	5.4%
ASUS construction	65,368	76,627	(11,259)	-14.7%
Net gain on sale of property	(55)	(2)	(53)	*
Total operating expenses	<u>346,746</u>	<u>353,005</u>	<u>(6,259)</u>	-1.8%
<b>OPERATING INCOME</b>	119,045	119,072	(27)	—%
<b>OTHER INCOME AND EXPENSES</b>				
Interest expense	(21,617)	(22,415)	798	-3.6%
Interest income	927	707	220	31.1%
Other, net	751	1,105	(354)	-32.0%
	<u>(19,939)</u>	<u>(20,603)</u>	<u>664</u>	-3.2%
<b>INCOME FROM OPERATIONS BEFORE INCOME TAX EXPENSE</b>	99,106	98,469	637	0.6%
Income tax expense	38,048	35,783	2,265	6.3%
<b>NET INCOME</b>	<u>\$ 61,058</u>	<u>\$ 62,686</u>	<u>\$ (1,628)</u>	-2.6%
Basic earnings per Common Share	\$ 1.57	\$ 1.61	\$ (0.04)	-2.5%
Fully diluted earnings per Common Share	\$ 1.57	\$ 1.61	\$ (0.04)	-2.5%

\* Not meaningful



## ***Operating Revenues***

### **General**

Registrant relies upon rate approvals by the CPUC to recover operating expenses and to provide for a return on invested and borrowed capital used to fund utility plant for GSWC. ASUS files price redeterminations and requests for equitable adjustments with the U.S. government in order to recover operating expenses and provide profit margin for contracted services. If adequate rate relief and price redeterminations and adjustments are not granted in a timely manner, operating revenues and earnings can be negatively impacted. ASUS's earnings have also been positively impacted by additional construction projects at each of the Military Utility Privatization Subsidiaries.

### **Water**

For the year ended December 31, 2014, revenues from water operations increased by \$6.5 million to \$326.7 million, compared to \$320.1 million for the year ended December 31, 2013. During 2014, the CPUC approved an increase in rates to specifically cover increases in supply costs experienced in certain rate-making areas. This \$3.5 million increase in revenues for the year ended December 31, 2014 is offset by a corresponding increase in supply cost, resulting in no impact to the water gross margin. There were also second-year rate increases approved by the CPUC effective January 1, 2014 for certain rate-making areas as well as increases related to advice letter filings. These increases were partially offset by a decrease of approximately \$580,000 in surcharges during the year ended December 31, 2014 to recover previously incurred costs approved by the CPUC. The decrease in revenues from these surcharges is offset by a corresponding decrease in operating expenses (primarily administrative and general) resulting in no impact to pretax operating income.

Billed water consumption for the year ended December 31, 2014 decreased by approximately 2.8% as compared to the same period in 2013. Changes in consumption do not have a significant impact on revenues due to the CPUC-approved Water Revenue Adjustment Mechanism ("WRAM") account in place in all three water regions. GSWC records the difference between what it bills its water customers and that which is authorized by the CPUC in the WRAM accounts as regulatory assets or liabilities.

### **Electric**

For the year ended December 31, 2014, revenues from electric operations were \$34.4 million compared to \$38.4 million for 2013. In November 2014, the CPUC issued a final decision on BVES's general rate case which sets new rates for the years 2013 - 2016. The new rates were retroactive to January 1, 2013. Prior to the decision, electric revenues for 2013 and 2014 were recorded based on 2012 adopted levels. The new adopted revenues for years 2013 through 2016 are lower than revenues in the previous rate cycle resulting from a revised return on equity of 9.95%, as well as lower depreciation and certain other operating expenses. As a result of the decision, a \$2.2 million cumulative reduction in revenues was recorded during the fourth quarter of 2014, along with a cumulative reduction in depreciation expense. The impact of the retroactive effect of the new rates to BVES's 2014 net earnings was not significant. There was also a \$936,000 decrease in surcharges to recover previously incurred costs during 2014 as compared to 2013, with a corresponding \$936,000 decrease in operating expenses resulting in no impact to pretax income. The remaining decrease in electric revenues was primarily due to lower electric usage, resulting in lower revenues and lower electric supply costs.

Billed electric usage for the year ended December 31, 2014 decreased 5.4% as compared to 2013. The winter experienced in the Big Bear area during the first quarter of 2014 was too warm for snowmaking, resulting in less electric usage than in the prior year. Due to the CPUC approved Base Revenue Requirement Adjustment Mechanism, which adjusts certain revenues to adopted levels authorized by the CPUC, this change in usage did not have a significant impact on earnings.

### **Contracted Services**

Revenues from contracted services are composed of construction revenues and management fees for operating and maintaining the water and/or wastewater systems at military bases. For the year ended December 31, 2014, revenues from contracted services decreased to \$104.7 million as compared to \$113.5 million for 2013. The decrease was mainly due to lower construction activity at various military bases, including a reduction in initial capital upgrade work at Fort Bragg and the military bases in Virginia. In addition, ASUS subsidiaries completed or are nearing completion of significant work on major capital projects at Fort Bliss and Fort Bragg, resulting in less revenue during the year ended December 31, 2014 as compared to the same period in 2013. The decrease in construction activity was partially offset by the resolution of price redeterminations at Fort Bragg, Fort Jackson and Andrews Air Force Base resulting in increased management fee revenues during the third quarter of 2014, including retroactive amounts related to prior years totaling \$1.7 million. Additionally, ASUS recorded \$1.6 million of additional revenues during the fourth quarter of 2014 in conjunction with the close-out of a large construction project at Fort Bragg. ONUS began work on this large project in 2010, which was completed and closed-out during the fourth quarter of 2014.

ASUS subsidiaries continue to enter into U.S. government awarded contract modifications and agreements with third-party prime contractors for new construction projects at the Military Utility Privatization Subsidiaries. During the third quarter

of 2014, the U.S. government awarded ASUS \$27.0 million in new construction projects, the majority of which are expected to be completed during the next twelve months. Earnings and cash flows from modifications to the original 50-year contracts with the U.S. government and agreements with third-party prime contractors for additional construction projects may or may not continue in future periods.

**Operating Expenses:**

**Supply Costs**

Supply costs for the water segment consist of purchased water, power purchased for pumping, groundwater production assessments and water supply cost balancing accounts. Supply costs for the electric segment consist of power purchased for resale, the cost of natural gas used by BVES's generating unit, renewable energy credits and the electric supply cost balancing account. Water and electric gross margins are computed by taking total revenues, less total supply costs. Registrant uses these gross margins and related percentages as important measures in evaluating its operating results. Registrant believes these measures are useful internal benchmarks in evaluating the utility business performance within its water and electric segments. Registrant reviews these measurements regularly and compares them to historical periods and to its operating budget. However, these measures, which are not presented in accordance with Generally Accepted Accounting Principles ("GAAP"), may not be comparable to similarly titled measures used by other entities and should not be considered as alternatives to operating income, which is determined in accordance with GAAP.

Total supply costs comprise the largest segment of total operating expenses. Supply costs accounted for 29.1% and 27.6% of total operating expenses for the years ended December 31, 2014 and 2013, respectively.

The table below provides the amount of increases (decreases), percent changes in supply costs, and gross margins during the years ended December 31, 2014 and 2013 (dollar amounts in thousands):

	Year Ended 12/31/2014	Year Ended 12/31/2013	\$ CHANGE	% CHANGE
WATER OPERATING REVENUES (1)	\$ 326,672	\$ 320,131	\$ 6,541	2.0%
WATER SUPPLY COSTS:				
Water purchased (1)	57,790	58,930	(1,140)	-1.9%
Power purchased for pumping (1)	10,700	9,518	1,182	12.4%
Groundwater production assessment (1)	16,450	15,541	909	5.8%
Water supply cost balancing accounts (1)	1,378	(1,958 )	3,336	-170.4%
TOTAL WATER SUPPLY COSTS	\$ 86,318	\$ 82,031	\$ 4,287	5.2%
WATER GROSS MARGIN (2)	\$ 240,354	\$ 238,100	\$ 2,254	0.9%
PERCENT MARGIN - WATER	73.6%	74.4%		
ELECTRIC OPERATING REVENUES (1)	\$ 34,387	\$ 38,409	\$ (4,022)	-10.5%
ELECTRIC SUPPLY COSTS:				
Power purchased for resale (1)	9,649	13,392	(3,743)	-27.9%
Electric supply cost balancing accounts (1)	4,968	2,172	2,796	128.7%
TOTAL ELECTRIC SUPPLY COSTS	\$ 14,617	\$ 15,564	\$ (947)	-6.1%
ELECTRIC GROSS MARGIN (2)	\$ 19,770	\$ 22,845	\$ (3,075)	-13.5%
PERCENT MARGIN - ELECTRIC	57.5%	59.5%		

(1) As reported on AWR's Consolidated Statements of Income, except for supply cost balancing accounts. The sum of water and electric supply cost balancing accounts in the table above is shown on AWR's Consolidated Statements of Income and totaled \$6,346,000 and \$214,000 for the years ended December 31, 2014 and 2013, respectively. Revenues include surcharges, which increase both revenues and operating expenses by corresponding amounts, thus having no net earnings impact.

(2) Water and electric gross margins do not include any depreciation and amortization, maintenance, administrative and general, property or other tax, or other operation expenses.

Two of the principal factors affecting water supply costs are the amount of water produced and the source of the water. Generally, the variable cost of producing water from wells is less than the cost of water purchased from wholesale suppliers. Under the modified cost balancing account (“MCBA”), GSWC tracks adopted and actual expense levels for purchased water, purchased power and pump taxes, as established by the CPUC. GSWC records the variances (which include the effects of changes in both rate and volume) between adopted and actual water purchased, power purchased, and pump tax expenses as regulatory assets or liabilities. GSWC recovers from or refunds to customers the amount of such variances. GSWC tracks these variances individually for each water ratemaking area.

The overall actual percentages for purchased water for the years ended December 31, 2014 and 2013 approximated the adopted overall percentage of 35%. The overall water gross margin percent was 73.6% for the year ended December 31, 2014 as compared to 74.4% in the same period of 2013.

Purchased water costs for the year ended December 31, 2014 decreased by 1.9% to \$57.8 million as compared to \$58.9 million in 2013 primarily due to a decrease in customer usage, partially offset by increases in wholesale water costs.

For the year ended December 31, 2014, the cost of power purchased for pumping increased to \$10.7 million as compared to \$9.5 million for 2013 primarily due to an increase in average electric costs. Groundwater production assessments were \$16.5 million in 2014 as compared to \$15.5 million in 2013 due to an increase in rates levied by government agencies.

The water supply cost balancing account increased \$3.3 million during the year ended December 31, 2014 as compared to the same period in 2013 due to an increase in rates specifically to cover increases in supply costs for certain rate-making areas, as previously discussed. This increase in revenues is offset by a corresponding increase in the water supply cost balancing account, resulting in no impact to the water gross margin.

For the year ended December 31, 2014, the cost of power purchased for resale to customers in GSWC’s BVES division decreased to \$9.6 million, as compared to \$13.4 million for the year ended December 31, 2013, due primarily to a decrease in the average price per MWh during the year ended December 31, 2014. The average price per MWh decreased from \$62.18 per MWh for the year ended December 31, 2013 to \$48.00 per MWh for the same period in 2014. There was also a 5.4% decrease in customer usage as compared to the year ended December 31, 2013. The electric supply cost balancing account included in total supply costs increased by \$2.8 million due to the decrease in the average price per MWh.

### *Other Operation*

The primary components of other operation expenses for GSWC include payroll, materials and supplies, chemicals and water treatment, and outside service costs of operating the regulated water systems, including the costs associated with water transmission and distribution, pumping, water quality, meter reading, billing and operations of district offices. Registrant’s contracted services operations incur many of the same types of costs as well. For the years ended December 31, 2014 and 2013, other operation expenses by segment consisted of the following (dollar amounts in thousands):

	Year Ended 12/31/2014	Year Ended 12/31/2013	\$ CHANGE	% CHANGE
Water Services	\$ 22,871	\$ 22,356	\$ 515	2.3%
Electric Services	2,677	2,754	(77)	-2.8%
Contracted Services	2,740	2,657	83	3.1%
Total other operation expenses	\$ 28,288	\$ 27,767	\$ 521	1.9%

For the year ended December 31, 2014, other operation expense for water services increased by \$515,000 as compared to 2013. As part of the CPUC's final decision on the water rate case approved in May 2013, during the first quarter of 2013 GSWC recorded a \$1.0 million reduction in other operation expense as a result of the CPUC approval for recovery of certain previously expensed costs. There was no similar reduction in 2014. Excluding the impact of this item, other operation expense for water services decreased by approximately \$485,000 due primarily to a decrease in labor resulting from a lower number of employees, and a decrease in conservation and outside service costs. Conservation costs are expected to increase in 2015.

For the year ended December 31, 2014, other operation expenses for electric services decreased by \$77,000 as compared to 2013. Billed surcharges in 2014 for the recovery of certain operation costs previously incurred decreased by \$435,000 as compared to the same period in 2013. As these surcharges are billed each month, a corresponding dollar amount is recorded to other operation expenses, having no impact on pretax operating income. Excluding this decrease, other operation expenses for electric services increased by \$358,000 due to increases in costs of operating BVES's generating unit.

### *Administrative and General*

Administrative and general expenses include payroll related to administrative and general functions, the related employee benefits, insurance expenses, outside legal and consulting fees, regulatory utility commission expenses, expenses associated with being a public company and general corporate expenses charged to expense accounts. For the years ended December 31, 2014 and 2013, administrative and general expenses by segment, including AWR (parent), consisted of the following (dollar amounts in thousands):

	Year Ended 12/31/2014	Year Ended 12/31/2013	\$ CHANGE	% CHANGE
Water Services	\$ 57,729	\$ 55,053	\$ 2,676	4.9%
Electric Services	8,085	9,592	(1,507)	-15.7%
Contracted Services	12,461	12,639	(178)	-1.4%
AWR (parent)	48	7	41	585.7%
Total administrative and general expenses	\$ 78,323	\$ 77,291	\$ 1,032	1.3%

For the year ended December 31, 2014, administrative and general expenses for water services increased by \$2.7 million compared to 2013. During the first quarter of 2013, as part of the CPUC's final decisions on the water rate case, GSWC recorded a \$1.7 million reduction in administrative and general expenses as a result of the CPUC approval of recovery of certain previously expensed costs. There was no similar reduction in 2014. Additionally, during the year ended December 31, 2014, there was a decrease of \$547,000 in surcharges billed for the recovery of various administrative and general costs previously incurred, as compared to the same period in 2013. As these costs are recovered in revenue through surcharges, a corresponding dollar amount is recorded to administrative and general expenses, having no impact on pretax operating income. Excluding the effect of these two items, administrative and general expenses for water services increased by approximately \$1.5 million due primarily to an increase in legal and outside service costs, partially offset by lower general liability and workers' compensation reserves and pension expense. Registrant expects pension expense to increase during 2015 as a result of lower discount rates and new mortality tables. CPUC-approved rate increases effective January 1, 2015 are expected to provide adequate rate recovery for these expected increases. In addition, for the water and electric segments, differences between actual pension expense and forecasted pension expense included in rates are tracked in the two-way pension balancing accounts, resulting in no impact to pretax income.

For the year ended December 31, 2014, administrative and general expenses for electric services decreased by \$1.5 million compared to 2013. Surcharges billed in 2014 for the recovery of various previously incurred administrative and general costs decreased by \$501,000 as compared to the same period in 2013. As discussed previously, as these surcharges are recorded as revenue, a corresponding dollar amount is recorded to administrative and general expenses, having no impact on pretax operating income. In May 2013 the CPUC approved recovery of \$834,000 in legal and outside service costs related to compliance with the CPUC's renewables portfolio standard. There was no similar reduction in 2014. Excluding the impact of these items, administrative and general expenses for electric services decreased by \$1.8 million due primarily to decreases in legal and outside service costs, pension expense and workers' compensation and general liability reserves.

For the year ended December 31, 2014, administrative and general expenses for contracted services decreased by \$178,000 primarily due to a decrease in legal and outside service costs and pension expense, partially offset by an increase in labor costs.

### ***Depreciation and Amortization***

For the years ended December 31, 2014 and 2013, depreciation and amortization expense by segment consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2014</b>	<b>Year Ended 12/31/2013</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 38,388	\$ 36,636	\$ 1,752	4.8%
Electric Services	1,466	2,316	(850)	-36.7%
Contracted Services	1,219	1,138	81	7.1%
Total depreciation and amortization	<u>\$ 41,073</u>	<u>\$ 40,090</u>	<u>\$ 983</u>	<u>2.5%</u>

For the year ended December 31, 2014, depreciation and amortization expense for water services increased by \$1.8 million due primarily to approximately \$91 million of additions to utility plant during 2013, partially offset by approximately \$11 million of asset retirements.

For the year ended December 31, 2014, depreciation and amortization expense for electric services decreased by \$850,000 primarily due to lower depreciation composite rates approved by the CPUC in the electric general rate case in November 2014.

### ***Maintenance***

For the years ended December 31, 2014 and 2013, maintenance expense by segment consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2014</b>	<b>Year Ended 12/31/2013</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 13,067	\$ 14,994	\$ (1,927)	-12.9%
Electric Services	878	829	49	5.9%
Contracted Services	2,147	1,949	198	10.2%
Total maintenance	<u>\$ 16,092</u>	<u>\$ 17,772</u>	<u>\$ (1,680)</u>	<u>-9.5%</u>

For the year ended December 31, 2014, maintenance expense for water services decreased by \$1.9 million compared to the year ended December 31, 2013 due to a higher level of planned maintenance performed in 2013. Planned maintenance expense for water services is expected to increase in 2015 as compared to 2014.

For the year ended December 31, 2014, maintenance expense for contracted services increased by \$198,000 due to increased maintenance activities performed at various military bases as compared to the same period in 2013.

### ***Property and Other Taxes***

For the years ended December 31, 2014 and 2013, property and other taxes by segment, consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2014</b>	<b>Year Ended 12/31/2013</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 14,285	\$ 13,130	\$ 1,155	8.8%
Electric Services	936	942	(6)	-0.6%
Contracted Services	1,501	1,793	(292)	-16.3%
Total property and other taxes	<u>\$ 16,722</u>	<u>\$ 15,865</u>	<u>\$ 857</u>	<u>5.4%</u>

For the year ended December 31, 2014, property and other taxes for water and electric services increased by \$1.2 million due primarily to increases in property taxes of approximately \$985,000 resulting from capital additions and associated higher assessed property values. There was also an increase in franchise fees.

For the year ended December 31, 2014, property and other taxes for contracted services decreased by \$292,000 due to lower accrued gross receipt taxes for the military bases in Virginia as a result of lower construction activity, and also at Fort Bragg as a result of the elimination of the gross receipt tax in North Carolina effective July 1, 2014.

### ***ASUS Construction***

For the year ended December 31, 2014, construction expenses for contracted services were \$65.4 million, decreasing by \$11.3 million compared to the same period in 2013 due to lower construction activity, primarily at FBWS and ODUS, partially offset by higher construction activity at TUS. As previously discussed, ASUS subsidiaries completed or are nearing completion of significant work on major capital projects at Fort Bliss and Fort Bragg, resulting in less construction expenses during the year ended December 31, 2014 as compared to the same period in 2013.

### ***Interest Expense***

For the years ended December 31, 2014 and 2013, interest expense by segment, including AWR (parent), consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2014</b>	<b>Year Ended 12/31/2013</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 20,260	\$ 20,849	\$ (589)	-2.8%
Electric Services	1,264	1,438	(174)	-12.1%
Contracted Services	151	286	(135)	-47.2%
AWR (parent)	(58)	(158)	100	-63.3%
Total interest expense	\$ 21,617	\$ 22,415	\$ (798)	-3.6%

Overall, interest expense for the year ended December 31, 2014 decreased by \$798,000 as compared to 2013 due primarily to the redemption of \$15.0 million of certain long-term notes in July 2014, as well as other debt maturing during the fourth quarter of 2013 totaling \$3.1 million. This was partially offset by an increase in short-term borrowings under the credit facility. The average bank balances under Registrant's revolving credit facility was \$6.2 million during 2014. There were no borrowings under the credit facility during 2013. The average interest rate on short term borrowings was 0.81% during 2014.

### ***Interest Income***

For the years ended December 31, 2014 and 2013, interest income by business segment, including AWR (parent), consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2014</b>	<b>Year Ended 12/31/2013</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 890	\$ 613	\$ 277	45.2%
Electric Services	4	2	2	100.0%
Contracted Services	9	22	(13)	-59.1%
AWR (parent)	24	70	(46)	-65.7%
Total interest income	\$ 927	\$ 707	\$ 220	31.1%

Interest income increased by \$220,000 for the year ended December 31, 2014 as compared to 2013 due primarily to interest collected on certain outstanding balances owed to GSWC. There was no similar item in 2013.

### ***Other, net***

For the year ended December 31, 2014, other income decreased by \$354,000 primarily due to lower accrued interest related to GSWC's allowance for funds used during construction and lower gains on investments held in a Rabbi Trust for the Supplemental Executive Retirement Plan as compared to the same period in 2013.

### *Income Tax Expense*

For the years ended December 31, 2014 and 2013, income tax expense by segment, including AWR (parent), consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2014</b>	<b>Year Ended 12/31/2013</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 30,410	\$ 30,679	\$ (269)	-0.9%
Electric Services	1,596	2,455	(859)	-35.0%
Contracted Services	7,038	4,911	2,127	43.3%
AWR (parent)	(996)	(2,262)	1,266	-56.0%
Total income tax expense	<u>\$ 38,048</u>	<u>\$ 35,783</u>	<u>\$ 2,265</u>	<u>6.3%</u>

For the year ended December 31, 2014, income tax expense for water and electric services decreased to \$32.0 million compared to \$33.1 million for the same period in 2013 due primarily to a decrease in pretax income. The effective tax rate (“ETR”) for GSWC for the year ended December 31, 2014 decreased slightly to 40.1% as compared to 40.5% in 2013. The ETR deviates from the federal statutory rate primarily due to state taxes and changes between book and taxable income that are treated as flow-through adjustments in accordance with regulatory requirements (principally plant-, rate-case- and compensation-related items), and changes in permanent items. Flow-through adjustments increase or decrease tax expense in one period, with an offsetting decrease or increase occurring in another period.

Income tax expense for contracted services increased to \$7.0 million compared to \$4.9 million. This was due to an increase in pretax income and a higher ETR than in 2013. The ETR for contracted services was 36.6% for 2014 as compared to 29.8% for 2013. In 2013, cumulative deductions were taken for 2013 and prior years related to certain construction activities.

For the year ended December 31, 2014, income tax benefit at AWR (parent) decreased by \$1.3 million as compared to 2013 due primarily to a cumulative tax benefit recorded in 2013 for deductions taken related to an employee benefit program, with no similar cumulative benefit recorded in 2014.

*Consolidated Results of Operations — Years Ended December 31, 2013 and 2012 (dollar amounts in thousands, except per share amounts):*

	Year Ended 12/31/2013	Year Ended 12/31/2012	\$ CHANGE	% CHANGE
<b>OPERATING REVENUES</b>				
Water	\$ 320,131	\$ 305,898	\$ 14,233	4.7%
Electric	38,409	37,033	1,376	3.7%
Contracted services	113,537	123,977	(10,440)	-8.4%
Total operating revenues	472,077	466,908	5,169	1.1%
<b>OPERATING EXPENSES</b>				
Water purchased	58,930	54,010	4,920	9.1%
Power purchased for pumping	9,518	8,355	1,163	13.9%
Groundwater production assessment	15,541	14,732	809	5.5%
Power purchased for resale	13,392	12,120	1,272	10.5%
Supply cost balancing accounts	214	11,709	(11,495)	-98.2%
Other operation	27,767	29,790	(2,023)	-6.8%
Administrative and general	77,291	70,556	6,735	9.5%
Depreciation and amortization	40,090	41,385	(1,295)	-3.1%
Maintenance	17,772	15,887	1,885	11.9%
Property and other taxes	15,865	15,381	484	3.1%
ASUS construction	76,627	81,957	(5,330)	-6.5%
Net gain on sale of property	(2)	(68)	66	-97.1%
Total operating expenses	353,005	355,814	(2,809)	-0.8%
OPERATING INCOME	119,072	111,094	7,978	7.2%
<b>OTHER INCOME AND EXPENSES</b>				
Interest expense	(22,415)	(22,765)	350	-1.5%
Interest income	707	1,333	(626)	-47.0%
Other, net	1,105	431	674	156.4%
	(20,603)	(21,001)	398	-1.9%
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAX EXPENSE	98,469	90,093	8,376	9.3%
Income tax expense	35,783	35,945	(162)	-0.5%
INCOME FROM CONTINUING OPERATIONS	62,686	54,148	8,538	15.8%
Basic earnings from continuing operations	\$ 1.61	\$ 1.42	\$ 0.19	13.4%
Diluted earnings from continuing operations	\$ 1.61	\$ 1.41	\$ 0.20	14.2%



The table below sets forth diluted earnings per share by business segment for AWR's operations:

	Diluted Earnings per Share			
	Year Ended		CHANGE	
	12/31/2013	12/31/2012		
Water	\$ 1.19	\$ 0.90	\$	0.29
Electric	0.06	0.12		(0.06)
Contracted services	0.30	0.39		(0.09)
AWR (parent)	0.06	—		0.06
Totals from operations, as reported	\$ 1.61	\$ 1.41	\$	0.20

For the year ended December 31, 2013, fully diluted earnings per share contributed by the water segment increased by \$0.29 per share to \$1.19 per share, as compared to \$0.90 per share for 2012. Items impacting the comparability of the two periods were:

- An increase in the water gross margin of approximately \$13.4 million, or \$0.20 per share, due primarily to rate increases and a higher adopted water gross margin effective January 1, 2013 approved by the CPUC on May 9, 2013 in connection with the water general rate case. In addition, there was an increase of \$4.6 million in revenues with a corresponding increase in operating expenses, representing new surcharges billed to customers during 2013 to recover previously incurred costs. These surcharges had no impact to net earnings.
- GSWC recorded a \$2.7 million, or \$0.04 per share, decrease in operating expenses as a result of the CPUC's approval for recovery of previously incurred operating expenses in connection with the water general rate case final decision issued in May 2013. Among other things, the final decision approved the one-time recovery of various memorandum accounts, which tracked certain costs that were previously expensed as incurred. As a result, GSWC recorded regulatory assets for these memorandum accounts with a corresponding reduction in operating expenses during the first quarter of 2013.
- Excluding supply costs, the \$4.6 million of surcharges and the impact of the memorandum accounts discussed above, operating expenses decreased by approximately \$1.7 million, or \$0.03 per share, due primarily to decreases in: (i) depreciation expense as a result of lower composite depreciation rates approved in the water rate case, and (ii) operation-related expenses resulting from lower bad debt expense, labor and other employee-related expenses. These decreases were partially offset by increases in: (i) administrative and general expenses resulting from higher legal and other outside services cost and workers compensation costs, and (ii) maintenance expense for planned maintenance work.
- A decrease in the water effective income tax rate for the water segment during the year ended December 31, 2013 as compared to 2012, which increased earnings by approximately \$0.02 per share primarily resulting from changes between book and taxable income that are treated as flow-through adjustments in accordance with regulatory requirements. Flow-through tax adjustments increase or decrease tax expense in one period, with an offsetting decrease or increase occurring in another period.

Diluted earnings from electric operations decreased by \$0.06 per share as compared to 2012. In May 2013, the CPUC approved recovery of legal and outside services costs previously expensed in connection with GSWC's effort to procure renewable resources under the CPUC's renewables portfolio standard ("RPS"). As a result, GSWC recorded an \$834,000 reduction in other operating expenses during 2013 as compared to the RPS recovery approved during 2012 of \$1.2 million. The difference resulted in a decrease of \$416,000 in pretax income, or \$0.01 per share for 2013. In addition to the impact of this RPS recovery, there was an increase of \$1.2 million, or \$0.03 per share, in other operating expenses, excluding supply costs and surcharges billed to customers during 2013 to recover previously incurred costs. These surcharges had no impact to net earnings. Finally, there was a higher electric effective income tax rate during 2013, negatively impacting earnings by \$0.02 per share.

Diluted earnings from contracted services decreased by \$0.09 per share during the year ended December 31, 2013 due primarily to: (i) an overall decrease in construction activities on major construction projects as compared to 2012; (ii) an increase in administrative expenses related to employee related costs and consulting and other outside services costs, incurred in part, to pursue new military base utility privatization opportunities, and (iii) a contract modification received in April 2012 for a major water and wastewater pipeline replacement project at Fort Bragg resulting in additional pretax operating income of \$820,000, or approximately \$0.01 per share with no similar contract modification received during 2013. The decrease in construction activities was due, in part, to delays in construction caused by unfavorable weather conditions and permitting delays outside the Company's control, which have now been resolved. These decreases were partially offset by a lower

effective tax rate as the result of a cumulative tax deduction for certain construction activities taken on a recently filed tax return and expected to be taken on amended tax returns. As a result, the lower effective income tax rate for contracted services increased earnings by \$0.04 per share as compared to 2012.

Diluted earnings from AWR (parent) increased by \$0.06 per share as compared to 2012 resulting primarily from a cumulative tax benefit related to an employee benefit program of approximately \$1.5 million recorded during the third quarter of 2013 for deductions taken on recently filed tax returns and amounts expected to be taken on amended income tax returns. Approximately \$1.3 million of this tax benefit related to periods prior to 2013. It is management's intention to amend tax returns for open years to reflect these deductions.

The following discussion and analysis for the years ended December 31, 2013 and 2012 provide information on AWR's consolidated operations and assets and where necessary, includes specific references to AWR's individual segments and/or subsidiaries, GSWC and ASUS and its subsidiaries.

### ***Operating Revenues***

#### ***Water***

For the year ended December 31, 2013, revenues from water operations increased by \$14.2 million to \$320.1 million, compared to \$305.9 million for the year ended December 31, 2012. The increase in water revenues is primarily due to higher water rates approved by the CPUC effective January 1, 2013 in connection with the general rate case for all three water regions and the general office, as previously discussed. The revenue increase adopted by the CPUC for 2013 was approximately \$10 million over 2012 adopted levels. In addition, there was also a \$4.6 million increase in surcharges during the year ended December 31, 2013 to recover previously incurred costs approved by the CPUC. The increase in revenues from these surcharges is offset by a corresponding increase in operating expenses (primarily administrative and general) resulting in no impact to pretax operating income.

GSWC's revenue requirement and volumetric revenues are adopted as part of a general rate case ("GRC") every three years. GSWC filed a GRC for all three water regions in July of 2014 with rates expected to be effective January 1, 2016. For the year ended December 31, 2013, GSWC's billed customer water usage increased by approximately 3.0% as compared to 2012, but was lower than adopted consumption. Changes in consumption do not have a significant impact on revenues due to the CPUC-approved Water Revenue Adjustment Mechanism ("WRAM") account in place in all three water regions. GSWC records the difference between what it bills its water customers and that which is authorized by the CPUC in the WRAM accounts as regulatory assets or liabilities.

#### ***Electric***

For the year ended December 31, 2013, revenues from electric operations were \$38.4 million compared to \$37.0 million for 2012. There was a \$1.4 million increase in surcharges during 2013 to recover previously incurred costs approved by the CPUC. As previously discussed, increases in revenues from these surcharges is offset by a corresponding increase in operating expenses (primarily administrative and general) resulting in no impact to pretax operating income. Excluding the impact of these surcharges, electric revenues remained unchanged compared to 2013 as a result of the delay in the rate case. In February 2012, GSWC filed its BVES rate case for rates in years 2013 through 2016. A final decision from the CPUC was received in November 2014. Due to the delay in receiving a final decision on the BVES rate case, 2013 electric revenues were recorded using 2012 adopted levels authorized by the CPUC.

Billed electric usage for the year ended December 31, 2013 increased 2.6% as compared to 2012. Due to the CPUC approved Base Revenue Requirement Adjustment Mechanism, which adjusts certain revenues to adopted levels authorized by the CPUC, this change in usage did not have a significant impact on revenues.

#### ***Contracted Services***

For the year ended December 31, 2013, revenues from contracted services decreased to \$113.5 million as compared to \$124.0 million for the year ended December 31, 2012. The decrease was mainly due to lower construction activity at various military bases, particularly at Fort Bliss in Texas and Fort Bragg in North Carolina. This decrease in construction activities was due, in part, to construction delays caused by unfavorable weather conditions and permitting delays outside the applicable Military Utility Privatization Subsidiary's control, which were resolved. This was partially offset by an increase in construction revenues at the military bases in Virginia as compared to 2012.

### ***Operating Expenses:***

#### ***Supply Costs***

Supply costs accounted for 27.6% and 28.4% of total operating expenses for the years ended December 31, 2013 and 2012, respectively.

The table below provides the amount of increases (decreases), percent changes in supply costs, and gross margins during the years ended December 31, 2013 and 2012 (dollar amounts in thousands):

	Year Ended 12/31/2013	Year Ended 12/31/2012	\$ CHANGE	% CHANGE
WATER OPERATING REVENUES (1)	\$ 320,131	\$ 305,898	\$ 14,233	4.7%
WATER SUPPLY COSTS:				
Water purchased (1)	58,930	54,010	4,920	9.1%
Power purchased for pumping (1)	9,518	8,355	1,163	13.9%
Groundwater production assessment (1)	15,541	14,732	809	5.5%
Water supply cost balancing accounts (1)	(1,958)	8,676	(10,634)	-122.6%
TOTAL WATER SUPPLY COSTS	\$ 82,031	\$ 85,773	\$ (3,742)	-4.4%
WATER GROSS MARGIN (2)	\$ 238,100	\$ 220,125	\$ 17,975	8.2%
PERCENT MARGIN - WATER	74.4%	72.0%		
ELECTRIC OPERATING REVENUES (1)	\$ 38,409	\$ 37,033	\$ 1,376	3.7%
ELECTRIC SUPPLY COSTS:				
Power purchased for resale (1)	13,392	12,120	1,272	10.5%
Electric supply cost balancing accounts (1)	2,172	3,033	(861)	-28.4%
TOTAL ELECTRIC SUPPLY COSTS	\$ 15,564	\$ 15,153	\$ 411	2.7%
ELECTRIC GROSS MARGIN (2)	\$ 22,845	\$ 21,880	\$ 965	4.4%
PERCENT MARGIN - ELECTRIC	59.5%	59.1%		

- (1) As reported on AWR's Consolidated Statements of Income, except for supply cost balancing accounts. The sum of water and electric supply cost balancing accounts in the table above is shown on AWR's Consolidated Statements of Income and totaled \$214,000 and \$11,709,000 for the years ended December 31, 2013 and 2012, respectively. Revenues include surcharges, which increase both revenues and operating expenses by corresponding amounts, thus having no net earnings impact.
- (2) Water and electric gross margins do not include any depreciation and amortization, maintenance, administrative and general, property or other tax, or other operation expenses.

The overall actual percentages for purchased water for the years ended December 31, 2013 and 2012 were approximately 35.2% and 35.3%, respectively, as compared to the adopted percentages of 35.3% and 41.6%, respectively. The overall water gross margin percent was 74.4% for the year ended December 31, 2013 as compared to 72.0% in the same period of 2012.

Purchased water costs for the year ended December 31, 2013 increased by 9.1% to \$58.9 million as compared to \$54.0 million in 2012. This increase was primarily due to higher wholesale water costs as compared to 2012 as well as an increase in customer water usage. The increase in costs resulted in an under-collection in the MCBA account.

For the year ended December 31, 2013, power purchased for pumping increased to \$9.5 million, compared to \$8.4 million for 2012. This was primarily due to an increase in average electric rates and an increase in customer usage.

For the year ended December 31, 2013, groundwater production assessments were \$15.5 million, as compared to \$14.7 million in 2012 due to increased rates levied during 2013.

There was a \$10.6 million decrease in the water supply cost balancing account provision during the year ended December 31, 2013 as compared to 2012 primarily due to an overall lower adopted water supply cost for 2013 and an increase in purchased water as discussed above.

For the year ended December 31, 2013, the cost of power purchased for resale to customers in GSWC's BVES division increased to \$13.4 million as compared to \$12.1 million for 2012 due primarily to an increase in power purchased as the result of an increase in customer usage as compared to 2012. The difference between the price of purchased power and \$77 per megawatt-hour authorized by the CPUC is reflected in the electric supply cost balancing account. Also, during 2013 BVES purchased renewable energy credits to meet the CPUC's renewables portfolio standards, the costs of which are included in the energy supply cost balancing account.

### *Other Operation*

For the years ended December 31, 2013 and 2012, other operation expenses by segment consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2013</b>	<b>Year Ended 12/31/2012</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 22,356	\$ 24,396	\$ (2,040)	-8.4%
Electric Services	2,754	2,542	212	8.3%
Contracted Services	2,657	2,852	(195)	-6.8%
Total other operation expenses	<u>\$ 27,767</u>	<u>\$ 29,790</u>	<u>\$ (2,023)</u>	<u>-6.8%</u>

For the year ended December 31, 2013, other operation expenses for water services decreased by \$2.0 million as compared to 2012. This decrease was partially due to the CPUC's final decision issued in May 2013 on the water rate case, which approved among other things, the recovery of \$1.0 million of certain other operation costs that were being tracked in memorandum accounts and which had previously been expensed as incurred. As a result of the final CPUC decision issued in May 2013, GSWC recorded additional regulatory assets with a corresponding reduction in other operation expenses during 2013. In addition, there were also decreases in: (i) bad debt expense of \$619,000; (ii) labor of \$573,000 due to fewer employees, and (iii) conservation costs of \$412,000. These decreases were partially offset by increased water treatment and other miscellaneous operation expenses, as well as surcharges implemented to recover the memorandum accounts approved by the CPUC, as discussed above. Approximately \$482,000 of surcharges related to the memorandum accounts approved in May 2013 was recorded with a corresponding increase to other operation expenses during 2013. These surcharges and additional other operation expenses have no impact on pretax operating income.

For the year ended December 31, 2013, other operation expenses for electric services increased by \$212,000 primarily due to \$435,000 in billed surcharges approved by the CPUC for recovery of previously incurred costs. These surcharges are recorded with a corresponding increase to other operation expenses and have no impact to pretax operating income. These increases were partially offset by a \$155,000 decrease in labor and other employee related benefits resulting from a decrease in number of employees, and an \$84,000 increase in materials and equipment costs.

For the year ended December 31, 2013, other operation expenses for contracted services decreased by \$195,000 as compared to 2012, due largely to a decrease in labor and related employee expenses charged to operation expenses and a decrease in other miscellaneous operation expenses.

### *Administrative and General*

For the years ended December 31, 2013 and 2012, administrative and general expenses by segment, including AWR (parent), consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2013</b>	<b>Year Ended 12/31/2012</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 55,053	\$ 53,273	\$ 1,780	3.3%
Electric Services	9,592	6,866	2,726	39.7%
Contracted Services	12,639	10,298	2,341	22.7%
AWR (parent)	7	119	(112)	-94.1%
Total administrative and general expenses	<u>\$ 77,291</u>	<u>\$ 70,556</u>	<u>\$ 6,735</u>	<u>9.5%</u>

For the year ended December 31, 2013, administrative and general expenses for water services increased by \$1.8 million compared to 2012. As authorized in the CPUC's final decision issued in May 2013 on the water rate case, during 2013 surcharges were implemented to recover costs tracked in certain memorandum accounts and other costs in balancing accounts such as pension expense. During 2013, approximately \$2.8 million of surcharges related to these memorandum accounts and the pension balancing account were recorded with a corresponding increase to administrative and general expenses. These surcharges and additional administrative and general expenses have no impact on pretax operating income. As part of the CPUC decision issued in May 2013, GSWC also recorded a \$1.7 million reduction in certain administrative and general costs that were being tracked in these memorandum accounts that had previously been expensed as incurred. Finally, the CPUC's final decision also decreased transportation expenses by approximately \$281,000 as a result of a lower composite depreciation rate used for GSWC's vehicles. Depreciation expense on vehicles is included in transportation expenses in accordance with CPUC guidelines.

Excluding the impact from the final decision and surcharges discussed above, administrative and general expenses for water services increased by approximately \$961,000 due primarily to an increase of \$1.5 million in legal and other outside services costs and \$693,000 in workers' compensation and other insurance-related costs. These increases were partially offset by decreases of: (i) of \$701,000 resulting primarily from a lower general office expense allocation percentage to the water segment in accordance with the approved water rate case; (ii) \$288,000 in labor and related benefit costs, and (iii) \$243,000 in other miscellaneous administrative and general expenses.

For the year ended December 31, 2013, administrative and general expenses for electric services increased by \$2.7 million compared to 2012. The increase was due to \$1.0 million in surcharges approved by the CPUC for recovery of previously incurred costs, which had no impact to pretax operating income as there was a corresponding increase in electric revenues, as previously discussed. These surcharges were due, in part, to the CPUC's approval in March 2012 for recovery of \$1.2 million in legal and outside services for costs incurred to procure renewable energy resources, which had previously been expensed as incurred; while in 2013, \$834,000 was filed and approved, a difference of \$416,000. In addition, there were increases of: (i) \$652,000 in additional legal and other outside services incurred primarily for the pending general rate case; (ii) \$466,000 in general office expense due to a higher allocation percentage to the electric segment in accordance with the approved water rate case, and (iii) \$192,000 in other administrative and general expenses.

For the year ended December 31, 2013, administrative and general expenses for contracted services increased by \$2.3 million due primarily to an increase of: (i) approximately \$1.5 million in labor and other employee related benefits resulting mostly from increases in the number of employees and in costs charged to administrative and general activities; (ii) \$700,000 in consulting and other outside services costs, and (iii) \$100,000 increase in other miscellaneous administrative and general expenses. These increases are, in part, due to the pursuit of new military base utility privatization opportunities with the U.S. government. Legal and outside services tend to fluctuate and are expected to continue to fluctuate.

### ***Depreciation and Amortization***

For the years ended December 31, 2013 and 2012, depreciation and amortization by segment consisted of the following (dollar amounts in thousands):

	Year Ended 12/31/2013	Year Ended 12/31/2012	\$ CHANGE	% CHANGE
Water Services	\$ 36,636	\$ 37,905	\$ (1,269)	-3.3%
Electric Services	2,316	2,292	24	1.0%
Contracted Services	1,138	1,188	(50)	-4.2%
Total depreciation and amortization	\$ 40,090	\$ 41,385	\$ (1,295)	-3.1%

For the year ended December 31, 2013, depreciation and amortization expense for water and electric services decreased by \$1.2 million to \$39.0 million compared to \$40.2 million for the year ended December 31, 2012, primarily due to lower depreciation composite rates approved by the CPUC in the water rate case decision in May 2013. The decrease resulting from lower depreciation rates was partially offset by approximately \$61.0 million of additions to utility plant during 2012.

### ***Maintenance***

For the years ended December 31, 2013 and 2012, maintenance expense by segment consisted of the following (dollar amounts in thousands):

	Year Ended 12/31/2013	Year Ended 12/31/2012	\$ CHANGE	% CHANGE
Water Services	\$ 14,994	\$ 13,567	\$ 1,427	10.5%
Electric Services	829	789	40	5.1%
Contracted Services	1,949	1,531	418	27.3%
Total maintenance	\$ 17,772	\$ 15,887	\$ 1,885	11.9%

For the year ended December 31, 2013, maintenance expense for water services increased by \$1.4 million compared to the year ended December 31, 2012 primarily due to planned maintenance work performed. Maintenance costs tend to fluctuate year over year, and are expected to continue to fluctuate.

For the year ended December 31, 2013, maintenance expense for contracted services increased by \$418,000 primarily due to increases in outside services costs, partially offset by a decrease in labor and related employee expenses charged to maintenance expenses.

### ***Property and Other Taxes***

For the years ended December 31, 2013 and 2012, property and other taxes by segment, consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2013</b>	<b>Year Ended 12/31/2012</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 13,130	\$ 12,946	\$ 184	1.4%
Electric Services	942	889	53	6.0%
Contracted Services	1,793	1,546	247	16.0%
Total property and other taxes	<u>\$ 15,865</u>	<u>\$ 15,381</u>	<u>\$ 484</u>	<u>3.1%</u>

For the year ended December 31, 2013, property and other taxes for water and electric services increased by \$237,000 primarily due to increases in payroll and property related taxes.

For the year ended December 31, 2013, property and other taxes were higher for contracted services due to an increase in payroll taxes resulting from an increase in the number of employees and higher gross receipts tax in connection with increased construction activity at the military bases in Virginia as compared to the same period in 2012.

### ***ASUS Construction***

For the year ended December 31, 2013, construction expenses for contracted services were \$76.6 million, decreasing by \$5.3 million compared to the same period in 2012, due primarily to a decrease in construction activity at Fort Bliss and at Fort Bragg. The decrease was due to external factors outside the applicable Military Utility Privatization Subsidiary's control such as unfavorable weather conditions, and permitting delays which were resolved. These decreases were partially offset by an increase in construction activity at the military bases in Virginia.

### ***Interest Expense***

For the years ended December 31, 2013 and 2012, interest expense by segment, including AWR (parent), consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2013</b>	<b>Year Ended 12/31/2012</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 20,849	\$ 21,029	\$ (180)	-0.9%
Electric Services	1,438	1,580	(142)	-9.0%
Contracted Services	286	186	100	53.8%
AWR (parent)	(158)	(30)	(128)	426.7%
Total interest expense	<u>\$ 22,415</u>	<u>\$ 22,765</u>	<u>\$ (350)</u>	<u>-1.5%</u>

Overall, interest expense for the year ended December 31, 2013 decreased by \$350,000 as compared to 2012. This was due primarily to GSWC's redemption of \$8.0 million of its 7.55% notes in October 2012. In addition, there were lower short-term bank loan balances during 2013 as compared to 2012. There were no bank loan balances outstanding under the credit facility during 2013, as compared to an average of \$885,000 during 2012. The average interest rate on short term borrowings was 1.5% for 2012.

### ***Interest Income***

For the years ended December 31, 2013 and 2012, interest income by segment, including AWR (parent) consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2013</b>	<b>Year Ended 12/31/2012</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 613	\$ 1,246	\$ (633)	-50.8%
Electric Services	2	47	(45)	-95.7%
Contracted Services	22	7	15	214.3%
AWR (parent)	70	33	37	112.1%
Total interest income	\$ 707	\$ 1,333	\$ (626)	-47.0%

Interest income decreased by \$626,000 for the year ended December 31, 2013 primarily due to refund claims approved by the Internal Revenue Service and recorded during 2012, with no similar amount recorded in 2013.

### ***Other, net***

For the year ended December 31, 2013, Registrant recorded other income of \$1.1 million primarily related to gains recorded on investments held in a Rabbi Trust for the Supplemental Executive Retirement Plan and accrued interest related to GSWC's allowance for funds used during construction.

### ***Income Tax Expense***

For the years ended December 31, 2013 and 2012, income tax expense by segment, including AWR (parent), consisted of the following (dollar amounts in thousands):

	<b>Year Ended 12/31/2013</b>	<b>Year Ended 12/31/2012</b>	<b>\$ CHANGE</b>	<b>% CHANGE</b>
Water Services	\$ 30,679	\$ 24,231	\$ 6,448	26.6%
Electric Services	2,455	2,269	186	8.2%
Contracted Services	4,911	9,437	(4,526)	-48.0%
AWR (parent)	(2,262)	8	(2,270)	*
Total income tax expense	\$ 35,783	\$ 35,945	\$ (162)	-0.5%

\* Not meaningful

For the year ended December 31, 2013, income tax expense for water and electric services increased to \$33.1 million compared to \$26.5 million for the same period in 2012 due primarily to an increase in pretax income. The effective tax rate ("ETR") for GSWC for the year ended December 31, 2013 increased slightly to 40.5% as compared to a 40.3% in 2012. The ETR deviates from the federal statutory rate primarily due to state taxes and changes between book and taxable income that are treated as flow-through adjustments in accordance with regulatory requirements (principally plant-, rate-case- and compensation-related items), and changes in permanent items. Flow-through adjustments increase or decrease tax expense in one period, with an offsetting decrease or increase occurring in another period.

Income tax expense for contracted services decreased to \$4.9 million compared to \$9.4 million. The ETR for contracted services was 29.8% for 2013 as compared to 38.6% for 2012 as the result of deductions for certain construction activities taken on a recently filed tax return and expected to be taken on amended tax returns.

For the year ended December 31, 2013, income tax expense at AWR (parent) decreased by \$2.3 million as compared to 2012 resulting primarily from a cumulative tax benefit of approximately \$1.5 million recorded during the third quarter of 2013 for deductions taken on recently filed tax returns and amounts expected to be taken on amended income tax returns. Approximately \$1.3 million of this tax benefit related to periods prior to 2013. It is management's intention to amend tax returns for open years to reflect these deductions. As a result of this and the deductions taken by the contracted services segment discussed previously, AWR's consolidated ETR was 36.3% for 2013 as compared to 39.9% for 2012.

## **Critical Accounting Policies and Estimates**

Critical accounting policies and estimates 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 accounting policies that are critical to the financial statements of AWR. For more information regarding the significant accounting policies of Registrant, see Note 1 of "Notes to Financial Statements" included in Part II, Item 8 in Financial Statements and Supplementary Data.

**Accounting for Rate Regulation** — Because the Registrant operates extensively in a regulated business, it is subject to the authoritative guidance for accounting for the effects of certain types of regulation. Application of this guidance requires accounting for certain transactions in accordance with regulations adopted by the regulatory commissions of the states in which operations are conducted. 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 ratemaking 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.

Regulation and the effects of regulatory accounting have the most significant impact on the financial statements. When GSWC files for adjustments to rates, the capital assets, operating costs and other matters are subject to review, and disallowances may occur. In the event that a portion of the Registrant's operations is no longer subject to the accounting guidance for the effects of certain types of regulation, Registrant is required to write-off related regulatory assets that are not specifically recoverable and determine if other assets might be impaired. If the CPUC determines that a portion of the Registrant's assets are not recoverable in customer rates, Registrant is required to determine if it has suffered an asset impairment that would require a write-down in the asset valuation. At December 31, 2014, the consolidated balance sheet included regulatory assets, less regulatory liabilities, of approximately \$125.7 million. Management continually evaluates the anticipated recovery of regulatory assets, liabilities, and revenues subject to refund and will provide for allowances and/or reserves as deemed necessary. In the event that Registrant's assessment as to the probability of the inclusion in the ratemaking process is incorrect, the associated regulatory asset or liability will be adjusted to reflect the change in assessment or the impact of regulatory approval of rates. Reviews by the CPUC may also result in additional regulatory liabilities to refund previously collected revenues to customers if the CPUC disallows costs included in the rate-making process.

Registrant also reviews its utility plant in service for possible impairment in accordance with accounting guidance for regulated entities for abandonments and disallowances of plant costs.

**Revenue Recognition** — GSWC records water and electric utility operating revenues when the service is provided to customers. Operating revenues include unbilled revenues that are earned (service has been provided) but not billed by the end of each accounting period. The unbilled revenues are calculated based on the number of days and total usage from each customer's most recent billing record that was billed prior to the end of the accounting period and is used to estimate unbilled consumption as of the year-end reporting period. Unbilled revenues are recorded for both monthly and bi-monthly customers.

The CPUC granted GSWC the authority to implement revenue decoupling mechanisms through the adoption of the Water Revenue Adjustment Mechanism ("WRAM") and the Base Revenue Requirement Adjustment Mechanism ("BRRAM"). With the adoption of these alternative revenue programs, GSWC adjusts revenues in the WRAM and BRRAM for the difference between what is billed to its regulated customers and that which is authorized by the CPUC.

As required by the accounting guidance for alternative revenue programs, GSWC is required to collect its WRAM, net of its MCBA, within 24 months following the year in which they are recorded. In April 2012, the CPUC set the recovery period for under-collected balances that are up to 15% of adopted annual revenues at 18 months or less. For net WRAM under-collected balances greater than 15%, the recovery period is 19 to 36 months. In addition to adopting an amortization schedule, the CPUC set a cap on total net WRAM/MCBA surcharges in any given calendar year of 10% of the last authorized revenue requirement.

Revenues for operations and maintenance contracts are recognized when services have been rendered to the U.S. government pursuant to 50-year contracts. Revenues from construction contracts are recognized based on either the percentage-of-completion or cost-plus methods of accounting. In accordance with GAAP, revenue recognition under these methods require management to estimate the progress toward completion on a contract in terms of efforts (such as costs incurred) or, in the case of the percentage-of-completion method, in terms of results achieved (such as units constructed). These approaches are used because management considers it to be the best available measure of progress on these contracts. Changes in job performance, job conditions, change orders and estimated profitability, including those arising



from any contract penalty provisions, and final contract settlements may result in revisions to costs and income and are recognized in the period in which the revisions are determined. Unbilled receivables from the U.S. government represent amounts to be billed for construction work completed and/or for services rendered pursuant to the 50-year contracts with the U.S. government, which are not presently billable but which will be billed under the terms of those contracts.

**Income Taxes** — Registrant’s income tax calculations require estimates due principally to the regulated nature of the operations of GSWC, 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 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. Changes in regulatory treatment, or significant changes in tax-related estimates, assumptions or law, could have a material impact on the financial position and results of operations of Registrant.

As a regulated utility, GSWC treats certain temporary differences as flow-through adjustments in computing its income tax expense consistent with the income tax approach approved by the CPUC for ratemaking purposes. Flow-through adjustments increase or decrease tax expense in one period, with an offsetting decrease or increase occurring in another period. Giving effect to these temporary differences as flow-through adjustments typically results in a greater variance between the effective tax rate and the statutory federal income tax rate in any given period than would otherwise exist if GSWC were not required to account for its income taxes as a regulated enterprise. As of December 31, 2014, Registrant’s total amount of unrecognized tax benefits was zero. In addition, effective January 1, 2014, the Company changed its tax method of accounting for certain repairs and maintenance expenditures pursuant to regulations issued by the U.S. Treasury Department in September 2013. The new tax regulations allow the Company to deduct a significant amount of linear asset costs previously capitalized for tax purposes. The Company completed its analysis of this deduction for 2014 and prior years and recorded the cumulative effect in 2014. See Note 10 (Income Taxes) of *Notes to Consolidated Financial Statements*.

**Pension Benefits** — Registrant’s pension benefit obligations and related costs are calculated using actuarial concepts within the framework of accounting guidance for employer’s accounting for pensions and post-retirement benefits other than pensions. Two critical assumptions, the discount rate and the expected return on plan assets, are important elements of expense and/or liability measurement. We evaluate these critical assumptions annually. Other assumptions include employee demographic factors such as retirement patterns, mortality, turnover and rate of compensation increase. The discount rate enables Registrant to state expected future cash payments for benefits as a present value on the measurement date. The guideline for setting this rate is a high-quality, long-term corporate bond rate. Registrant’s discount rates were determined by considering the average of pension yield curves constructed using a large population of high quality corporate bonds. The resulting discount rates reflect the matching of plan liability cash flows to the yield curves. A lower discount rate increases the present value of benefit obligations and increases periodic pension expense. Conversely, a higher discount rate decreases the present value of benefit obligations and decreases periodic pension expense. To determine the expected long-term rate of return on the plan assets, Registrant considers the current and expected asset allocation, as well as historical and expected returns on each plan asset class. A lower expected rate of return on plan assets will increase pension expense. The long-term expected return on plan assets was 7.00% in 2014 and 2013, for the pension plan.

For the pension plan obligation, Registrant decreased the discount rate to 4.25% as of December 31, 2014 from 5.10% as of December 31, 2013 to reflect market interest rate conditions at December 31, 2014. A 25 basis point decrease in the assumed discount rate would have increased total net periodic pension expense for 2014 by approximately \$440,000 or 10.1%, and would have increased the projected benefit obligation (“PBO”) and accumulated benefit obligation (“ABO”) at December 31, 2014 by a total of \$7.5 million, or approximately 4.1%. A 25 basis point decrease in the long-term return on pension plan asset assumption would have increased 2014 pension cost by approximately \$318,000 or 7.3%.

In addition, changes in the fair value of plan assets will impact future pension cost and the Plan’s funded status. Volatile market conditions can affect the value of AWR’s trust established to fund its future long-term pension benefits. Any reductions in the value of plan assets will result in increased future expense, an increase in the underfunded position and increased future contributions.

In May 2013, the CPUC issued a final decision which authorized GSWC to continue the use of a two-way pension balancing account to track the differences between forecasted annual pension expense adopted in water rates and the actual annual water expense recorded by GSWC in accordance with the accounting guidance for pension costs. These differences are recorded as a regulatory asset or liability for any shortfalls or excesses. In November 2014, as part of the BVES general rate case decision, the CPUC also authorized the use of a balancing account for the electric segment. As of December 31, 2014, GSWC has a net \$2.7 million under-collection in the two-way pension balancing accounts, consisting of a \$2.8 million under-collection related to the general office and water regions, and a \$124,000 over-collection related to BVES.

Funding requirements for qualified defined benefit pension plans are determined by government regulations. In establishing the contribution amount, Registrant has considered the potential impact of funding rule changes under the Pension Protection Act of 2006. Registrant contributes the minimum required contribution as determined by government regulations or the forecasted annual pension cost authorized by the CPUC and included in customer rates, whichever is higher. In accordance with this funding policy, for 2015 the pension contribution is expected to be at least \$6.0 million. As previously discussed, any difference between the forecasted annual pension costs in rates and the actual pension costs are included in the two-way pension balancing account.

Additionally, our pension and postretirement benefit plan liabilities are sensitive to changes in interest rates. As interest rates decrease, thereby reducing returns, our liabilities increase, potentially increasing benefit expense and funding requirements. In addition, market factors can affect assumptions we use in determining funding requirements with respect to our pension and postretirement plans. For example, a relatively modest change in our assumptions regarding discount rates can materially affect our calculation of funding requirements. To the extent that market data compels us to reduce the discount rate used in our assumptions, our benefit obligations could be materially increased.

Changes in demographics, including increased numbers of retirees or increases in life expectancy assumptions may also increase the funding requirements of our obligations related to the pension and other postretirement benefit plans. Mortality assumptions are a critical component of benefit obligation amounts and a key factor in determining the expected length of time for annuity payments. In 2014, the Society of Actuaries released new mortality tables for pension plans. Beginning with 2014, the benefit obligation amounts will assume a longer life expectancy of participants as a result of the actuarial update to mortality tables. The change in the mortality tables resulted in an increase in the benefit obligation of approximately \$5.8 million, or 3.3%, as of December 31, 2014. The update to the mortality tables is also expected to result in increases to future annual net periodic costs. Assuming no other changes in actuarial assumptions or plan amendments, the costs over the long-term are expected to decrease due to the closure of Registrant's defined benefit pension plan to new employees as of January 1, 2011. In January 2011, the Board of Directors approved an amendment to the pension plan, closing the plan to employees hired after December 31, 2010. Employees hired or rehired after December 31, 2010 are eligible to participate in a defined contribution plan.

## **Liquidity and Capital Resources**

### **AWR**

Registrant's regulated business is capital intensive and requires considerable capital resources. A portion of these capital resources are provided by internally generated cash flows from operations. AWR anticipates that interest expense will increase in future periods due to the need for additional external capital to fund its construction program, and as market interest rates increase. AWR believes that costs associated with capital used to fund construction at GSWC will continue to be recovered through water and electric rates charged to customers.

AWR funds its operating expenses and pays dividends on its outstanding Common Shares primarily through dividends from GSWC. The ability of GSWC to pay dividends to AWR is restricted by California law. Under these restrictions, approximately \$199.6 million was available on December 31, 2014 to pay dividends to AWR.

When necessary, Registrant obtains funds from external sources in the capital markets and through bank borrowings. Access to external financing on reasonable terms depends on the credit ratings of AWR and GSWC and current business conditions, including that of the water utility industry in general as well as conditions in the debt or equity capital markets. AWR also has access to a \$100.0 million revolving credit facility which expires in May 2018. AWR may elect to increase the aggregate commitment by up to an additional \$50.0 million. AWR borrows under this facility and provides funds to its subsidiaries, including GSWC, in support of their operations. Any amounts owed to AWR for borrowings under this facility are included in inter-company payables on GSWC's balance sheet. The interest rate charged to GSWC and other affiliates is sufficient to cover AWR's interest cost under the credit facility. As of December 31, 2014, there were no outstanding borrowings under this facility and \$11.2 million of letters of credit outstanding. As of December 31, 2014, AWR had \$88.8 million available to borrow under the credit facility.

On July 15, 2014, GSWC redeemed its \$5,000,000, 6.87% Medium-Term Notes Series A due 2023, and \$10,000,000, 7.00% Medium-Term Notes Series A, also due 2023. The notes were redeemed at a price of 100% of the outstanding principal amount of the notes, plus interest. To replace these notes, on December 23, 2014, GSWC issued \$15,000,000 in 3.45% Senior Notes due December 23, 2029.

In July 2014, Standard & Poor's Ratings Services ("S&P") revised its rating outlook on AWR and GSWC from stable to positive. S&P also affirmed the 'A+' corporate credit rating on both AWR and GSWC. S&P debt ratings range from AAA (highest rating possible) to D (obligation is in default). In December 2014, Moody's Investors Service ("Moody's") affirmed its 'A2' rating with a stable outlook for GSWC. 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. Registrant believes that AWR's sound capital structure and "A+ positive" credit rating, combined with its financial discipline, will enable AWR to access the debt and/or equity markets. However, unpredictable financial market conditions in the future may limit its access or impact the timing of when to access the market, in which case, Registrant may choose to temporarily reduce its capital spending. During 2015, GSWC's company-funded capital expenditures are estimated to be approximately \$85 - \$95 million.

AWR filed a Registration Statement in August 2012 with the Securities and Exchange Commission for the sale from time to time of debt and equity securities. As of December 31, 2014, \$100.0 million was available for issuance under this Registration Statement. The Registration Statement expires in August 2015.

AWR's ability to pay cash dividends on its Common Shares outstanding depends primarily upon cash flows from GSWC. AWR intends to continue paying quarterly cash dividends in the future, on or about March 1, June 1, September 1 and December 1, subject to earnings and financial condition, regulatory requirements and such other factors as the Board of Directors may deem relevant. Registrant has paid common dividends for over 75 consecutive years. On January 27, 2015, AWR's Board of Directors approved a first quarter dividend of \$0.213 per share on the AWR Common Shares of the Company. Dividends on the Common Shares will be payable on March 2, 2015 to shareholders of record at the close of business on February 17, 2015.

On March 27, 2014, AWR's Board of Directors approved a stock repurchase program, authorizing AWR to repurchase up to 1.25 million shares of AWR's Common Shares from time to time through June 30, 2016. The repurchase program is intended to enable AWR to achieve a consolidated shareholders' equity ratio as percentage of total capitalization that is more reflective of appropriate equity ratios for GSWC and ASUS. The current ratio of 61% equity and 39% debt as of December 31, 2014 is partly the result of the sale in 2011 of AWR's Arizona subsidiary, Chaparral City Water Company, which generated approximately \$30 million in cash proceeds. Based upon current expectations, including the projected infrastructure needs for GSWC and the expected growth of ASUS, which is currently not capital intensive, management does not anticipate AWR will conduct a secondary offering of its Common Shares in the near term.

### Cash Flows from Operating Activities:

Cash flows from operating activities have generally been sufficient to meet operating requirements and a portion of capital expenditure requirements. Registrant's future cash flows from operating activities will be affected by a number of factors, including utility regulation; infrastructure investment; maintenance expenses; inflation; compliance with environmental, health and safety standards; production costs; customer growth; per customer usage of water and electricity; weather and seasonality; conservation efforts; compliance with local governmental requirements and required cash contributions to pension and post-retirement plans. In addition, future cash flows from contracted services subsidiaries will depend on new business activities, existing operations, the construction of new and/or replacement infrastructure at military bases, timely redetermination and equitable adjustment of prices and timely collection of payments from the U.S. government and other prime contractors operating at the military bases.

Cash flows from operating activities are primarily generated by net income, adjusted for non-cash expenses such as depreciation and amortization, and deferred income taxes. Cash generated by operations varies during the year. Net cash provided by operating activities was \$163.3 million for the year ended December 31, 2014 as compared to \$135.7 million for the year ended December 31, 2013, and \$101.5 million for the year ended December 31, 2012. The increase in operating cash flow during 2014 was primarily due to cash generated by contracted services due to the billing of and cash receipts for construction work at military bases. The increase during 2013 compared to 2012 was primarily due to GSWC's collection of various surcharges implemented during 2013 in connection with the net WRAM under-collection and other previously incurred costs approved for recovery by the CPUC in May 2013 in connection with the water general rate case. This increase in 2013 compared to 2012 was partially offset by a decrease at ASUS due primarily to lower construction activity and the timing of the billing for construction work at the military bases during the year ended December 31, 2013. The billings (and cash receipts) for this construction work generally occur at completion of the work or in accordance with a billing schedule contractually agreed to with the U.S. government and/or other prime contractors. Thus, cash flow from construction-related activities may fluctuate from period to period with such fluctuations representing timing differences of when the work is being performed and when the cash is received for payment of the work. The timing of cash receipts and disbursements related to other working capital items also affected the changes in net cash provided by operating activities.

### Cash Flows from Investing Activities:

Net cash used in investing activities was \$74.1 million for the year ended December 31, 2014 as compared to \$98.8 million and \$68.0 million used for the same periods in 2013 and 2012, respectively. There was a decrease in capital expenditures during 2014 compared to 2013 due to project delays for several projects at GSWC. Project delays in 2014 resulted from new paving moratoriums, additional paving requirements imposed by local cities and a delay in drilling a well because suitable groundwater was not found in the area. The higher capital expenditures in 2013 compared to 2012 were consistent with GSWC's capital investment program in 2013 which was also in-line with the water general rate case approved by the CPUC in May 2013. Registrant expects 2015 company-funded capital expenditures to be between \$85 and \$95 million.

Registrant invests capital to provide essential services to its regulated customer base, while working with its regulators to have the opportunity to earn a fair rate of return on investment. Registrant's infrastructure investment plan consists of both infrastructure renewal programs, where infrastructure is replaced, as needed, and major capital investment projects, where new water treatment and delivery facilities are constructed. GSWC may also be required from time to time to relocate existing infrastructure in order to accommodate local infrastructure improvement projects. Projected capital expenditures and other investments are subject to periodic review and revision.

Cash used for other investments consists primarily of cash invested in the Rabbi Trust for Registrant's supplemental executive retirement plan.

### Cash Flows from Financing Activities:

Registrant's financing activities include primarily: (i) the sale proceeds from, and repurchase of, Common Shares and stock option exercises and short-term and long-term debt; (ii) the repayment of long-term debt and notes payable to banks; and (iii) the payment of dividends on Common Shares. In order to finance new infrastructure, Registrant also receives customer advances (net of refunds) for and contributions in aid of construction. Short-term borrowings are used to fund capital expenditures until long-term financing is arranged.

Net cash used in financing activities was \$51.4 million for the year ended December 31, 2014 as compared to \$22.2 million and \$11.3 million for the same periods in 2013 and 2012, respectively. The increase in cash used during 2014 was primarily due to the repurchase of approximately \$17.2 million in AWR Common Shares as part of the stock repurchase program approved by the Board of Directors during the year ended December 31, 2014. Additionally, GSWC repaid \$21.3 million of long-term debt, including redemption of \$15 million in certain long-term notes, in 2014. There was also a decrease in cash receipts from advances for and contributions in aid of construction. AWR also increased the dividend payment as

compared to the year ended December 31, 2013. These increases in cash used in financing activities were offset by proceeds from the issuance of long-term debt, net of issuance costs, of \$14.8 million in 2014. The increase in net cash used in financing activities during 2013 compared to 2012 was due primarily to a decrease in cash proceeds received from AWR's stock incentive plans as compared to 2012, and an increase in dividends paid during 2013 as compared to the same period in 2012. These decreases were partially offset by an increase in cash receipts from advances for and contributions in aid of construction. The amount of cash receipts from advances for and contributions in aid of construction will fluctuate from period to period depending on the level of activities from developers.

### **GSWC**

GSWC funds the majority of its operating expenses, payments on its debt, and dividends on its outstanding Common Shares and a portion of its construction expenditures 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, conservation efforts, environmental regulation, litigation, changes in supply costs and regulatory decisions affecting GSWC's ability to recover these supply costs, timing of rate relief, increases in maintenance expenses and capital expenditures, surcharges authorized by the CPUC to enable GSWC to recover expenses previously incurred from customers and CPUC requirements to refund amounts previously charged to customers.

GSWC may, at times, utilize external sources, including equity investments and short-term borrowings from AWR, and long-term debt to help fund a portion of its construction expenditures. In addition, GSWC receives advances and contributions from customers, home builders and real estate developers to fund construction necessary to extend service to new areas. Advances for construction are generally refundable at a rate of 2.5% in equal annual installments over 40 years. Amounts which are no longer refundable are reclassified to contributions in aid of construction. Utility plant funded by advances and contributions is excluded from rate base. Generally, GSWC amortizes contributions in aid of construction at the same composite rate of depreciation for the related property.

As is often the case with public utilities, GSWC's current liabilities may at times exceed its current assets. Management believes that internally-generated funds along with the proceeds from the issuance of long-term debt, borrowings from AWR and Common Shares issuances to AWR will be adequate to provide sufficient capital to enable GSWC to maintain normal operations and to meet its capital and financing requirements pending recovery of costs in rates.

#### *Cash Flows from Operating Activities:*

Net cash provided by operating activities was \$132.7 million for the year ended December 31, 2014 as compared to \$138.2 million for the same period in 2013, and \$99.9 million in 2012. The decrease in 2014 compared to 2013 was partly due to the expiration of certain CPUC-approved water surcharges implemented in mid-2013 in connection with the CPUC's May 2013 final decision on the water general rate case. The CPUC approved recovery of previously incurred costs in the general rate case final decision. There was also an increase in pension contributions during 2014 as compared to 2013. These items were partially offset by lower tax payments made during 2014 as a result of a tax method change for repairs and maintenance deductions. The increase during 2013 compared to 2012 was primarily due to GSWC's collection of various surcharges implemented during 2013 in connection with the net WRAM under-collection and other previously incurred costs approved for recovery by the CPUC in May 2013 in connection with the water general rate case. The timing of cash receipts and disbursements related to working capital items affected the changes in net cash provided by operating activities.

#### *Cash Flows from Investing Activities:*

Net cash used in investing activities was \$72.0 million for the year ended December 31, 2014 as compared to \$98.6 million and \$66.8 million for the same periods in 2013 and 2012, respectively. Cash used for capital expenditures for the year ended December 31, 2014 of \$70.9 million decreased as compared to 2013 due to project delays. However, capital expenditures had increased in 2013 compared to 2012 consistent with GSWC's capital investment program in 2013, which was also in-line with the water general rate case approved by the CPUC in May 2013. GSWC expects to increase its company-funded capital expenditures to be between \$85 million and \$95 million during 2015. During the years ended December 31, 2014, 2013 and 2012, GSWC funded \$60.8 million, \$98.9 million and \$63.2 million, respectively, in capital expenditures.

During 2013, GSWC also executed an interest bearing note from AWR which expires in May 2018, whereby AWR may borrow up to \$20.0 million for working capital purposes. During 2013, AWR borrowed \$18.2 million from GSWC, of which \$17.7 million was repaid by AWR during that year. During 2014, AWR borrowed \$8.3 million, but had repaid the entire outstanding balance under the note during 2014. As of December 31, 2014, there were no amounts outstanding under this note.

### Cash Flows from Financing Activities:

Net cash used in financing activities was \$54.6 million for the year ended December 31, 2014 as compared to cash used of \$24.3 million and \$10.6 million for the same periods in 2013 and 2012, respectively. The increase in cash used in financing activities during 2014 was due to an increase in dividends paid by GSWC to AWR and a decrease in cash receipts from advances for and contributions in aid of construction during the year ended December 31, 2014. Additionally, GSWC repaid \$21.3 million of long-term debt, including the redemption of \$15 million of certain long-term notes, in 2014. These increases in cash used in financing activities were offset by proceeds from the issuance of long-term debt, net of issuance costs, of \$14.8 million in 2014. During 2013, the increase in cash used in financing activities compared to 2012 was due to an increase in dividends paid to AWR during 2013. During 2012, AWR had more cash on hand, including a \$6.7 million dividend received from ASUS, to fund dividends to shareholders as compared to 2013.

### **ASUS**

ASUS funds its operating expenses primarily through internal operating sources and investments by or loans from AWR. ASUS, in turn, provides funding to its subsidiaries.

### **Contractual Obligations, Commitments and Off Balance Sheet Arrangements**

Registrant has various contractual obligations which are recorded as liabilities in the consolidated financial statements. Other items, such as certain purchase commitments and operating leases are not recognized as liabilities in the consolidated financial statements, but are required to be disclosed.

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 payments to service debt are generally made from cash flow from operations.

The following table reflects Registrant's contractual obligations and commitments to make future payments pursuant to contracts as of December 31, 2014. All obligations and commitments are obligations and commitments of GSWC 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)	\$ 187,000	\$ —	\$ —	\$ —	\$ 187,000
Private Placement Notes (3)	123,000	—	—	40,000	83,000
Tax-Exempt Obligations (4)	11,807	132	279	284	11,112
Other Debt Instruments (5)	4,283	160	360	357	3,406
Total AWR Long-Term Debt	<u>\$ 326,090</u>	<u>\$ 292</u>	<u>639</u>	<u>\$ 40,641</u>	<u>\$ 284,518</u>
Interest on Long-Term Debt (6)	\$ 338,354	\$ 21,663	\$ 43,263	\$ 40,992	\$ 232,436
Advances for Construction (7)	71,574	3,246	6,493	6,493	55,342
Renewable Energy Credit Agreement (8)	3,774	108	498	845	2,323
Purchased Power Contracts (9)	31,140	6,385	6,694	6,717	11,344
Capital Expenditure Commitments (10)	19,547	19,547	—	—	—
Water Purchase Agreements (11)	5,264	447	638	638	3,541
Operating Leases (12)	11,014	2,345	4,025	2,740	1,904
Employer Contributions (13)	20,915	5,994	10,480	4,441	—
SUB-TOTAL	<u>\$ 501,582</u>	<u>\$ 59,735</u>	<u>\$ 72,091</u>	<u>\$ 62,866</u>	<u>\$ 306,890</u>
Other Commitments (14)	<u>14,459</u>				
TOTAL	<u>\$ 842,131</u>				

(1) Excludes dividends and facility fees.

(2) The notes and debentures have been issued by GSWC under an Indenture dated as of September 1, 1993, as amended in December 2008. The notes and debentures do not contain any financial covenants that Registrant believes to be material or any cross default provisions.

(3) GSWC issued private placement notes in the amount of \$28 million pursuant to the terms of note purchase agreements with substantially similar terms. These agreements contain restrictions on the payment of dividends, minimum interest coverage requirements, a maximum debt to capitalization ratio and a negative pledge. Pursuant to the terms of these agreements, GSWC must maintain a minimum interest coverage ratio of two times interest expense. In addition, two senior notes in the amount of \$40 million each were issued by GSWC in October 2005 and in March 2009 to CoBank, ACB. A senior note in the amount of \$15,000,000 was issued to The Prudential Insurance Company of America in December 2014. Under the terms of these senior notes, GSWC may not incur any additional debt or pay any distributions to its shareholders if, after giving effect thereto, it would have a debt to capitalization ratio in excess of 0.6667 to 1 or a debt to Earnings Before Interest, Taxes, Depreciation and Amortization (“EBITDA”) ratio of more than 8 to 1. GSWC is in compliance with these covenant provisions as of December 31, 2014. GSWC does not currently have any outstanding mortgages or other liens on indebtedness on its properties.

(4) Consists of obligations at GSWC related to: (i) a loan agreement supporting \$7.7 million in outstanding debt issued by the California Pollution Control Financing Authority and (ii) \$4.1 million of obligations with respect to GSWC's 500 acre-foot entitlement to water from the State Water Project (“SWP”). These obligations do not contain any financial covenants believed to be material to Registrant or any cross default provisions. In regards to its SWP entitlement, GSWC has entered into agreements with various developers for a portion of its 500 acre-foot entitlement to water from the SWP.

(5) Consists of (i) \$4.1 million outstanding representing the debt portion of funds received under the American Recovery and Reinvestment Act for reimbursements of capital costs related to the installation of meters for conversion of non-metered service to metered service in GSWC's Arden-Cordova District and (ii) \$125,000 outstanding under a variable rate obligation of GSWC incurred to fund construction of water delivery facilities with the Three Valleys Municipal Water District. These obligations do not contain any financial covenants believed to be material to Registrant or any cross default provisions.

(6) Consists of expected interest expense payments based on the assumption that GSWC's long-term debt remains outstanding until maturity. Current interest rates were used to estimate expected interest expense payments on variable rate long-term debt.

(7) Advances for construction represent annual contract refunds by GSWC to developers for the cost of water systems paid for by the developers. The advances are generally refundable in equal annual installments over 40-year periods.

(8) Consists of an agreement by GSWC to purchase a total of 582,000 renewable energy credits through 2023. These renewable energy credits are used by GSWC's electric division to meet California's renewables portfolio standard.

(9) Consists of purchased power contracts executed in December 2014 with Shell Energy North America (US), L.P. and EDF Trading North America, LLC that will begin providing power to BVES effective January 1, 2015 at a fixed cost.

(10) Consists of noncancelable commitments primarily for capital projects under signed contracts at GSWC.

(11) Water purchase agreements consist of: (i) a remaining amount of \$3.1 million under an agreement expiring in 2028 to lease water rights from a third party, and (ii) an aggregate amount of \$2.2 million of other water purchase commitments with other third parties which expire through 2038.

(12) Reflects future minimum payments under noncancelable operating leases for both GSWC and ASUS.

(13) Consists of expected contributions to Registrant's pension plan for the years 2015 through 2018. Contribution to the pension plan will either be the minimum required contribution under the Employee Retirement Income Security Act (“ERISA”) or the contribution amounts that are recovered in customer rates and approved by the CPUC. These amounts are estimates and are subject to change based on, among other things, the limits established for federal tax deductibility (pension plan) and the significant impact that returns on plan assets and changes in discount rates have on such amounts.

(14) Other commitments consist primarily of: (i) a \$3.2 million asset retirement obligation of GSWC that reflects the retirement of wells by GSWC, which by law need to be properly capped at the time of removal; (ii) an irrevocable letter of credit in the amount of \$340,000 for the deductible in Registrant's business automobile insurance policy; (iii) an irrevocable letter of credit issued on behalf of GSWC in the amount of \$585,000 as security for the purchase of power by GSWC, under an energy scheduling agreement with Automated Power Exchange; (iv) \$6.7 million in letters of credit issued on behalf of GSWC representing a percentage of total American Recovery and Reinvestment Act funds received for reimbursement of capital costs related to the installation of meters for conversion of non-metered service to metered service in GSWC's Arden-Cordova district; (v) a \$15,000 irrevocable letter of credit issued on behalf of GSWC pursuant to a franchise agreement with the City of Rancho Cordova, and (vi) an irrevocable letter of credit in the amount of \$3.6 million pursuant to a settlement

agreement with Southern California Edison Company to cover GSWC's commitment to pay the settlement amount. All of the letters of credit are issued pursuant to the syndicated revolving credit facility. The syndicated revolving credit facility contains restrictions on prepayments, disposition 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 from Moody's or S&P of Baa3 or BBB-, respectively. As of December 31, 2014, AWR was in compliance with these covenants with an interest coverage ratio of 7.52 times interest expense, a debt ratio of 0.40 to 1.00 and debt ratings of A+ and A2.

### **Off-Balance Sheet Arrangements**

As noted above, Registrant has various contractual obligations which are recorded as liabilities in the consolidated financial statements. Other items, such as certain purchase commitments and operating leases are not recognized as liabilities in the consolidated financial statements, but are required to be disclosed. Except for those disclosed above in the table, Registrant does not have any other off-balance sheet arrangements.

### **Effects of Inflation**

The rates of GSWC are established to provide recovery of costs and a fair return on shareholders' investment. Recovery of the effects of inflation through higher water rates is dependent upon receiving adequate and timely rate increases. However, authorized rates charged to customers are usually based on a forecast of expenses and capital costs for GSWC. Rates may lag increases in costs caused by unanticipated inflation. During periods of moderate to low inflation, as has been experienced for the past several years, the effects of inflation on operating results have not been significant. Furthermore, the CPUC approves projections for a future test year in general rate cases which reduces the impact of inflation to the extent that GSWC's inflation forecasts are accurate.

For the Military Utility Privatization Subsidiaries, under the terms of the contracts with the U.S. government, the contract price is subject to price redetermination every three years following the initial two years of the contracts. These price redeterminations include adjustments to reflect changes in operating conditions, as well as inflation in costs. Recovery of the effects of inflation is dependent upon receiving adequate and timely price redeterminations. ASUS has experienced and continues to experience delays in the redetermination of prices at some bases. However, when adjustments are finalized, they are implemented retroactive to the effective date of the price redetermination.

### **Climate Change**

#### **Water:**

Based on historical data for greenhouse gas ("GHG") emissions generated from its water operations, GSWC has developed a baseline carbon footprint. Annually, GSWC compares the GHG emissions generated by its water operations to this baseline as part of monitoring its carbon footprint and making efforts to reduce it.

In addition, as part of the planning process, GSWC intends to continue to assess the possible impact climate change may have on its water supply and operations.

#### **Electric:**

The California Air Resources Board ("CARB") published regulations in December 2011 establishing a California cap-and-trade program under which the first compliance period commenced with the 2013 GHG Emissions Report. While BVES's power plant emissions are below the reporting threshold, as a "Covered Entity" BVES has an obligation to file a report in June of each year under the program.

As further discussed under *Other Regulatory Matters*, the CPUC issued a final decision in December 2011 establishing renewable energy procurement requirement timelines. BVES was authorized to procure renewable energy credits ("RECs") to satisfy these compliance obligations and entered into a ten-year contract for RECs that was approved by the CPUC. As a result of this agreement, BVES believes it will be in compliance with both the CPUC's past renewable energy procurement requirements and future requirements through 2023.

BVES is also required to comply with the CPUC's emission performance standards ("EPS") regarding GHG emissions. Under these standards, BVES must file an annual attestation with the CPUC stating that BVES is in compliance with the EPS. Specifically, BVES must attest to having no new ownership investment in generation facilities or no long-term commitments for generation. In February 2015, BVES filed with the CPUC stating that BVES was in compliance with the EPS for 2014.

At this time, management cannot estimate the impact, if any, that these regulations may have on the cost of BVES' power plant operations or the cost of BVES' purchased power from third party providers.



## **Power Supply Arrangements at GSWC's Bear Valley Electric Service Area**

In December 2014, the CPUC approved an application that allowed GSWC to immediately execute new purchased power contracts with energy providers on December 9, 2014. GSWC began taking power effective January 1, 2015 at a fixed cost over three and five year terms depending on the amount of power and period during which the power is purchased under the contracts. During 2014, GSWC's power purchases were based on month-to-month arrangements, as the previous purchase power contract expired in 2013.

In addition to the purchased power contracts, GSWC buys additional energy to meet peak demand and sells surplus power as needed. The average cost of power purchased, including the transactions in the spot market, was approximately \$48.00 per MWh for the year ended December 31, 2014 as compared to \$62.18 per MWh for the same period of 2013. GSWC's average energy costs are impacted by pricing fluctuations on the spot market. However, GSWC has implemented an electric supply cost balancing account, as approved by the CPUC, to alleviate any impacts to earnings.

## **Construction Program**

Registrant's utility businesses require significant annual capital expenditures. GSWC maintains an ongoing water distribution main replacement program throughout its customer service areas based on the age and type of distribution system materials, priority of leaks detected, remaining productive life of the distribution system and an underlying replacement schedule. In addition, GSWC upgrades its electric and water supply facilities in accordance with industry standards, local requirements and CPUC requirements. As of December 31, 2014, GSWC has unconditional purchase obligations for capital projects of approximately \$19.5 million. During the years ended December 31, 2014, 2013 and 2012, GSWC had capital expenditures of \$70.9 million, \$96.7 million, and \$66.8 million, respectively. A portion of these capital expenditures is funded by developers through advances, which must be repaid, or contributions in aid of construction, which are not required to be repaid. During 2015, GSWC's company-funded capital expenditures are estimated to be approximately \$85 - \$95 million.

## **Contracted Services**

Under the terms of the current utility privatization contracts with the U.S. government, each contract's price is subject to price redetermination every three years after the initial two years of the contract, unless otherwise agreed to by the parties. In the event that ASUS (i) is managing more assets at specific military bases than were included in the U.S. government's request for proposal; (ii) is managing assets that are in substandard condition as compared to what was disclosed in the request for proposal; or (iii) becomes subject to new regulatory requirements such as more stringent water quality standards, ASUS is permitted to file, and has filed, requests for equitable adjustment. The timely filing for and receipt of price redeterminations continues to be critical in order for ASUS to recover increasing costs of operating and maintaining, and renewing and replacing the water and/or wastewater systems at the military bases it serves.

In August 2011, Congress enacted the Budget Control Act (the "Act") which committed the U.S. government to significantly reduce the federal deficit over ten years. The Act called for very substantial automatic spending cuts, known as "sequestration," that have impacted the expected levels of Department of Defense budgeting. ASUS has not seen any earnings impact to its existing operations and maintenance and renewal and replacement services, as utility privatization contracts are an "excepted service" within the Act. While the on-going effects of sequestration have been mitigated through the passage of a fiscal year 2014-15 Department of Defense budget, similar issues may arise as part of fiscal uncertainty and/or future debt ceiling limit debates in Congress. However, any future impact on ASUS and its operations will likely be limited to the timing of funding to pay for services rendered, delays in the processing of price redeterminations and issuance of contract modifications for new construction work not already funded by the U.S. government, and/or delays in the solicitation and/or awarding of new utility privatization opportunities under the Department of Defense utility privatization program.

The timing of the processing of future filings of price redeterminations may also be impacted by government actions, including audits by the Defense Contract Audit Agency ("DCAA"). The DCAA conducts audits of contractors for compliance with government guidance and regulations such as Federal Acquisition Regulations ("FAR") and Cost Accounting Standards ("CAS"). If the DCAA believes we have accounted for such costs in a manner inconsistent with the requirements for FAR or CAS, the DCAA auditor may recommend to our U.S. government corporate administrative contracting officer that such costs be disallowed. In addition, certain audit findings such as system deficiencies for government contract reporting requirements may result in delays in the timing of resolution of price redetermination filings. At times, the processing of our filing of price redeterminations and requests for equitable adjustment may be delayed pending the outcome of such audits or upon mutual agreement with the U.S. government.

Below is a summary of significant projects and price redetermination filings by subsidiaries of ASUS.

- FBWS - A filing to operate and maintain the East Bliss area at Fort Bliss was finalized in the third quarter of 2014 with an annual increase in operations and maintenance fees of approximately \$575,000, \$2.7 million in annual renewal & replacement fees and \$2.9 million of funding for capital upgrade modifications.
- TUS - The second and third price redeterminations for the contract to serve Andrews Air Force Base were filed with the U.S. government in November 2013. These price redeterminations cover the period February 2011 to January 2017. The second price redetermination was approved in September 2014. This agreement provided for an annualized increase in operations and maintenance fees of \$256,000 and included a retroactive amount for operations and maintenance for the period February 2011 through December 2013 of approximately \$747,000. In addition, renewal and replacement funds totaling approximately \$496,000 covering the period through September 2014 were added to the contract. The third price redetermination is expected to be resolved in the first quarter of 2015.
- ODUS - The second price redetermination for the Fort Lee privatization contract in Virginia, for the three-year period beginning February 2011, was filed in May 2012. The second price redetermination for the other bases that ODUS operates in Virginia, for the three-year period beginning April 2011, was filed in July 2012. Both of these filings were revised and resubmitted to the U.S. government in January 2014. These price redeterminations are expected to be resolved in the first quarter of 2015.
- PSUS - In February 2012, PSUS filed the first price redetermination for Fort Jackson, to be effective beginning February 16, 2010. Pending resolution of this filing, the U.S. government approved an interim increase of 3.4%, retroactive to February 2010. Based on negotiations, this redetermination filing was subsequently modified and re-submitted to the U.S. government in the first quarter of 2014. The revised first price redetermination was approved in September 2014. The approved agreement provided for an annual increase in operations and maintenance fees of approximately \$103,000 above the interim rate level. A retroactive O&M adjustment for the period through December 2013 of approximately \$405,000 was also provided. The second redetermination for Fort Jackson, covering the period February 2013 through February 2016, was filed in the third quarter of 2014 and is expected to be resolved in the first half of 2015.
- ONUS - In November 2013, ONUS filed the second price redetermination for the contract to serve Fort Bragg for the period covering March 2013 through February 2016. The second price redetermination was approved in September 30, 2014, resulting in an annualized increase in operations and maintenance fees of approximately \$615,000 together with a retroactive adjustment for the period through December 2013 of approximately \$513,000. The agreement also provided for additional renewal and replacement funding for the period through September 2014 of approximately \$5.8 million.

In September 2012, ONUS received a contract modification for approximately \$17.6 million for construction of water and sewer infrastructure at a new area in Fort Bragg. A second modification received in January 2014 reduced the contract amount to approximately \$16.5 million. The construction portion of this project was substantially completed during the fourth quarter of 2014.

In March 2012, ONUS received a contract modification based on a request for equitable adjustment regarding installation of new water meters at Fort Bragg. The contract modification provided for a reduction in the number of water meters to be installed and reduced the price associated with this revised scope. This \$11.0 million project commenced during the second quarter of 2012 and is expected to be completed by the fourth quarter of 2015. A \$12 million companion project to install backflow preventers was completed in December 2013.

In 2010, ONUS began work on a \$58 million pipeline replacement capital project at Fort Bragg, which was completed during the fourth quarter of 2014.

## **Regulatory Matters**

### ***Certificates of Public Convenience and Necessity***

GSWC holds Certificates of Public Convenience and Necessity (“CPCN”) granted by the CPUC in each of the ratemaking areas it serves. FBWS holds a CPCN from the Texas Commission on Environmental Quality. The Virginia State Corporation Commission exercises jurisdiction over ODUS as a public service company. The Maryland Public Service Commission approved the right of TUS to operate as a water and wastewater utility at Andrews Air Force Base, Maryland, based on certain conditions. The South Carolina Public Service Commission exercises jurisdiction over PSUS as a public service company. ONUS is regulated by the North Carolina Public Service Commission.

### ***Rate Regulation***

GSWC is subject to regulation by the CPUC, which has broad authority over service and facilities, rates, classification 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.

Rates that GSWC is authorized to charge are determined by the CPUC in general rate cases and are derived using rate base, cost of service and cost of capital, as projected for a future test year. 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 fair 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.

GSWC is required to file a water general rate case (“GRC”) application every three years according to a schedule established by the CPUC. GRCs typically include an increase in the first test year with inflation rate adjustments for expenses for the second and third years of the GRC cycle. For capital projects, there are two test years. Rates are based on a forecast of expenses and capital costs for the test year. Electric GRCs are typically filed every four years.

Rates may also be increased by offsets for certain expense increases, including, but not limited to, supply cost offset and balancing account amortization, advice letter filings related to certain plant additions and other operating cost increases.

Neither the operations nor rates of AWR and ASUS are directly regulated by the CPUC. The CPUC does, however, regulate certain transactions between GSWC and ASUS and between GSWC and AWR.

### ***Changes in Rates***

On May 9, 2013, the CPUC issued a final decision on GSWC’s water general rate case approving new rates for 2013 through 2015 at GSWC’s three water regions which include recovery of costs incurred at the general office. The new rates were retroactive to January 1, 2013 and generated approximately \$10 million in additional annual revenues in 2013 as compared to 2012 adopted revenues. The adopted water gross margin increased by approximately \$14 million, or 6.6%, when compared to the 2012 CPUC-adopted water gross margin. The CPUC also approved attrition year rate increases for five rate-making areas in Region I effective January 1, 2014. Attrition rate increases are based on an earnings test and inflation factors.

During 2014, the CPUC also approved rate increases in Region II and Region III related to supply cost increases experienced in those rate-making areas, which on an annual basis is expected to increase revenue by approximately \$6 million. These increases in revenues are offset by a corresponding increase in supply cost, resulting in no impact to earnings.

In February 2012, BVES filed its general rate case (“GRC”) for new rates in years 2013 through 2016. In May 2014, GSWC filed a settlement agreement with the CPUC covering all matters in the rate case which had been approved by all parties. On November 6, 2014, the CPUC issued a final decision approving the settlement agreement. The final decision, which was retroactive to January 1, 2013, did not have a significant impact on GSWC’s 2014 financial statements.

### ***Changes in Rates for 2015***

In November 2014, GSWC filed advice letters with the CPUC requesting its third-year rate increases. These authorized revenue increases were effective January 1, 2015 and are expected to generate an additional increase in the water gross margin for 2015 of approximately \$1.8 million as compared to the gross margin in 2014. Attrition rate increases are based on an earnings test and inflation factors.

For BVES, the CPUC-approved base revenues for 2015 that are expected to generate an additional \$400,000 in revenues as compared to the adopted 2014 base revenues.

### ***Pending Rate Requests***

In July 2014, GSWC filed a general rate case for all of its water regions and the general office. The application will determine rates for the years 2016, 2017 and 2018. GSWC's requested capital budgets in the application average approximately \$90 million a year for the three year period. The 2016 water gross margin is expected to decrease by approximately \$700,000 as compared to the currently adopted levels due, in part, to a decrease in annual depreciation expense resulting from an updated depreciation study.

### ***Cost of Capital Proceedings for Water Regions***

In July 2012, the CPUC issued a final decision on GSWC's water cost of capital proceeding. The decision authorized, among other things, a return on equity ("ROE") of 9.99% and for GSWC to continue the Water Cost of Capital Mechanism ("WCCM"). The WCCM adjusts ROE and rate of return on rate base between the three-year cost of capital proceedings only if there is a positive or negative change of more than 100 basis points in the average of the Moody's Aa utility bond rate as measured over the period October 1 through September 30. If the average Moody's rate for this period changes by over 100 basis points from the benchmark, the ROE will be adjusted by one half of the difference. For the period October 1, 2011 through September 30, 2012, the Moody's rate declined by 112 basis points from the benchmark. As a result, in 2012 GSWC filed an advice letter to lower its water ROE by 56 basis points, from 9.99% to 9.43%, which was incorporated into 2013 water rates. For the period October 1, 2013 through September 30, 2014, the Moody's rate increased by 30 basis points from the benchmark. As a result, GSWC's current water ROE of 9.43% remained unchanged for 2014.

GSWC was scheduled to file its next cost of capital application in March 2015 based on an extension previously granted. However, in November 2014 GSWC, along with three other Class A California water companies ("Joint Parties"), filed with the CPUC a request for further extension of the date by which each of them is required to file its 2015 Cost of Capital Application. The Joint Parties requested approval to postpone this filing date one additional year until March 31, 2016, with a corresponding effective date of January 1, 2017 in compliance with the Rate Case Plan. The Joint Parties believe that postponing the filing one year will alleviate administrative processing costs on the four Class A utilities as well as Commission staff, and provide relief for both Commission and utility resources already strained by numerous proceedings. The Joint Parties also believe that the current economic environment is such that a change from the currently adopted return on equity would be small. The CPUC approved this request in January 2015. As a result of the approval, GSWC's current authorized cost of capital will continue in effect through December 2016, and GSWC will forgo a cost of capital adjustment in 2016 in the event that the WCCM mechanism is triggered.

### ***Other Regulatory Matters***

#### **Alternative Revenue Mechanisms:**

GSWC records the difference between the adopted level of volumetric revenues as authorized by the CPUC for metered accounts (volumetric revenues) and the actual volumetric revenues recovered in customer rates. GSWC also records the difference between adopted and actual expense levels for purchased water, purchased power and pump taxes, as established by the CPUC, using the MCBA. As required by the accounting guidance for alternative revenue programs, GSWC is required to collect its WRAM, net of its MCBA, within 24 months following the year in which they are recorded. In April 2012, the CPUC issued a final decision which, among other things, sets the recovery period for under-collected balances that are up to 15% of adopted annual revenues at 18 months or less. For under-collected balances greater than 15%, the recovery period is 19 to 36 months. At December 31, 2014, the recovery periods for the majority of GSWC's WRAM/MCBA balances were primarily within the 12 to 18 month period.

In addition to adopting an amortization schedule, the final decision sets a cap on total net WRAM/MCBA surcharges in any given calendar year of 10% of the last authorized revenue requirement. This cap has not impacted any GSWC WRAM/MCBA recoveries to-date. Surcharges are currently in place to recover the WRAM/MCBA balances for 2013.

For BVES, the CPUC approved the BRRAM, which adjusts certain revenues to adopted levels. In November 2014, the CPUC issued a final decision on the BVES general rate case, setting rates and adopted revenues for years 2013 through 2016. As a result of this decision, GSWC filed with the CPUC for recovery of the 2013 BRRAM under-collection of \$2.3 million to be collected over 24 months. As of December 31, 2014, GSWC had a \$7.8 million under-collection in the BRRAM, which is reflected as a regulatory asset.

Procurement Audits:

In December 2011, the CPUC issued a final decision adopting a settlement between GSWC and the CPUC on its investigation of certain work orders and charges paid to a specific contractor used previously for numerous construction projects primarily in one of GSWC's three main geographic water regions. As part of the settlement reached with the CPUC on this matter, GSWC agreed to be subject to three separate independent audits of its procurement practices over a period of 10 years from the date the settlement was approved by the CPUC. The audits cover GSWC's procurement practices for contracts with other contractors from 1994 forward. The first audit started in 2014 and covers almost a 20-year period from January 1, 1994 through September 30, 2013.

In December 2014, the accounting firm engaged by the CPUC to conduct the first audit provided its draft report to GSWC for comments. The draft report provides details on the accounting firm's findings and corresponding recommendations. The report asserts that GSWC had not complied, in all material respects, with the CPUC's requirements and GSWC's procurement policies during the period from 1994 to 2006. Subsequent to 2006, except for certain instances of alleged noncompliance, GSWC was found to be in compliance, in all material respects, with the CPUC's requirements and GSWC's procurement policies. The findings and corresponding recommendations in the draft report focused on, among other things, inadequate documentation to support competitive bidding procedures, change orders, and sole source justifications.

In February 2015, management provided to the auditors its responses to the draft report and each of the findings noted by the auditors. Among other things, GSWC informed the auditors of certain factual inaccuracies in their report, asserted that GSWC has complied, in all material respects, with the CPUC's requirements throughout the entire audit period and, has been in material compliance with its own procurement policies throughout the audit period. The auditors are finalizing their audit report in light of GSWC's comments. After the report is finalized, GSWC will meet with the CPUC to discuss what, if any, further action is required. If the CPUC determines that GSWC has violated the CPUC's or GSWC's procurement policies during the 20-year audit period, the CPUC may pursue disallowances and/or penalties from GSWC in the pending rate case proceeding or in a new proceeding. GSWC likely will be given an opportunity to defend itself against any such attempt by the CPUC to pursue disallowances and/or penalties. At this time management cannot predict the final outcome of this first audit and cannot determine a possible loss or range of loss, if any, associated with any disallowances and/or penalties that may be pursued by the CPUC against GSWC.

Rural Acquisition:

In October 2013, GSWC filed an Application to acquire the assets of Rural Water Company used to provide water service in Rural's service territory, to expand GSWC's Certificate of Public Convenience and Necessity to incorporate the Rural service territory into GSWC's existing Santa Maria district, and to authorize GSWC to provide service in Rural's service territory. On July 18, 2014, GSWC filed a Motion to Adopt a Settlement resolving all issues in GSWC's application. Under the terms of the settlement, if approved by the CPUC, the purchase price for the acquisition of Rural Water will be included in GSWC's rate base. GSWC expects that it will be able to recover the associated revenue requirement from customers in rates. Rural serves approximately 900 customers in the county of San Luis Obispo, California.

Renewables portfolio standard:

In December 2011, a renewables portfolio standard ("RPS") law went into effect which changed, among other things, annual procurement targets to multi-year procurement targets. In December 2012, GSWC entered into a ten-year agreement with a third party to purchase renewable energy credits ("RECs") whereby GSWC agreed to purchase approximately 582,000 RECs over a 10-year period which would be used towards meeting the CPUC's RPS procurement requirements. As of December 31, 2014, GSWC has purchased sufficient RECs to be in compliance for all periods through 2014. Accordingly, no provision for loss or potential penalties has been recorded in the financial statements as of December 31, 2014. GSWC intends to file its 2014 compliance report with the CPUC by the August 2015 deadline. The cost of these RECs have been included as part of the electric supply cost balancing account as of December 31, 2014.

New Service Territory Application, Sutter County:

On June 26, 2014, the CPUC approved a Certificate of Public Convenience and Necessity application granting GSWC the authority to provide water utility services to an area to be developed near Sacramento, in Sutter County, California, called Sutter Pointe. The CPUC's decision approved a settlement that was jointly filed by GSWC, Sutter County, the Sutter Pointe Developers, and a coalition of Sutter County residents. With the CPUC's approval, GSWC will create a water service district to supply the Sutter Pointe development with groundwater and surface water from the Sacramento River. The project will involve the construction of underground infrastructure and groundwater wells with a treatment plant and storage facility to serve retail, industrial and approximately 17,000 residential customers at final build out. The decision also sets a cap on the revenue requirement per Sutter Pointe customer during the first two rate cycles. As part of the agreement, GSWC will also request approval from the CPUC to acquire the water system that currently serves the community of Robbins in Sutter County. In

August 2014, the Office of Ratepayer Advocates filed an application for rehearing on the application. At this time, management cannot predict if a rehearing will be granted or the outcome of any rehearing if granted.

*New Service Territory Application, Westborough Development, Sacramento County:*

On October 12, 2004, GSWC and Aerojet-General Corporation (“Aerojet”) reached a settlement relating to groundwater contamination impacting GSWC’s Arden-Cordova Water System. Portions of the settlement called for GSWC to serve new territory, subject to CPUC approval, on property owned by Aerojet known as Westborough. Aerojet and GSWC are working cooperatively to identify and implement the best alternative to meet the long-term water supply needs of GSWC’s Rancho Cordova customers within the Arden-Cordova service area as well as supply for the new Westborough development area owned by Aerojet. The County of Sacramento and the City of Folsom, through various arrangements, have agreed not to protest GSWC’s application to the CPUC for a CPCN for this territory.

GSWC intends to file with the CPUC to incorporate the Westborough development in Sacramento County into the Rancho Cordova service area and to provide water service to that new development following completion of a water supply solution for the area.

*Affiliate Transaction Rules:*

Rules adopted by the CPUC regarding affiliate transactions and use of regulated assets establish a standard set of rules to govern transactions between a regulated water utility, its parent, and other affiliated companies. Registrant monitors its cost allocation and management of the regulated and non-regulated segments for compliance with these rules.

For more information regarding significant regulatory matters, see Note 2 of “*Notes to Financial Statements*” included in Part II, Item 8 in Financial Statements and Supplementary Data.

**Environmental Matters**

AWR’s subsidiaries are subject to stringent environmental regulations, including the 1996 amendments to the Federal Safe Drinking Water Act; interim enhanced surface water treatment rules; regulation of disinfectant/disinfection by-products; and the long-term enhanced surface water treatment rules; the ground water rule; contaminant regulation of arsenic, perchlorate and hexavalent chromium; and unregulated contaminants monitoring rule.

The CPUC requires GSWC to comply with the safe drinking water standards established by the U.S. Environmental Protection Agency (“EPA”) and the Division of Drinking Water (DDW), formerly the California Department of Public Health, under the State Water Resources Control Board (“SWRCB”). The EPA regulates contaminants that may have adverse health effects that 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 DDW, acting on behalf of the EPA, administers the EPA’s program in California. Similar state agencies administer these rules in the other states in which Registrant operates.

GSWC currently tests its water supplies and water systems according to, among other things, requirements listed in the Federal Safe Drinking Water Act (“SDWA”). In compliance with the SDWA and to assure a safe drinking water supply to its customers, GSWC has incurred operating costs for testing to determine the levels, if any, of the constituents in its sources of supply and additional expense to treat contaminants in order to meet the federal and state maximum contaminant level (“MCL”) standards and consumer demands. GSWC expects to incur additional capital costs as well as increased operating costs to maintain or improve the quality of water delivered to its customers in light of anticipated stress on water resources associated with watershed and aquifer pollution, as well as to meet future water quality standards. The CPUC ratemaking process provides GSWC with the opportunity to recover prudently incurred capital and operating costs in future filings associated with achieving water quality standards. Management believes that such incurred and expected future costs should be authorized for recovery by the CPUC.

In August 2013, the DDW proposed a maximum contaminant level (“MCL”) for hexavalent chromium (chromium-6) of 0.010 milligram per liter. On April 15, 2014, after reviewing and addressing all the comments, DDW determined to maintain the proposed chromium-6 MCL at 0.010 mg/L. The MCL took effect on July 1, 2014. All water systems are required by the new regulation to conduct initial monitoring to determine compliance before January 1, 2015. Based on monitoring results, management does not believe that the chromium-6 MCL poses significant impact on GSWC groundwater sources.

The SWRCB adopted a new discharge permit for drinking water systems in November 2014. The new requirements centralize the permit process, which could result in cost savings for GSWC in terms of fees, laboratory analysis and labor. The deadline for application is September 1, 2015. GSWC plans to transition its current permits to the single permit by the required deadline.

### ***Matters Relating to GSWC's Arden-Cordova Water System***

In GSWC's Arden-Cordova system, several wells have been removed from service and destroyed due to perchlorate, and/or nitrosodimethylamine ("NDMA") levels that exceed the regulatory standards or notification levels.

It is believed that this contamination is related to the activities of Aerojet who has, in the past, used ammonium perchlorate in oxidizing rocket fuels.

On October 12, 2004, GSWC and Aerojet reached a settlement relating to this contamination. Under the terms of the settlement, Aerojet paid GSWC \$8.7 million in 2004 and paid an additional \$8 million over a period of five years from 2009 through 2013, plus interest. These payments offset GSWC's costs of utility plant and purchased water used to cure the water supply impacted by contamination by \$16 million and \$735,000, respectively.

GSWC and Aerojet are developing alternatives to meet the water supply needs of GSWC to ensure a continued reliable and safe water supply for GSWC's Rancho Cordova customers within the Arden-Cordova service area as well as supply for the new Westborough development area owned by Aerojet.

### ***Matters Relating to GSWC's Florence Graham Water System***

Perchlorate has been detected in five wells servicing GSWC's Florence-Graham System. Two of these wells exceeded the perchlorate drinking water standard and were removed from service, yet remain below the MCL. Continued monitoring shows that perchlorate levels are increasing in the three wells that remain in service. The Water Replenishment District of Southern California is partnering with the Department of Toxic Substances Control to examine the perchlorate contamination in this area and is trying to determine the source(s) of the plume.

To maintain reliable water supply within the Florence-Graham system, GSWC used blending and treatment to return those two wells to service in 2014.

### ***Matters Relating to GSWC's Norwalk Water System***

Volatile Organic Compounds ("VOCs") have been detected in eight wells in GSWC's Norwalk Water System. Seven of these wells are equipped with granular activated carbon filter treatment for VOC removal. These wells are located within a Superfund site that the EPA has designated as the Omega Operable Unit 2. EPA is currently working on a remediation project to clean up the VOC plume. Recent modeling data have shown that at least three GSWC wells, and potentially more, are impacted by the Omega plume. GSWC intends to work closely with the EPA to ensure that the remediation remedy proposed by the EPA will address GSWC's concerns regarding impacts to its water supply.

### ***Matters Relating to Environmental Clean-Up***

GSWC has been involved in environmental remediation and clean-up at a plant site ("Chadron Plant") that contained an underground storage tank which was used to store gasoline for its vehicles. This tank was removed from the ground in July 1990 along with the dispenser and ancillary piping. Since then, GSWC has been involved in various remediation activities at this site. Recent analysis indicates that offsite monitoring wells may also be necessary to document effectiveness of remediation.

As of December 31, 2014, the total spent to clean-up and remediate GSWC's plant facility was approximately \$4.5 million, of which \$1.5 million has been paid by the State of California Underground Storage Tank Fund. Amounts paid by GSWC have been included in rate base and approved by the CPUC for recovery. As of December 31, 2014, GSWC has a regulatory asset and an accrued liability for the estimated additional cost of \$1.4 million to complete the clean-up at the site. The estimate includes costs for two years of continued activities of groundwater cleanup and monitoring, future soil treatment and site closure related activities. The ultimate cost may vary as there are many unknowns in remediation of underground gasoline spills and this is an estimate based on currently available information. Management also believes it is probable that the estimated additional costs will be approved in rate base by the CPUC.

### ***Matters Relating to Military Privatization Contracts***

Each of the Military Utility Privatization Subsidiaries is responsible for testing the water and wastewater systems on the military bases on which it operates in accordance with applicable law.

Each of the Military Utility Privatization Subsidiaries has the right to seek an equitable adjustment to its contract in the event that there are changes in environmental laws, a change in the quality of water used in providing water service or wastewater discharged by the U.S. government or contamination of the air or soil not caused by the fault or negligence of the Military Utility Privatization Subsidiary. These changes can impact the cost of operating and maintaining or renewing and replacing facilities under the contracts. The U.S. government is responsible for environmental contamination due to its fault or negligence and for environmental contamination that occurred prior to the execution of the contract(s).

## **Security Issues**

GSWC has implemented measures to increase security in accordance with a vulnerability assessment of its water systems and has upgraded its facilities to enhance the safety of water system operations. GSWC also has security systems and infrastructure in place intended to prevent cyber-attacks. Despite its efforts, GSWC cannot be assured that a cyber or terrorist attack will not cause water or electric system problems, disrupt service to customers, compromise important data or systems or result in unintended release of customer or employee information.

GSWC periodically revises its Emergency Response Plan and periodically conducts operational security exercises for all of its water systems. GSWC also considers advances in security technology and relevant industry developments in developing its capital improvement plans. GSWC intends to seek approval of the CPUC to recover any additional costs that it incurs in enhancing the security of its water systems.

The Military Utility Privatization Subsidiaries operate facilities within the boundaries of military bases which provide limited access to the general public. To further enhance security, certain upgrades were completed at various military bases through contract modifications funded by the U.S. government.

## **Water Supply**

### ***GSWC's Water Supply***

During 2014, GSWC delivered approximately 69,248,000 hundred cubic feet ("ccf") of water to its customers, which is an average of about 436 acre-feet per day. (An acre-foot is about 435.6 ccf or 326,000 gallons). Approximately 60% came from groundwater production wells situated throughout GSWC's service areas. GSWC supplemented groundwater production with wholesale purchases from Metropolitan Water District of Southern California ("MWD") member agencies and regional water suppliers (roughly 35% of total demand) and with authorized diversions from rivers (roughly 5%) under contracts with the United States Bureau of Reclamation ("Bureau") and the Sacramento Municipal Utility District ("SMUD"). During 2013, GSWC supplied 73,430,000 ccf of water, approximately 60% of which was produced from groundwater sources and 40% was purchased from regional wholesalers and surface water diversions under contracts with the Bureau and SMUD. GSWC continually assesses its water rights and groundwater storage assets. In addition, GSWC encourages voluntary conservation measures by its customers and has implemented customer education initiatives to help with supply variability and the general scarcity of water supplies.

### ***Groundwater***

Over the years, population growth in GSWC's service areas and increases in the amount of groundwater used have resulted in both cooperative and judicially-enforced regimes for owning water rights and managing groundwater basins for long-term sustainability. GSWC management actively participates in efforts to protect groundwater basins from over-use and from contamination and to protect its water rights. In some periods, these efforts require reductions in groundwater pumping and increased reliance on alternative water resources.

GSWC owns approximately 85,000 acre-feet of adjudicated water rights, mostly groundwater, and a number of unadjudicated water rights to help meet supply requirements. The productivity of GSWC's groundwater resources varies from year to year depending upon a variety of factors, including the amount, duration, length and location of rainfall, the availability of imported replenishment water, the amount of water previously stored in groundwater basins, the amount and seasonality of water use by GSWC's customers and others, evolving challenges to water quality, and a variety of legal limitations on use, if a groundwater basin is, or may be, in an over-drafted condition.

On September 16, 2014, California Governor Edmund G. Brown, Jr. signed a package of three bills, which taken together are known as the "Sustainable Groundwater Management Act." The purpose of the act is to provide local agencies with tools and authority to manage groundwater basins in a sustainable manner over the long-term. Local "Groundwater Sustainability Agencies" are to be formed for each defined groundwater basin, and Groundwater Sustainability Plans must be completed for those basins considered in critical overdraft. The Act contains numerous provisions to protect existing water rights, and is not anticipated to infringe upon or otherwise alter existing surface water or groundwater rights under current law. GSWC intends to cooperate to the fullest extent allowed in the development of these Groundwater Sustainability Agencies and resulting Groundwater Sustainability Plans to protect its interests in proper management of these groundwater basins.



### ***Imported Water***

GSWC also manages a portfolio of water supply arrangements with water wholesalers. For example, GSWC has contracts with various governmental entities (principally MWD's member agencies) and other parties to purchase water through a total of 63 connections for distribution to customers, in addition to numerous emergency connections. MWD is a public agency organized and managed to provide a supplemental, imported supply to its member public agencies. There are 26 such member agencies, consisting of 14 cities, 11 municipal water districts, and one county water authority. GSWC has 46 connections to MWD's water distribution facilities and those of member agencies. GSWC purchases MWD water through six separate member agencies aggregating more than 47,100 acre-feet annually. MWD's principal sources of water are the State Water Project ("SWP") which conveys water from northern California and the Colorado River.

GSWC has contracts to purchase water or water rights for an aggregate amount of \$5.3 million as of December 31, 2014. Included in the \$5.3 million is a remaining commitment of \$3.1 million under an agreement with the City of Claremont ("the City") to lease water rights that were ascribed to the City as part of the Six Basins adjudication. The initial term of the agreement expires in 2028. GSWC can exercise an option to renew this agreement for 10 additional years. The remaining \$2.2 million are commitments for purchased water with other third parties which expire through 2038.

### ***Metropolitan Water District/ State Water Project***

Water supplies available to the MWD through the State Water Project vary from year to year based on several factors. Historically, weather was the primary factor in determining annual deliveries. However, biological opinions issued in late 2007 have limited water diversions through the Sacramento/San Joaquin Delta ("Delta") resulting in pumping restrictions on the State Water Project. Even with variable State Water Project deliveries, MWD has been able to provide sufficient quantities of water to satisfy the needs of its member agencies and their customers. Under its Integrated Resources Plan, MWD estimates that it can meet its member agencies' demands over at least the next 20 years.

Every year, the California Department of Water Resources ("DWR") establishes the State Water Project allocation for water deliveries to the state water contractors. DWR generally establishes a percentage allocation of delivery requests based on a number of factors, including weather patterns, snow pack levels, reservoir levels and biological diversion restrictions. In January 2015, DWR increased the water allocation from 10% to 15% of state contractor requests.

MWD has stated that it intends to recommend to its board that MWD adopt a water allocation plan in June or July 2015 if allocations from the State Water Project are below 40% in April or May 2015. At this time, GSWC cannot predict what impact, if any, a water allocation plan will have on GSWC's water supplies. Lower water allocations from the State Water Project has resulted in more reliance on water from the Colorado River and other sources to meet MWD members' needs.

### ***Colorado River***

On October 17, 2003, the Federal government, acting through the Bureau in its capacity as Colorado River watermaster, the State of California, and four southern California water agencies, including MWD, reached an agreement, known as the Quantification Settlement Agreement ("QSA"). The QSA allocates California's annual 4.4 million acre-feet ("MAF") share of the Colorado River among those agencies and provides the framework for accounting and transfers among them. Under the QSA, MWD will continue to have access to its base allotment of Colorado River water each year, as well as excess Colorado River water until October 2016, and up to 1.6 MAF of additional water that the Imperial Irrigation District proposes to conserve and sell to the state for use by MWD members.

### ***Climate Outlook and Impacts of Low Precipitation on Groundwater Supplies***

In January 2014, California Governor Edmund G. Brown, Jr. declared a drought state of emergency for California after the state experienced one of the driest years in recorded state history and the third consecutive year of below average precipitation and snowfall throughout the state. In response, GSWC has asked its customers to voluntarily reduce their water usage by 20%. In May 2014, GSWC revised its water conservation and rationing plan approved by the CPUC that prohibits wasteful water use. On January 29, 2015, the Department of Water Resources reported that the state's snowpack was at 25% of historical average.

In July 2014, the SWRCB approved emergency regulations that implement mandatory restrictions on certain outdoor urban water uses. Any violation of these uses is considered a criminal offense with possible fines of up to \$500 per day. In addition, urban water suppliers are required to implement their Water Shortage Contingency Plans at a level that triggers mandatory restrictions on outdoor water use. Failure to comply with this requirement may result in potential fines of \$10,000 per day issued by the SWRCB. The CPUC issued Resolution W-5000 requiring regulated utilities to comply with the SWRCB regulations and work with local enforcement agencies on water waste reporting. In response to the CPUC Resolution and the SWRCB emergency regulations, GSWC implemented Stage II of its Water Shortage Contingency Plans (WSCP) for all systems in August 2014 and informed all customers of the SWRCB regulations via direct bill messaging. GSWC's water

conservation and rationing plan approved by the CPUC is aligned with the emergency regulations. However, GSWC may implement further response plans that include additional water use restrictions and possible penalties pending direction from the CPUC.

As of January 20, 2015, the U.S. Drought Monitor lists 94 percent of California in the rank of “Severe Drought” or “Exceptional Drought”. If dry conditions continue, GSWC may implement mandatory water rationing to its customers. Also, in the event of water supply shortages, GSWC would need to transport additional water from other areas, increasing the cost of water supply. These additional costs would result in higher costs to customers which, taken together with mandatory water rationing, may lead to increased complaints.

Reduced rainfall results in reduced recharge to the State’s groundwater basins. Water levels in several of these basins, especially smaller basins, are dropping. GSWC utilizes groundwater from seventeen groundwater basins throughout the State. Several GSWC service areas rely on groundwater as their only source of supply. Should dry conditions persist, areas served by these smaller basins may be more likely to experience future mandatory conservation measures.

***Potential Additional Sources of Supply:***

GSWC continues to assess additional water supply opportunities to expand and firm up its water supply portfolio for service to customers. In June, 2010, GSWC signed an agreement with Cadiz Inc. giving GSWC the right to acquire an annual supply of Cadiz water once Cadiz secures appropriate transport and conveyance facilities and necessary agreements to move water from Cadiz’s property in Fenner Valley to metropolitan Southern California. In addition, GSWC in March 2010 signed a non-binding Letter of Intent with Poseidon Resources to purchase desalination water from a seawater desalination plant under consideration for construction by Poseidon Resources in the City of Huntington Beach in the future.

***Military Utility Privatization Subsidiaries***

The U.S. government is responsible for providing the source of supply for all water on each of the bases served by the Military Utility Privatization Subsidiaries at no cost to the Military Utility Privatization Subsidiaries.

**New Accounting Pronouncements**

Registrant is subject to newly issued requirements as well as changes in existing requirements issued by the Financial Accounting Standards Board. Differences in financial reporting between periods could occur unless and until the CPUC approves such changes for conformity through regulatory proceedings. See *Note 1 of Notes to Consolidated Financial Statements*.

## **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

Registrant is exposed to certain market risks, including fluctuations in interest rates, and commodity price risk primarily relating to changes in the market price of electricity. Market risk is the potential loss arising from adverse changes in prevailing market rates and prices.

### **Interest Rate Risk**

A significant portion of Registrant's capital structure is comprised primarily of fixed-rate debt. Market risk related to our fixed-rate debt is deemed to be the potential increase in fair value resulting from a decrease in interest rates. At December 31, 2014, the fair value of Registrant's long-term debt was \$417.1 million. A hypothetical ten percent decrease in market interest rates would have resulted in an \$18.6 million increase in the fair value of Registrant's long-term debt.

Market risk related to Registrant's variable-rate debt is estimated as the potential decrease in pretax earnings resulting from an increase in interest rates. In November 2014, Registrant repaid \$6.0 million in variable interest debt and as of December 31, 2014, had \$125,000 in variable interest rate debt outstanding. A hypothetical one percent rise in interest rates would not result in a material impact to earnings.

At December 31, 2014, Registrant did not believe that its short-term debt was subject to interest rate risk due to the fair market value being approximately equal to the carrying value.

### **Commodity/Derivative Risk**

GSWC is exposed to commodity price risk primarily relating to changes in the market price of electricity for its electric division, BVES. To manage its exposure to energy price risk, GSWC from time to time executes purchased power contracts that qualify as derivative instruments, requiring mark-to-market derivative accounting under the accounting guidance for derivatives. A derivative financial instrument or other contract derives its value from another investment or designated benchmark.

In June 2013, GSWC filed an application with the CPUC for pre-approval of purchased power contracts with two providers. In December 2014, the CPUC approved the application, which allowed GSWC to immediately execute new long-term purchased power contracts with the energy providers on December 9, 2014. GSWC began taking power under these long-term contracts effective January 1, 2015 at a fixed cost over three and five year terms depending on the amount of power and period during which the power is purchased under the contracts. During 2014, GSWC's power purchases were based on month-to-month arrangements, as the previous long-term purchase power contract expired in 2013.

The new long-term contracts executed in December 2014 qualify for derivative accounting treatment. Among other things, the CPUC approval in December 2014 also authorized GSWC to establish a regulatory asset and liability memorandum account to offset the mark-to-market entries required by the accounting guidance. Accordingly, all unrealized gains and losses generated from these purchased power contracts will be deferred on a monthly basis into a non-interest bearing regulatory memorandum account that tracks the changes in fair value of the derivative throughout the term of the contract. As a result, these unrealized gains and losses on these contracts will not impact GSWC's earnings. As of December 31, 2014, there was a \$3.3 million unrealized loss in the memorandum account for the new purchased power contracts as a result of the recent drop in energy prices.

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

## **Item 8. Financial Statements and Supplementary Data**

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**AMERICAN STATES WATER COMPANY  
CONSOLIDATED BALANCE SHEETS**

(in thousands)	December 31,	
	2014	2013
<b>Assets</b>		
<b>Utility Plant</b>		
<u>Regulated utility plant, at cost:</u>		
Water	\$ 1,363,074	\$ 1,307,509
Electric	81,636	79,360
Total	1,444,710	1,386,869
Non-regulated utility property, at cost	10,706	9,090
Total utility plant, at cost	1,455,416	1,395,959
Less — accumulated depreciation	(500,239)	(471,665)
	955,177	924,294
Construction work in progress	48,343	57,183
Net utility plant	1,003,520	981,477
<b>Other Property and Investments</b>		
Goodwill	1,116	1,116
Other property and investments	17,536	15,806
Total other property and investments	18,652	16,922
<b>Current Assets</b>		
Cash and cash equivalents	75,988	38,226
Accounts receivable-customers, less allowance for doubtful accounts	18,814	23,829
Unbilled revenue	21,422	18,552
Receivable from U.S. government, less allowance for doubtful accounts	6,709	7,106
Other accounts receivable, less allowance for doubtful accounts	4,843	4,914
Income taxes receivable	20,993	9,214
Materials and supplies	3,588	4,558
Regulatory assets — current	12,379	27,676
Prepayments and other current assets	2,745	2,481
Costs and estimated earnings in excess of billings on uncompleted contracts	34,535	45,508
Deferred income taxes — current	7,435	9,553
Total current assets	209,451	191,617
<b>Regulatory and Other Assets</b>		
Regulatory assets	118,829	95,005
Costs and estimated earnings in excess of billings on uncompleted contracts	12,228	7,823
Unbilled receivable	3,513	3,104
Deferred income taxes	—	8
Other	12,105	14,227
Total regulatory and other assets	146,675	120,167
<b>Total Assets</b>	\$ 1,378,298	\$ 1,310,183

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

**AMERICAN STATES WATER COMPANY  
CONSOLIDATED BALANCE SHEETS**

(in thousands)	December 31,	
	2014	2013
<b>Capitalization and Liabilities</b>		
<b>Capitalization</b>		
Common shareholders' equity	\$ 506,801	\$ 492,404
Long-term debt	325,798	326,079
Total capitalization	832,599	818,483
<b>Current Liabilities</b>		
Long-term debt — current	292	6,298
Accounts payable	41,855	49,787
Income taxes payable	638	507
Accrued other taxes	8,602	9,802
Accrued employee expenses	10,519	10,801
Accrued interest	3,549	3,897
Unrealized loss on purchased power contracts	3,339	—
Billings in excess of costs and estimated earnings on uncompleted contracts	11,736	6,852
Other	18,760	12,962
Total current liabilities	99,290	100,906
<b>Other Credits</b>		
Advances for construction	68,328	69,332
Contributions in aid of construction — net	116,629	114,916
Deferred income taxes	191,209	159,506
Unamortized investment tax credits	1,699	1,790
Accrued pension and other post-retirement benefits	61,773	38,726
Other	6,771	6,524
Total other credits	446,409	390,794
<b>Commitments and Contingencies (Notes 13 and 14)</b>		
<b>Total Capitalization and Liabilities</b>	<b>\$ 1,378,298</b>	<b>\$ 1,310,183</b>

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

**AMERICAN STATES WATER COMPANY**  
**CONSOLIDATED STATEMENTS OF CAPITALIZATION**

(in thousands, except share data)	December 31,	
	2014	2013
<b>Common Shareholders' Equity:</b>		
Common Shares, no par value:		
Authorized: 60,000,000 shares		
Outstanding: 38,286,626 shares in 2014 and 38,720,693 shares in 2013	\$ 253,199	\$ 253,961
Earnings reinvested in the business	253,602	238,443
	506,801	492,404
<b>Long-Term Debt (All are of GSWC)</b>		
Notes/Debentures:		
6.87% notes due 2023	—	5,000
7.00% notes due 2023	—	10,000
6.81% notes due 2028	15,000	15,000
6.59% notes due 2029	40,000	40,000
7.875% notes due 2030	20,000	20,000
7.23% notes due 2031	50,000	50,000
6.00% notes due 2041	62,000	62,000
Private Placement Notes:		
3.45% notes due 2029	15,000	—
9.56% notes due 2031	28,000	28,000
5.87% notes due 2028	40,000	40,000
6.70% notes due 2019	40,000	40,000
Tax-Exempt Obligations:		
5.50% notes due 2026	7,730	7,730
Variable Rate Obligation due 2014	—	6,000
State Water Project due 2035	4,077	4,190
Other Debt Instruments:		
Variable Rate Obligation due 2018	125	161
American Recovery and Reinvestment Act Obligation due 2033	4,158	4,269
Capital lease obligations	—	27
	326,090	332,377
Less: Current maturities	(292)	(6,298)
	325,798	326,079
<b>Total Capitalization</b>	<b>\$ 832,599</b>	<b>\$ 818,483</b>

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

**AMERICAN STATES WATER COMPANY**  
**CONSOLIDATED STATEMENTS OF INCOME**

(in thousands, except per share amounts)	For the years ended December 31,		
	2014	2013	2012
<b>Operating Revenues</b>			
Water	\$ 326,672	\$ 320,131	\$ 305,898
Electric	34,387	38,409	37,033
Contracted services	104,732	113,537	123,977
Total operating revenues	465,791	472,077	466,908
<b>Operating Expenses</b>			
Water purchased	57,790	58,930	54,010
Power purchased for pumping	10,700	9,518	8,355
Groundwater production assessment	16,450	15,541	14,732
Power purchased for resale	9,649	13,392	12,120
Supply cost balancing accounts	6,346	214	11,709
Other operation	28,288	27,767	29,790
Administrative and general	78,323	77,291	70,556
Depreciation and amortization	41,073	40,090	41,385
Maintenance	16,092	17,772	15,887
Property and other taxes	16,722	15,865	15,381
ASUS construction	65,368	76,627	81,957
Net gain on sale of property	(55)	(2)	(68)
Total operating expenses	346,746	353,005	355,814
<b>Operating Income</b>	119,045	119,072	111,094
<b>Other Income and Expenses</b>			
Interest expense	(21,617)	(22,415)	(22,765)
Interest income	927	707	1,333
Other, net	751	1,105	431
Total other income and expenses	(19,939)	(20,603)	(21,001)
<b>Income from operations before income tax expense</b>	99,106	98,469	90,093
Income tax expense	38,048	35,783	35,945
<b>Net Income</b>	\$ 61,058	\$ 62,686	\$ 54,148
<b>Weighted Average Number of Shares Outstanding</b>	38,658	38,639	37,998
<b>Basic Earnings Per Common Share</b>	\$ 1.57	\$ 1.61	\$ 1.42
<b>Weighted Average Number of Diluted Shares</b>	38,880	38,869	38,262
<b>Fully Diluted Earnings Per Share</b>	\$ 1.57	\$ 1.61	\$ 1.41
<b>Dividends Declared Per Common Share</b>	\$ 0.831	\$ 0.760	\$ 0.635

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



**AMERICAN STATES WATER COMPANY**  
**CONSOLIDATED STATEMENTS OF CHANGES**  
**IN COMMON SHAREHOLDERS' EQUITY**

(in thousands)	Common Shares		Earnings Reinvested in the Business	Total
	Number of Shares	Amount		
<b>Balances at December 31, 2011</b>	37,578	\$ 233,306	\$ 175,360	\$ 408,666
Add:				
Net income			54,148	54,148
Exercise of stock options and other issuance of Common Shares	896	13,295		13,295
Tax benefit from employee stock-based awards		890		890
Compensation on stock-based awards		1,710		1,710
Dividend equivalent rights on stock-based awards not paid in cash		121		121
Deduct:				
Dividends on Common Shares			24,130	24,130
Dividend equivalent rights on stock-based awards not paid in cash			121	121
<b>Balances at December 31, 2012</b>	38,474	249,322	205,257	454,579
Add:				
Net income			62,686	62,686
Exercise of stock options and other issuance of Common Shares	247	2,111		2,111
Tax benefit from employee stock-based awards		1,026		1,026
Compensation on stock-based awards		1,362		1,362
Dividend equivalent rights on stock-based awards not paid in cash		140		140
Deduct:				
Dividends on Common Shares			29,360	29,360
Dividend equivalent rights on stock-based awards not paid in cash			140	140
<b>Balances at December 31, 2013</b>	38,721	253,961	238,443	492,404
Add:				
Net income			61,058	61,058
Exercise of stock options and other issuance of Common Shares	111	589		589
Tax benefit from employee stock-based awards		533		533
Compensation on stock-based awards		1,508		1,508
Dividend equivalent rights on stock-based awards not paid in cash		197		197
Deduct:				
Repurchase of Common Shares	545	3,589	13,591	17,180
Dividends on Common Shares			32,111	32,111
Dividend equivalent rights on stock-based awards not paid in cash			197	197
<b>Balances at December 31, 2014</b>	38,287	\$ 253,199	\$ 253,602	\$ 506,801

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

**AMERICAN STATES WATER COMPANY**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)	For the years ended December 31,		
	2014	2013	2012
<b>Cash Flows From Operating Activities:</b>			
Net income	\$ 61,058	\$ 62,686	\$ 54,148
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	41,751	40,967	43,234
Net gain on sale of property	(55)	(2)	(68)
Provision for doubtful accounts	991	1,145	1,710
Deferred income taxes and investment tax credits	32,316	16,112	15,087
Stock-based compensation expense	2,222	2,009	1,931
Impairment and other charges	—	—	416
Other — net	55	(438)	(35)
Changes in assets and liabilities:			
Accounts receivable — customers	3,979	(5,306)	(1,773)
Unbilled revenue	(3,279)	(974)	3,233
Other accounts receivable	1,029	2,503	5,416
Receivables from the U.S. government	397	5,799	(5,321)
Materials and supplies	970	790	(2,278)
Prepayments and other current assets	(264)	1,910	(432)
Other assets (including other regulatory assets)	27,622	12,758	(8,430)
Costs and estimated earnings in excess of billings on uncompleted contracts	6,568	(15,192)	(3,075)
Accounts payable	(1,622)	1,815	4,300
Income taxes receivable/payable	(11,648)	7,329	4,169
Billings in excess of costs and estimated earnings on uncompleted contracts	4,884	(5,720)	(17,673)
Accrued pension and other post-retirement benefits	(2,356)	4,396	5,954
Other liabilities	(1,348)	3,124	981
Net cash provided	163,270	135,711	101,494
<b>Cash Flows From Investing Activities:</b>			
Capital expenditures	(72,553)	(97,379)	(68,104)
Other investments	(1,568)	(1,408)	—
Proceeds from sale of property	62	12	68
Net cash used	(74,059)	(98,775)	(68,036)
<b>Cash Flows From Financing Activities:</b>			
Proceeds from stock option exercises	589	2,111	13,295
Repurchase of Common Shares	(17,180)	—	—
Tax benefits from exercise of stock-based awards	533	1,026	890
Receipt of advances for and contributions in aid of construction	7,598	12,133	9,647
Refunds on advances for construction	(3,469)	(3,711)	(3,614)
Retirement or repayments of long-term debt	(21,287)	(3,474)	(8,303)
Proceeds from issuance of long-term debt, net of issuance costs	14,846	60	3,408
Net change in notes payable to banks	—	—	(2,000)
Dividends paid	(32,111)	(29,360)	(24,130)
Other	(968)	(981)	(480)
Net cash used	(51,449)	(22,196)	(11,287)
<b>Net increase in cash and cash equivalents</b>	37,762	14,740	22,171
Cash and cash equivalents, beginning of year	38,226	23,486	1,315
<b>Cash and cash equivalents, end of year</b>	\$ 75,988	\$ 38,226	\$ 23,486

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

**GOLDEN STATE WATER COMPANY**  
**BALANCE SHEETS**

(in thousands)	December 31,	
	2014	2013
<b>Assets</b>		
<b>Utility Plant, at cost</b>		
Water	\$ 1,363,074	\$ 1,307,509
Electric	81,636	79,360
Total	1,444,710	1,386,869
Less — accumulated depreciation	(494,000)	(466,329)
	950,710	920,540
Construction work in progress	48,170	56,754
Net utility plant	998,880	977,294
<b>Other Property and Investments</b>	15,395	13,653
	15,395	13,653
<b>Current Assets</b>		
Cash and cash equivalents	44,005	37,875
Accounts receivable-customers, less allowance for doubtful accounts	18,814	23,829
Unbilled revenue	17,733	18,552
Inter-company receivable	499	718
Other accounts receivable, less allowance for doubtful accounts	3,795	3,570
Income taxes receivable from Parent	29,580	9,704
Note receivable from Parent	—	500
Materials and supplies	2,791	1,859
Regulatory assets — current	12,379	27,676
Prepayments and other current assets	2,507	2,218
Deferred income taxes — current	6,500	8,573
Total current assets	138,603	135,074
<b>Regulatory and Other Assets</b>		
Regulatory assets	118,829	95,005
Other accounts receivable	—	913
Other	10,667	11,442
Total regulatory and other assets	129,496	107,360
<b>Total Assets</b>	\$ 1,282,374	\$ 1,233,381

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

**GOLDEN STATE WATER COMPANY  
BALANCE SHEETS**

(in thousands)	December 31,	
	2014	2013
<b>Capitalization and Liabilities</b>		
<b>Capitalization</b>		
Common shareholder's equity	\$ 435,190	\$ 437,613
Long-term debt	325,798	326,079
Total capitalization	760,988	763,692
<b>Current Liabilities</b>		
Long-term debt — current	292	6,298
Accounts payable	29,619	37,611
Accrued other taxes	8,442	9,299
Accrued employee expenses	9,591	9,536
Accrued interest	3,593	3,897
Unrealized loss on purchased power contracts	3,339	—
Other	18,659	12,880
Total current liabilities	73,535	79,521
<b>Other Credits</b>		
Advances for construction	68,328	69,332
Contributions in aid of construction — net	116,629	114,916
Deferred income taxes	192,787	158,994
Unamortized investment tax credits	1,699	1,790
Accrued pension and other post-retirement benefits	61,773	38,726
Other	6,635	6,410
Total other credits	447,851	390,168
<b>Commitments and Contingencies (Notes 13 and 14)</b>		
<b>Total Capitalization and Liabilities</b>	<b>\$ 1,282,374</b>	<b>\$ 1,233,381</b>

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

**GOLDEN STATE WATER COMPANY  
STATEMENTS OF CAPITALIZATION**

(in thousands, except share data)	December 31,	
	2014	2013
<b>Common Shareholder's Equity:</b>		
Common Shares, no par value, Outstanding: 146 shares in 2014 and 2013	\$ 235,607	\$ 233,721
Earnings reinvested in the business	199,583	203,892
	435,190	437,613
<b>Long-Term Debt</b>		
Notes/Debentures:		
6.87% notes due 2023	—	5,000
7.00% notes due 2023	—	10,000
6.81% notes due 2028	15,000	15,000
6.59% notes due 2029	40,000	40,000
7.875% notes due 2030	20,000	20,000
7.23% notes due 2031	50,000	50,000
6.00% notes due 2041	62,000	62,000
Private Placement Notes:		
3.45% notes due 2029	15,000	—
9.56% notes due 2031	28,000	28,000
5.87% notes due 2028	40,000	40,000
6.70% notes due 2019	40,000	40,000
Tax-Exempt Obligations:		
5.50% notes due 2026	7,730	7,730
Variable Rate Obligation due 2014	—	6,000
State Water Project due 2035	4,077	4,190
Other Debt Instruments:		
Variable rate obligation due 2018	125	161
American Recovery and Reinvestment Act Obligation due 2033	4,158	4,269
Capital lease obligations	—	27
	326,090	332,377
Less: Current maturities	(292)	(6,298)
	325,798	326,079
<b>Total Capitalization</b>	<b>\$ 760,988</b>	<b>\$ 763,692</b>

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

**GOLDEN STATE WATER COMPANY**  
**STATEMENTS OF INCOME**

(in thousands)	For the years ended December 31,		
	2014	2013	2012
<b>Operating Revenues</b>			
Water	\$ 326,672	\$ 320,131	\$ 305,898
Electric	34,387	38,409	37,033
Total operating revenues	361,059	358,540	342,931
<b>Operating Expenses</b>			
Water purchased	57,790	58,930	54,010
Power purchased for pumping	10,700	9,518	8,355
Groundwater production assessment	16,450	15,541	14,732
Power purchased for resale	9,649	13,392	12,120
Supply cost balancing accounts	6,346	214	11,709
Other operation	25,548	25,110	26,938
Administrative and general	65,814	64,645	60,139
Depreciation and amortization	39,854	38,952	40,197
Maintenance	13,945	15,823	14,356
Property and other taxes	15,221	14,072	13,835
Net gain on sale of property	—	—	(65)
Total operating expenses	261,317	256,197	256,326
<b>Operating Income</b>	99,742	102,343	86,605
<b>Other Income and Expenses</b>			
Interest expense	(21,524)	(22,287)	(22,609)
Interest income	894	615	1,293
Other, net	751	1,105	431
Total other income and expenses	(19,879)	(20,567)	(20,885)
<b>Income from operations before income tax expense</b>	79,863	81,776	65,720
Income tax expense	32,006	33,134	26,500
<b>Net Income</b>	\$ 47,857	\$ 48,642	\$ 39,220

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

**GOLDEN STATE WATER COMPANY  
STATEMENTS OF CHANGES IN  
COMMON SHAREHOLDER'S EQUITY**

(in thousands, except number of shares)	Common Shares		Earnings	Total
	Number of Shares	Amount	Reinvested in the Business	
<b>Balances at December 31, 2011</b>	146	\$ 228,936	\$ 155,870	\$ 384,806
Add:				
Net income			39,220	39,220
Tax benefit from employee stock-based awards		895		895
Compensation on stock based awards		1,536		1,536
Dividend equivalent rights on stock-based awards not paid in cash		113		113
Deduct:				
Dividends on Common Shares			10,200	10,200
Dividend equivalent rights on stock-based awards not paid in cash			113	113
	146	231,480	184,777	416,257
<b>Balances at December 31, 2012</b>				
Add:				
Net income			48,642	48,642
Tax benefit from employee stock-based awards		943		943
Compensation on stock based awards		1,171		1,171
Dividend equivalent rights on stock-based awards not paid in cash		127		127
Deduct:				
Dividends on Common Shares			29,400	29,400
Dividend equivalent rights on stock-based awards not paid in cash			127	127
	146	233,721	203,892	437,613
<b>Balances at December 31, 2013</b>				
Add:				
Net income			47,857	47,857
Tax benefit from employee stock-based awards		514		514
Compensation on stock based awards		1,206		1,206
Dividend equivalent rights on stock-based awards not paid in cash		166		166
Deduct:				
Dividends on Common Shares			52,000	52,000
Dividend equivalent rights on stock-based awards not paid in cash			166	166
	146	235,607	199,583	435,190
<b>Balances at December 31, 2014</b>	146	\$ 235,607	\$ 199,583	\$ 435,190

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

**GOLDEN STATE WATER COMPANY**  
**STATEMENTS OF CASH FLOWS**

(in thousands)	For the years ended December 31,		
	2014	2013	2012
<b>Cash Flows From Operating Activities:</b>			
Net income	\$ 47,857	\$ 48,642	\$ 39,220
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	40,532	39,829	42,046
Net gain on sale of property	—	—	(65)
Provision for doubtful accounts	1,054	1,056	1,668
Deferred income taxes and investment tax credits	34,352	16,051	14,713
Impairment and other charges	—	—	416
Stock-based compensation expense	1,748	1,647	1,667
Other — net	(12)	(333)	(107)
Changes in assets and liabilities:			
Accounts receivable — customers	3,979	(5,306)	(1,773)
Unbilled revenue	819	(2,405)	1,108
Other accounts receivable	670	3,251	1,717
Materials and supplies	(932)	385	(318)
Prepayments and other assets	(289)	1,944	(452)
Other assets (including other regulatory assets)	27,258	14,715	(8,347)
Accounts payable	(1,676)	2,916	(2,331)
Inter-company receivable/payable	219	1,790	277
Income taxes receivable/payable from/to Parent	(19,876)	6,738	3,472
Accrued pension and other post-retirement benefits	(2,356)	4,396	5,954
Other liabilities	(664)	2,854	1,035
Net cash provided	132,683	138,170	99,900
<b>Cash Flows From Investing Activities:</b>			
Capital expenditures	(70,888)	(96,705)	(66,831)
Note receivable from AWR parent	(8,300)	(18,236)	—
Receipt of payment of note receivable from AWR parent	8,800	17,736	—
Other investing activities	(1,568)	(1,408)	65
Net cash used	(71,956)	(98,613)	(66,766)
<b>Cash Flows From Financing Activities:</b>			
Proceeds from issuance of long-term debt, net of issuance costs	14,846	60	3,408
Tax benefits from exercise of stock-based awards	514	943	895
Receipt of advances for and contributions in aid of construction	7,598	12,133	9,647
Refunds on advances for construction	(3,469)	(3,711)	(3,614)
Retirement or repayments of long-term debt	(21,287)	(3,474)	(8,303)
Net change in inter-company borrowings	—	—	(2,000)
Dividends paid	(52,000)	(29,400)	(10,200)
Other	(799)	(811)	(389)
Net cash used	(54,597)	(24,260)	(10,556)
<b>Net increase in cash and cash equivalents</b>	6,130	15,297	22,578
Cash and cash equivalents, beginning of year	37,875	22,578	—
<b>Cash and cash equivalents, end of year</b>	\$ 44,005	\$ 37,875	\$ 22,578

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



**AMERICAN STATES WATER COMPANY AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1 — Summary of Significant Accounting Policies**

**Nature of Operations:** American States Water Company (“AWR”) is the parent company of Golden State Water Company (“GSWC”) and American States Utility Services, Inc. (“ASUS”) (and its subsidiaries, Fort Bliss Water Services Company (“FBWS”), Terrapin Utility Services, Inc. (“TUS”), Old Dominion Utility Services, Inc. (“ODUS”), Palmetto State Utility Services, Inc. (“PSUS”) and Old North Utility Services, Inc. (“ONUS”). AWR and its subsidiaries may be collectively referred to herein as “Registrant” or “the Company.” The subsidiaries of ASUS may be individually referred to herein as a “Military Utility Privatization Subsidiary” and collectively referred to herein as the “Military Utility Privatization Subsidiaries.”

GSWC is a public utility engaged principally in the purchase, production, distribution and sale of water in California serving approximately 258,000 customers. GSWC also distributes electricity in several San Bernardino County Mountain communities in California serving approximately 24,000 electric customers through its Bear Valley Electric Service (“BVES”) division. Although Registrant has a diversified base of residential, industrial and other customers, revenues derived from commercial and residential water customers accounted for approximately 90% of total water revenues in 2014, 2013 and 2012. The California Public Utilities Commission (“CPUC”) regulates GSWC’s water and electric business, in matters including properties, rates, services, facilities and other matters, and transactions by GSWC with its affiliates. AWR’s assets and operating income are primarily those of GSWC.

ASUS, through its wholly-owned subsidiaries, operates, maintains and performs construction activities (including renewal and replacement capital work) on water and/or wastewater systems at various United States military bases pursuant to 50-year firm fixed-price contracts. These contracts are subject to periodic price redeterminations and modifications for changes in circumstances and changes in laws and regulations.

There is no direct regulatory oversight by the CPUC over AWR or the operations, rates or services provided by ASUS or any of its wholly owned subsidiaries.

**Basis of Presentation:** The consolidated financial statements and notes thereto are being presented in a combined report being filed by two separate Registrants: AWR and GSWC. References in this report to “Registrant” are to AWR and GSWC, collectively, unless otherwise specified. Certain prior period amounts have been reclassified to conform to the 2014 financial statement presentation.

The consolidated financial statements of AWR include the accounts of AWR and its subsidiaries, all of which are wholly-owned. These financial statements are prepared in conformity with accounting principles generally accepted in the United States of America. Inter-company transactions and balances have been eliminated in the AWR consolidated financial statements.

On May 20, 2013, AWR’s Board of Directors approved a two-for-one stock split of the Company’s Common Shares. In September 2013, shareholders of record received one additional share for each AWR Common Share they owned. This two-for-one stock split was retroactively applied to the historical financial statements.

**Related Party Transactions:** GSWC and ASUS provide and receive various support services to and from their parent, AWR, and among themselves. GSWC also allocates certain corporate office administrative and general costs to its affiliate, ASUS, using allocation factors approved by the CPUC. During the years ended December 31, 2014, 2013 and 2012, GSWC allocated to ASUS approximately \$2.7 million, \$2.6 million and \$2.4 million, respectively, of corporate office administrative and general costs. In addition, AWR has a \$100.0 million syndicated credit facility. AWR borrows under this facility and provides funds to its subsidiaries, including GSWC, in support of their operations. The interest rate charged to GSWC and ASUS is sufficient to cover AWR’s interest cost under the credit facility. Amounts owed to GSWC by its parent, AWR, or for allocated expenses are included in inter-company receivables as of December 31, 2014 and 2013.

In May 2013, AWR issued an interest bearing promissory note (the “Note”) to GSWC for \$20.0 million which expires on May 23, 2018. Under the terms of the Note, AWR may borrow from GSWC amounts up to \$20.0 million for working capital purposes. As of December 31, 2014, there were no amounts outstanding under this Note.

AWR owns all of the outstanding Common Shares of GSWC and ASUS. ASUS owns all of the outstanding Common Stock of the Military Utility Privatization Subsidiaries.

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**Utility Accounting:** Registrant’s accounting policies conform to accounting principles generally accepted in the United States of America ("U.S. GAAP"), including the accounting principles for rate-regulated enterprises, which reflect the ratemaking policies of the CPUC and the Federal Energy Regulatory Commission. GSWC has 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 the guidance for accounting for the effects of certain types of regulation. This guidance sets forth the application of accounting principles generally accepted in the United States of America for those companies whose rates are established by or are subject to approval by an independent third-party regulator.

Under such accounting guidance, rate regulated entities 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 ratemaking process in a period different from the period in which they would have been reflected in income by an unregulated company. These regulatory assets and liabilities are then recognized in the income statement in the period in which the same amounts are reflected in the rates charged for service. The amounts included as regulatory assets and liabilities that will be collected over a period exceeding one year are classified as long-term assets and liabilities as of December 31, 2014 and 2013.

**Property and Depreciation:** GSWC capitalizes, as utility plant, the cost of construction and the cost of additions, betterments and replacements of retired units of property. Such cost includes labor, material and certain indirect charges. Water systems acquired are recorded at estimated original cost of utility plant when first devoted to utility service and the applicable accumulated depreciation is recorded to accumulated depreciation. The difference between the estimated original cost, less accumulated depreciation, and the purchase price, if recognized by the regulator, is recorded as an acquisition adjustment within utility plant.

Depreciation is computed on the straight-line, remaining-life basis, group method, based on depreciable plant in accordance with the applicable ratemaking process. GSWC's provision for depreciation expressed as a percentage of the aggregate depreciable asset balances was 3.2% for 2014, 3.4% for 2013 and 3.7% for 2012. Depreciation computed on GSWC’s transportation equipment is recorded in other operating expenses and totaled \$678,000, \$877,000 and \$1.8 million for the years ended December 31, 2014, 2013 and 2012, respectively. Expenditures for maintenance and repairs are expensed as incurred. Replaced or retired property costs, including cost of removal, are charged to the accumulated provision for depreciation. Property owned and depreciation recorded by ASUS and its subsidiaries are not material to Registrant’s financial statements.

Estimated useful lives of GSWC’s utility plant, as authorized by the CPUC, are as follows:

Source of water supply	30 years to 50 years
Pumping	25 years to 40 years
Water treatment	20 years to 35 years
Transmission and distribution	25 years to 55 years
Generation	40 years
Other plant	7 years to 40 years

**Asset Retirement Obligations:** GSWC has a legal obligation for the retirement of its wells, which by law need to be properly capped at the time of removal. As such, GSWC incurs asset retirement obligations. GSWC records the fair value of a liability for these asset retirement obligations in the period in which they are incurred. When the liability is initially recorded, GSWC 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, GSWC either settles the obligation for its recorded amount or incurs a gain or loss upon settlement. Retirement costs have historically been recovered through rates subsequent to the retirement costs being incurred. Accordingly, GSWC’s asset retirement obligations are reflected as a regulatory asset. GSWC also reflects the gain or loss at settlement as a regulatory asset or liability on the balance sheet.

With regards to removal costs associated with certain other long-lived assets, such as water mains, distribution and transmission assets, asset retirement obligations have not been recognized as GSWC believes that it will not be obligated to retire these assets. There are no CPUC rules or regulations that require GSWC to remove any of its other long-lived assets. In addition, GSWC’s water pipelines are not subject to regulation by any federal regulatory agency. GSWC has franchise agreements with various municipalities in order to use the public right of way for utility purposes (i.e., operate water distribution and transmission assets), and if certain events occur in the future, could be required to remove or relocate certain of its pipelines. However, it is not possible to estimate an asset retirement amount since the timing and the amount of assets that may be required to be removed, if any, is not known.

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Amounts recorded for asset retirement obligations 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. Estimating the fair value of the costs of removal were determined based on third party costs.

Impairment of Long-Lived Assets: Long-lived assets are reviewed for impairment annually or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be fully recoverable in accordance with accounting guidance for impairment or disposal of long-lived assets. Registrant would recognize an impairment loss on its regulated assets only if the carrying value amount of a long-lived asset is not recoverable from customer rates authorized by the CPUC. Impairment loss is measured as the excess of the carrying value over the amounts recovered in customer rates. During the year ended December 31, 2012, a \$416,000 impairment loss was recorded in operating expenses as a result of the disallowance of certain capital costs by the CPUC. For the years ended December 31, 2014 and 2013, no impairment loss was recorded.

Goodwill: At December 31, 2014 and 2013, AWR had approximately \$1.1 million of goodwill. The \$1.1 million goodwill arose from ASUS's acquisition of a subcontractor's business. In accordance with the accounting guidance for testing goodwill, AWR annually assesses qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. For 2014, AWR's assessment of qualitative factors did not indicate that an impairment had occurred for the goodwill amount of \$1.1 million at ASUS.

Cash and Cash Equivalents: Cash and cash equivalents include short-term cash investments with an original maturity of three months or less. At times, cash and cash equivalent balances may be in excess of federally insured limits. Cash and cash equivalents are held with financial institutions with high credit standings.

Accounts Receivable: Accounts receivable is reported on the balance sheet net of any allowance for doubtful accounts. The allowance for doubtful accounts is Registrant's best estimate of the amount of probable credit losses in Registrant's existing accounts receivable from its water and electric customers, and is determined based on historical write-off experience and the aging of account balances. Registrant reviews the allowance for doubtful accounts quarterly. Account balances are written off against the allowance when it is probable the receivable will not be recovered. When utility customers request extended payment terms, credit is extended based on regulatory guidelines, and collateral is not required. Other accounts receivable consist of amounts due from third parties (non-utility customers) for various reasons, including amounts due from contractors, amounts due under settlement agreements, and amounts due from the U.S. government or other third-party prime government contractors pursuant to contracts or modifications thereto or agreements to operate and maintain, and/or provide construction services for the water and/or wastewater systems at military bases. The allowance for these other accounts receivable is based on Registrant's evaluation of the receivable portfolio under current conditions and a review of specific problems and such other factors that, in Registrant's judgment, should be considered in estimating losses. Allowances for doubtful accounts are disclosed in Note 17.

Materials and Supplies: Materials and supplies are stated at the lower of cost or market. Cost is computed using average cost.

Interest: Interest incurred during the construction of capital assets has generally not been capitalized for financial reporting purposes as such policy is not followed in the ratemaking process. Interest expense is generally recovered through the regulatory process. However, the CPUC has authorized certain capital projects to be filed for revenue recovery with advice letters when those projects are completed. During the time that such projects are under development and construction, GSWC may accrue an allowance for funds used during construction ("AFUDC") on the incurred expenditures to offset the cost of financing project construction. For the years ended December 31, 2014, 2013 and 2012, GSWC recorded \$24,000, \$270,000 and \$299,000, respectively, of AFUDC related to these capital projects based on a weighted cost of capital of 8.64% as approved by the CPUC.

Water and Electric Operating Revenues: GSWC records water and electric utility operating revenues when the service is provided to customers. Revenues include amounts billed to customers on a cycle basis based on meter reading for services provided and unbilled revenues representing estimated amounts to be billed for usage from the last meter reading date to the end of the accounting period. The unbilled revenues are based on historic customer usage to estimate unbilled usage. Flat-rate customers are billed in advance at the beginning of the service period. Revenue from flat-rate customers is deferred and adjustments are calculated to determine the revenue related to the applicable period.

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Alternative-Revenue Programs: As authorized by the CPUC, GSWC records in revenues the difference between the adopted level of volumetric revenues as authorized by the CPUC for metered accounts (volumetric revenues) and the actual volumetric revenues recovered in customer rates. If this difference results in an under-collection of revenues, GSWC records the additional revenue only to the extent that they are expected to be collected within 24 months following the year in which they are recorded in accordance with the accounting guidance for alternative-revenue programs.

Contracted Services Revenues: Revenues from ASUS contract operations and maintenance agreements are recognized on a monthly basis when services have been rendered to the customers under such agreements. Revenues from firm, fixed-price construction contracts are recognized based on the percentage-of-completion and cost-plus methods of accounting. In accordance with GAAP, revenue recognition under these methods require ASUS to estimate the progress toward completion on a contract in terms of efforts (such as costs incurred) or, in the case of the percentage of completion method, in terms of results achieved (such as units constructed). These approaches are used because management considers them to be the best available measure of progress on these contracts. Revenues from cost-plus-profit contracts of ASUS are recognized on the basis of costs incurred during the period plus the profit earned, measured by the cost-to-cost method. Unbilled receivables from the U.S. government represent amounts to be billed for construction work completed and/or for services rendered pursuant to the 50-year contracts with the U.S government, which are not presently billable but which will be billed under the terms of those contracts.

Construction costs for ASUS include all direct material and labor costs charged by subcontractors and those indirect costs related to contract performance, such as indirect labor, supplies, and tools. The factors considered in including such costs in revenues and expenses are that ASUS and/or its subsidiaries: (i) are the primary obligor in these arrangements with the U.S. government and the third party prime contractors; (ii) have latitude in establishing pricing, and (iii) bear credit risk in the collection of receivables. Administrative and general costs are charged to expense as incurred. Precontract costs for ASUS, which consist of design and engineering labor costs, are deferred if they are probable of recovery and are expensed as incurred if they are not probable of recovery. Deferred precontract costs have been immaterial to date. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined.

Changes in job performance, job conditions, change orders and estimated profitability, including those arising from contract penalty provisions, and final contract settlements may result in revisions to costs and income for ASUS and are recognized in the period in which the revisions are determined.

The asset, "Costs and estimated earnings in excess of billings on uncompleted contracts," represents revenues recognized in excess of amounts billed. The liability, "Billings in excess of costs and estimated earnings on uncompleted contracts," represents billings in excess of revenues recognized. Amounts expected to be earned/collected in the next 12-months have been classified as current.

Debt Issuance Costs and Redemption Premiums: Original debt issuance costs are capitalized and amortized over the lives of the respective issues. Premiums paid on the early redemption of debt, which is reacquired through refunding, are deferred and amortized over the life of the debt issued to finance the refunding as Registrant normally receives recovery of these costs in rates.

Advances for Construction and Contributions in Aid of Construction: Advances for construction represent amounts advanced by developers for the cost to construct water system facilities in order to extend water service to their properties. Advances are generally refundable in equal annual installments, generally over 40 years. In certain instances, GSWC makes refunds on these advances over a specific period of time based on operating revenues related to the main or as new customers are connected to receive service from the main. Utility plant funded by advances and contributions is excluded from rate base. Generally, GSWC depreciates contributed property and amortizes contributions in aid of construction at the composite rate of the related property. Contributions in aid of construction are similar to advances, but require no refunding.

Fair Value of Financial Instruments: For cash and cash equivalents, accounts receivable, accounts payable and short-term debt, the carrying amount is assumed to approximate fair value due to the short-term nature of the amounts. The table below estimates the fair value of long-term debt issued by GSWC. Rates available to GSWC at December 31, 2014 and 2013 for debt with similar terms and remaining maturities were used to estimate fair value for long-term debt. Changes in the assumptions will produce differing results.

(dollars in thousands)	2014		2013	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term debt—GSWC	\$ 326,090	\$ 417,057	\$ 332,377	\$ 412,590

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The accounting guidance for fair value measurements applies to all financial assets and financial liabilities that are being measured and reported on a fair value basis. Under the accounting guidance, GSWC makes fair value measurements that are classified and disclosed in one of the following three categories:

*Level 1:* Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

*Level 2:* Quoted prices in markets that are not active, or inputs which are observable, either directly or indirectly, for substantially the full term of the asset or liability, or

*Level 3:* Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported by little or no market activity).

Publicly issued notes, private placement notes and other long-term debt are measured using current U.S. corporate bond yields for similar debt instruments and are classified as Level 2. The following tables set forth by level, within the fair value hierarchy, GSWC's long-term debt measured at fair value as of December 31, 2014:

(dollars in thousands)	Level 1	Level 2	Level 3	Total
Long-term debt—GSWC	—	\$ 417,057	—	\$ 417,057

**Stock Awards:** AWR has issued stock awards to its employees under the 2000 Stock Incentive Plan, or 2000 employee plan, and the 2008 Stock Incentive Plan, or 2008 employee plan, and to directors under the 2003 Non-Employee Directors Stock Plan, or 2003 directors plan, and the 2013 Non-Employee Directors Plan, or 2013 directors plan. Registrant applies the provisions in the accounting guidance for share-based payments in accounting for all of its stock-based awards. See Note 12 for further discussion.

**Sales and Use Taxes:** GSWC bills certain sales and use taxes levied by state or local governments to its customers. Included in these sales and use taxes are franchise fees, which GSWC pays to various municipalities (based on ordinances adopted by these municipalities) in order to use public right of way for utility purposes. GSWC bills these franchise fees to its customers based on a CPUC-authorized rate for each rate-making area as applicable. These franchise fees, which are required to be paid regardless of GSWC's ability to collect from the customer, are accounted for on a gross basis. GSWC's franchise fees billed to customers and recorded as operating revenue were approximately \$3.7 million, \$3.6 million and \$3.4 million for the years ended December 31, 2014, 2013 and 2012, respectively. When GSWC acts as an agent, and the tax is not required to be remitted if it is not collected from the customer, the taxes are accounted for on a net basis.

Depending on the state in which the operations are conducted, ASUS and its subsidiaries are also subject to certain state non-income tax assessments generally computed on a "gross receipts" or "gross revenues" basis. These non-income tax assessments are required to be paid regardless of whether the subsidiary is reimbursed by the U.S. government for these assessments under its 50-year contracts. The non-income tax assessments are accounted for on a gross basis and totaled \$490,000, \$864,000 and \$717,000 during the years ended December 31, 2014, 2013 and 2012, respectively.

**Recently Issued Accounting Pronouncements:** In May 2014, the Financial Accounting Standards Board ("FASB") issued updated accounting guidance on revenue recognition. The guidance will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. Under this guidance, an entity will recognize revenue when it transfers promised goods or services to customers in an amount that reflects what the entity expects in exchange for the goods or services. This guidance also requires more detailed disclosures to enable users of the financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016, and early application is not permitted. The guidance allows entities to select one or two methods of adoption, either the full retrospective approach, meaning the guidance would be applied to all periods presented, or modified retrospective approach, meaning the cumulative effect of applying the guidance would be recognized as an adjustment to opening retained earnings at January 1, 2017, along with providing certain additional disclosures. Registrant will adopt this guidance in the fiscal year beginning January 1, 2017. Management has not yet selected a transition method nor has determined the effect of the standard on the Company's ongoing financial reporting.

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**Note 2 — Regulatory Matters**

In accordance with accounting principles for rate-regulated enterprises, Registrant records regulatory assets, which represent probable future recovery of costs from customers through the ratemaking process, and regulatory liabilities, which represent probable future refunds that are to be credited to customers through the ratemaking process. At December 31, 2014, Registrant had approximately \$67.5 million of regulatory assets, net of regulatory liabilities, not accruing carrying costs. Of this amount, \$40.7 million relates to the underfunded positions of the pension and other post-retirement obligations, \$3.3 million relates to a memorandum account authorized by the CPUC to track unrealized gains and losses on GSWC's purchase power contracts over the life of the contract, and \$17.6 million relates to deferred income taxes representing accelerated tax benefits flowed through to customers, which will be included in rates concurrently with recognition of the associated future tax expense. The remainder relates to other items that do not provide for or incur carrying costs.

Regulatory assets are offset against regulatory liabilities within each rate-making area. Amounts expected to be collected or refunded in the next 12-months have been classified as current assets and current liabilities by rate-making area. As of December 31, 2014, GSWC has a total of \$125.7 million in net regulatory assets, of which \$5.5 million have been included in "Other Current Liabilities". Regulatory assets, less regulatory liabilities, included in the consolidated balance sheets are as follows:

(dollars in thousands)	December 31,	
	2014	2013
<b>GSWC</b>		
Water Revenue Adjustment Mechanism, net of Modified Cost Balancing Account	\$ 9,369	\$ 16,345
Base Revenue Requirement Adjustment Mechanism	7,761	8,725
Costs deferred for future recovery on Aerojet case	13,629	14,763
Pensions and other post-retirement obligations (Note 11)	43,426	20,241
Derivative unrealized loss (Note 4)	3,339	—
Flow-through taxes, net (Note 10)	17,612	16,189
Low income rate assistance balancing accounts	9,109	9,979
General rate case memorandum accounts	4,731	15,645
Other regulatory assets	17,487	25,086
Various refunds to customers	(759)	(4,292)
Total	\$ 125,704	\$ 122,681

**Alternative-Revenue Programs:**

Under the Water Revenue Adjustment Mechanism ("WRAM"), GSWC records the difference between the adopted level of volumetric revenues as authorized by the CPUC for metered accounts (adopted volumetric revenues) and the actual volumetric revenues recovered in customer rates. While the WRAM tracks volumetric-based revenues, the revenue requirements approved by the CPUC include service charges, flat rate charges, and other items that are not subject to the WRAM. The adopted volumetric revenues consider the seasonality of consumption of water based upon historical averages. The variance between adopted volumetric revenues and actual billed volumetric revenues for metered accounts is recorded as a component of revenue with an offsetting entry to an asset or liability balancing account (tracked individually for each rate making area). The variance amount may be positive or negative and represents amounts that will be billed or refunded to customers in the future. The WRAM only applies to customer classes with conservation rates in place. Currently, the majority of GSWC's water customers have conservation rate structures.

Under the Modified Cost Balancing Account ("MCBA"), GSWC tracks adopted expense levels for purchased water, purchased power and pump taxes, as established by the CPUC. Variances (which include the effects of changes in both rate and volume) between adopted and actual purchased water, purchased power, and pump tax expenses are recorded as a component of the MCBA to be recovered from or refunded to GSWC's customers at a later date. This is reflected with an offsetting entry to an asset or liability balancing account (tracked individually for each rate-making area). Unlike the WRAM, the MCBA applies to all customer classes.

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The recovery or refund of the WRAM is netted against the MCBA over- or under-collection for the corresponding rate-making area and is interest bearing at the current 90-day commercial paper rate. During the year ended December 31, 2014, surcharges of \$14.3 million were billed to customers to decrease previously incurred under-collections in the pre-2014 WRAM, net of MCBA accounts. During the year ended December 31, 2014, GSWC recorded an additional \$7.4 million under-collection in the WRAM account, net of the MCBA. As of December 31, 2014, GSWC has a net aggregated regulatory asset of \$9.4 million, which is comprised of a \$10.5 million under-collection in the WRAM accounts and \$1.1 million over-collection in the MCBA accounts.

As required by the accounting guidance for alternative revenue programs, GSWC is required to collect its WRAM, net of its MCBA, within 24 months following the year in which an under-collection is recorded. In April 2012, the CPUC issued a final decision which, among other things, sets the recovery period for under-collected balances that are up to 15% of adopted annual revenues at 18 months or less. For under-collected balances greater than 15%, the recovery period is 19 to 36 months. As of December 31, 2014, the recovery periods for the majority of GSWC's WRAM/MCBA balances were primarily within the 12 to 18 month period. In addition to adopting an amortization schedule, the final decision sets a cap on total net WRAM/MCBA surcharges in any given calendar year of 10% of the last authorized revenue requirement. This cap has not impacted any WRAM/MCBA recoveries to-date. Surcharges are currently in place to recover the WRAM/MCBA balances for 2013.

For BVES, the CPUC approved the Base Revenue Requirement Adjustment Mechanism ("BRRAM") which adjusts certain revenues to adopted levels. In November 2014, the CPUC issued a final decision on BVES's general rate case, setting rates and adopted revenues for years 2013 through 2016. As a result of this decision, GSWC filed with the CPUC for recovery of the 2013 BRRAM under-collection of \$2.3 million to be collected over 24 months.

**Costs Deferred for Future Recovery:**

The CPUC authorized a memorandum account to allow for the recovery of costs incurred by GSWC related to contamination lawsuits brought against Aerojet and the state of California. In July 2005, the CPUC authorized GSWC to recover approximately \$21.3 million of the Aerojet litigation memorandum account, through a rate surcharge, which will continue for no longer than 20 years. Beginning in October 2005, a surcharge went into effect to begin amortizing the memorandum account over a 20-year period.

Aerojet also agreed to reimburse GSWC \$17.5 million, plus interest accruing from January 1, 2004, for GSWC's past legal and expert costs, which is included in the Aerojet litigation memorandum account. The reimbursement of the \$17.5 million is contingent upon the issuance of land use approvals for development in a defined area within Aerojet property in Eastern Sacramento County and the receipt of certain fees in connection with such development. It is management's intention to offset any proceeds from the housing development by Aerojet in this area against the balance in this litigation memorandum account.

At this time, management believes the full balance of the Aerojet litigation memorandum account will be collected either from customers or Aerojet.

**Pensions and Other Postretirement Obligations:**

A regulatory asset has been recorded at December 31, 2014 and 2013 for the costs that would otherwise be charged to "other comprehensive income" within shareholders' equity for the underfunded status of Registrant's pension and other postretirement benefit plans because the cost of these plans has historically been recovered through rates. As discussed in Note 11, as of December 31, 2014, Registrant's underfunded position for these plans that have been recorded as a regulatory asset totaled \$40.7 million. Registrant expects this regulatory asset to be recovered through rates in future periods.

The May 2013 CPUC decision in the water general rate case authorized GSWC to continue using a two-way balancing account for its three water regions and the general office to track differences between the forecasted annual pension expenses adopted in rates and the actual annual expense to be recorded by GSWC in accordance with the accounting guidance for pension costs. In November 2014, as part of the BVES general rate case decision, the CPUC also authorized the use of a balancing account for the electric segment. The two-way balancing accounts are interest bearing at the current 90-day commercial paper rate. As of December 31, 2014, GSWC has a net \$2.7 million under-collection in the two-way pension balancing accounts, consisting of a \$2.8 million under-collection related to the general office and water regions, and a \$124,000 over-collection related to BVES. As authorized in the CPUC's final decision on the water rate case, GSWC implemented a twelve-month surcharge in 2013 to recover balances in the water two-way balancing account. Surcharges totaling \$748,000 and \$1.2 million were billed to customers during 2014 and 2013, respectively.

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**Low Income Balancing Accounts:**

This regulatory asset reflects primarily the costs of implementing and administering the California Alternate Rates for Water program in GSWC's water regions and the California Alternate Rate for Energy program in GSWC's BVES division. These programs mandated by the CPUC provide a discount of a fixed dollar amount which is intended to represent a 15% discount based on a typical customer bill for qualified low-income water customers and 20% for qualified low-income electric customers. GSWC accrues interest on its low income balancing accounts at the prevailing rate for 90-day commercial paper. As of December 31, 2014, there is an aggregate \$9.1 million under-collection in the low income balancing accounts. Surcharges have been implemented to recover the costs included in these balancing accounts.

**General Rate Case Memorandum Accounts:**

The balance in the general rate case memorandum accounts represents the revenue differences between interim rates and final rates authorized by the CPUC due to delays in receiving decisions on various general rate case applications. As of December 31, 2014, there is an aggregate \$4.7 million in the general rate case memorandum accounts, \$4.1 million of which relates to retroactive rate increases resulting from the 2010 water general rate case, and \$617,000 of which is for the general rate case approved by the CPUC in May 2013. Surcharges ranging from 12 to 24 months, with the majority being 12 months, were implemented during the third quarter of 2013 to recover the retroactive adopted revenues related to the May 2013 CPUC decision. Unrecovered amounts will be addressed in a future rate case or other filing.

**Other Regulatory Assets:**

Other regulatory assets represent costs incurred by GSWC for which it has received or expects to receive rate recovery in the future. In determining the probability of costs being recovered in future periods, GSWC considers regulatory rules and decisions, past practices, and other facts or circumstances that would indicate if recovery is probable. If the CPUC determines that a portion of GSWC's regulatory assets are no longer recoverable in customer rates, GSWC would need to determine if it has suffered an asset impairment that would require a write-down in the assets' valuation.

**Other Regulatory Matters:**

**Procurement Audits:**

In December 2011, the CPUC issued a final decision adopting a settlement between GSWC and the CPUC on its investigation of certain work orders and charges paid to a specific contractor used previously for numerous construction projects primarily in one of GSWC's three main geographic water regions. As part of the settlement reached with the CPUC on this matter, GSWC agreed to be subject to three separate independent audits of its procurement practices over a period of 10 years from the date the settlement was approved by the CPUC. The audits cover GSWC's procurement practices for contracts with other contractors from 1994 forward. The first audit started in 2014 and covers almost a 20-year period from January 1, 1994 through September 30, 2013.

In December 2014, the accounting firm engaged by the CPUC to conduct the first audit provided its draft report to GSWC for comments. The draft report provides details on the accounting firm's findings and corresponding recommendations. The report asserts that GSWC had not complied, in all material respects, with the CPUC's requirements and GSWC's procurement policies during the period from 1994 to 2006. Subsequent to 2006, except for certain instances of alleged noncompliance, GSWC was found to be in compliance, in all material respects, with the CPUC's requirements and GSWC's procurement policies. The findings and corresponding recommendations in the draft report focused on, among other things, inadequate documentation to support competitive bidding procedures, change orders, and sole source justifications.

In February 2015, management provided to the auditors its responses to the draft report and for each of the findings noted by the auditors. Among other things, GSWC informed the auditors of certain factual inaccuracies in their report, asserted that GSWC has complied, in all material respects, with the CPUC's requirements throughout the entire audit period and, has been in material compliance with its own procurement policies throughout the audit period. The auditors are finalizing their audit report in light of GSWC's comments. After the report is finalized, GSWC will meet with the CPUC to discuss what, if any, further action is required. If the CPUC determines that GSWC has violated the CPUC's or GSWC's procurement policies during the 20-year audit period, the CPUC may pursue disallowances and/or penalties from GSWC in the pending rate case proceeding or in a new proceeding. GSWC likely will be given an opportunity to defend itself against any such attempt by the CPUC to pursue disallowances and/or penalties. At this time management cannot predict the final outcome of this first audit and cannot determine a possible loss or range of loss, if any, associated with any disallowances and/or penalties that may be pursued by the CPUC against GSWC.



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*BVES General Rate Case:*

In February 2012, BVES filed its general rate case for new rates in years 2013 through 2016. On May 7, 2014, GSWC filed a settlement agreement with the CPUC covering all matters in the rate case which had been approved by all parties. On November 6, 2014, the CPUC issued its final decision, adopting the settlement agreement. The final decision, which was retroactive to January 1, 2013, did not have a significant impact on GSWC's financial statements.

*Renewables Portfolio Standard:*

In December 2011, a renewables portfolio standard ("RPS") law went into effect which changed, among other things, annual procurement targets to multi-year procurement targets. In December 2012, GSWC entered into a ten-year agreement with a third party to purchase renewable energy credits ("RECs") whereby GSWC agreed to purchase approximately 582,000 RECs over a 10 -year period which would be used towards meeting the CPUC's RPS procurement requirements. As of December 31, 2014, GSWC has purchased sufficient RECs to be in compliance for all periods through 2014. Accordingly, no provision for loss or potential penalties has been recorded in the financial statements as of December 31, 2014. GSWC intends to file its 2014 compliance report with the CPUC by the August 2015 deadline. The cost of these RECs has been included as part of the electric supply cost balancing account as of December 31, 2014.

*Cost of Capital Proceeding for Water Regions:*

In July 2012, the CPUC issued a final decision on GSWC's water cost of capital proceeding. The decision authorized, among other things, a return on equity ("ROE") of 9.99% and for GSWC to continue the Water Cost of Capital Mechanism ("WCCM"). The WCCM adjusts ROE and rate of return on rate base between the three-year cost of capital proceedings only if there is a positive or negative change of more than 100 basis points in the average of the Moody's Aa utility bond rate as measured over the period October 1 through September 30. If the average Moody's rate for this period changes by over 100 basis points from the benchmark, the ROE will be adjusted by one half of the difference. For the period October 1, 2011 through September 30, 2012, the Moody's rate declined by 112 basis points from the benchmark. As a result, in 2012 GSWC filed an advice letter to lower its water ROE by 56 basis points, from 9.99% to 9.43%, which was incorporated into 2013 water rates. For the period October 1, 2013 through September 30, 2014, the Moody's rate increased by 30 basis points from the benchmark. As a result, GSWC's current water ROE of 9.43% remained unchanged for 2014.

GSWC was scheduled to file its next cost of capital application in March 2015 based on an extension previously granted. However, in November 2014 GSWC, along with three other Class A California water companies ("Joint Parties"), filed with the CPUC a request for further extension of the date by which each of them is required to file its 2015 Cost of Capital Application. The Joint Parties requested approval to postpone this filing date one additional year until March 31, 2016, with a corresponding effective date of January 1, 2017 in compliance with the Rate Case Plan. The Joint Parties believe that postponing the filing one year will alleviate administrative processing costs on the four Class A utilities as well as Commission staff, and provide relief for both Commission and utility resources already strained by numerous proceedings. The Joint Parties also believe that the current economic environment is such that a change from the currently adopted return on equity would be small. The CPUC approved this request in January 2015. As a result of the approval, GSWC's current authorized cost of capital will continue in effect through December 2016, and GSWC will forgo a cost of capital adjustment in 2016 in the event that the WCCM mechanism is triggered.

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**Note 3 — Utility Plant and Intangible Assets**

The following table shows Registrant's utility plant by major asset class:

(dollars in thousands)	GSWC December 31,		AWR December 31,	
	2014	2013	2014	2013
<b><u>Water</u></b>				
Land	\$ 15,423	\$ 15,423	\$ 15,423	\$ 15,423
Intangible assets	34,063	34,001	34,081	34,019
Source of water supply	80,614	75,651	80,614	75,651
Pumping	155,802	147,390	155,802	147,390
Water treatment	71,519	70,947	71,519	70,947
Transmission and distribution	894,789	856,823	894,789	856,823
General	110,864	107,274	121,552	116,346
	1,363,074	1,307,509	1,373,780	1,316,599
<b><u>Electric</u></b>				
Transmission and distribution	60,035	58,400	60,035	58,400
Generation	12,547	12,547	12,547	12,547
General (1)	9,054	8,413	9,054	8,413
	81,636	79,360	81,636	79,360
Less — accumulated depreciation	(494,000)	(466,329)	(500,239)	(471,665)
Construction work in progress	48,170	56,754	48,343	57,183
Net utility plant	\$ 998,880	\$ 977,294	\$ 1,003,520	\$ 981,477

- (1) Includes intangible assets of \$1.2 million for the years ended December 31, 2014 and 2013 for studies performed in association with the electricity segment of the Registrant's operations.

As of December 31, 2014 and 2013, intangible assets consist of the following:

(dollars in thousands)	Weighted Average Amortization Period	GSWC December 31,		AWR December 31,	
		2014	2013	2014	2013
<b><u>Intangible assets:</u></b>					
Conservation	26 years	\$ 9,496	\$ 9,496	\$ 9,496	\$ 9,496
Water and service rights (2)	30 years	8,124	8,124	8,695	8,695
Water planning studies	13 years	17,277	17,214	17,277	17,214
Total intangible assets		34,897	34,834	35,468	35,405
Less — accumulated amortization		(24,373)	(22,459)	(24,456)	(22,530)
Intangible assets, net of amortization		\$ 10,524	\$ 12,375	\$ 11,012	\$ 12,875
Intangible assets not subject to amortization (3)		\$ 409	\$ 409	\$ 427	\$ 427

- (2) Includes intangible assets of \$571,000 for contracted services included in "Other Property and Investments" on the consolidated balance sheets as of December 31, 2014 and 2013.
- (3) The intangible assets not subject to amortization primarily consist of organization and consent fees.

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For the years ended December 31, 2014, 2013 and 2012, amortization of intangible assets was \$1.9 million, \$1.9 million and \$2.4 million, respectively, for AWR and GSWC. Estimated future consolidated amortization expenses related to intangible assets for the succeeding five years are (in thousands):

	Amortization Expense
2015	\$ 2,441
2016	1,605
2017	1,491
2018	1,491
2019	1,320
Total	\$ 8,348

There is no material difference between the consolidated operations of AWR and the operations of GSWC in regards to the future amortization expense of intangible assets.

**Asset Retirement Obligations:**

The following is a reconciliation of the beginning and ending aggregate carrying amount of asset retirement obligations, which are included in “Other Credits” on the balance sheets as of December 31, 2014 and 2013:

(dollars in thousands)	GSWC
Obligation at December 31, 2012	\$ 3,018
Additional liabilities incurred	11
Liabilities settled	(126)
Accretion	192
Obligation at December 31, 2013	\$ 3,095
Additional liabilities incurred	6
Liabilities settled	(66)
Accretion	199
Obligation at December 31, 2014	\$ 3,234

Registrant follows the accounting guidance for asset retirement obligations. Because retirement costs have historically been recovered through rates at the time of retirement, upon implementing this guidance, the cumulative effect of the adoption of the authoritative guidance was reflected as a regulatory asset.

**Note 4 — Derivative Instruments**

GSWC’s electric division, BVES, purchases power under long-term contracts at a fixed cost depending on the amount of power and the period during which the power is purchased under such contracts. These contracts are generally subject to the accounting guidance for derivatives and require mark-to-market derivative accounting. However, during 2014 GSWC’s power purchases were based on month-to-month arrangements, as the previous long-term contract had expired in 2013. In December 2014, the CPUC approved an application that allowed GSWC to immediately execute new long-term purchased power contracts with energy providers on December 9, 2014. GSWC began taking power under these long-term contracts effective January 1, 2015 at a fixed cost over three and five year terms depending on the amount of power and period during which the power is purchased under the contracts.

The new long-term contracts executed in December 2014 are subject to the accounting guidance for derivatives and require mark-to-market derivative accounting. Among other things, the CPUC approval in December 2014 also authorized GSWC to establish a regulatory asset and liability memorandum account to offset the mark-to-market entries required by the accounting guidance. Accordingly, all unrealized gains and losses generated from the new purchased power contracts executed in December 2014 will be deferred on a monthly basis into a non-interest bearing regulatory memorandum account that tracks the changes in fair value of the derivative throughout the term of the contract. As a result, these unrealized gains and losses will not impact GSWC’s earnings. As of December 31, 2014, there was a \$3.3 million unrealized loss in the memorandum account for the new purchased power contracts as a result of the recent drop in energy prices.

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As previously discussed in Note 1, the accounting guidance for fair value measurements establishes a framework for measuring fair value and requires fair value measurements to be classified and disclosed in one of three levels. Registrant's valuation model utilizes various inputs that include quoted market prices for energy over the duration of the contract. The market prices used to determine the fair value for this derivative instrument were estimated based on independent sources such as broker quotes and publications that are not observable in or corroborated by the market. Registrant received one broker quote to determine the fair value of its derivative instrument. When such inputs have a significant impact on the measurement of fair value, the instrument is categorized in Level 3. Accordingly, the valuation of the derivative on Registrant's purchased power contract has been classified as Level 3 for all periods presented.

The following table presents changes in the fair value of GSWC's derivatives for the years ended December 31, 2014 and 2013.

(dollars in thousands)	2014	2013
Balance, at beginning of the period	\$ —	\$ (3,060)
Unrealized gain (loss) on purchased power contracts	(3,339)	3,060
Balance, at end of the period	<u>\$ (3,339)</u>	<u>\$ —</u>

**Note 5 — Military Privatization**

Each Military Utility Privatization Subsidiary has entered into a service contract with the U.S. government to operate and maintain, as well as perform construction activities to renew and replace the water and/or wastewater systems at a military base or bases. The amounts charged by each Military Utility Privatization Subsidiary for these services are based upon the terms of the 50-year contract between the Military Utility Privatization Subsidiary and the U.S. government. Under the terms of each of these agreements, the Military Utility Privatization Subsidiaries agreed to operate and maintain the water and/or wastewater systems for: (i) a monthly net fixed-price for operation and maintenance, and (ii) an amount to cover renewals and replacements. Under the terms of each of these contracts, prices are to be redetermined at the end of the initial two year period and every three years thereafter. In addition, these contracts may also include firm, fixed-priced initial capital upgrade projects to upgrade the existing infrastructure.

Prices may be equitably adjusted for changes in law and other circumstances. These adjustments can be retrospective and/or prospective. The Military Utility Privatization Subsidiaries have experienced delays in obtaining price redeterminations as required by the terms of these contracts. Interim rate increases have, at times, been implemented pending the outcome of these price redeterminations. In addition, contract modifications may be issued for other necessary capital upgrades to the existing infrastructure approved by the U.S. government. Each of the contracts may be subject to termination, in whole or in part, prior to the end of the 50-year term for convenience of the U.S. government or as a result of default or nonperformance by the applicable Military Utility Privatization Subsidiary.

In September 2014, the U.S. government approved price redeterminations related to the operations at Fort Bragg, Fort Jackson and Andrews Air Force Base. ASUS received contract modifications from the U.S. government for these price redeterminations, which included retroactive operation and maintenance management fees and retroactive renewal and replacement fees for prior periods. Revenues from operation and maintenance management fees are recognized when services are rendered. Accordingly, ASUS recorded approximately \$1.7 million of retroactive revenues and pretax operating income related to periods prior to 2014 in connection with these contract modifications during the third quarter of 2014. In addition, approximately \$6.1 million related to renewal and replacement funds was also recorded in "billings in excess of costs and estimated earnings on uncompleted contracts", which will be recognized in construction revenues (along with the related construction costs) when the work is performed.

The receivable from the U.S. government represents amounts billed to the U.S. government that have not yet been collected. Unbilled receivables from the U.S. government represent amounts to be billed for construction work completed and/or for services rendered pursuant to the 50-year contracts with the U.S. government, which are not presently billable but which will be billed under the terms of those contracts.

The asset, "Costs and estimated earnings in excess of billings on uncompleted contracts," represents revenues recognized in excess of amounts billed. The liability, "Billings in excess of costs and estimated earnings on uncompleted contracts," represents billings in excess of revenues recognized for renewal and replacement work.

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Costs and estimated earnings on uncompleted contracts and amounts due from the U.S. government as of December 31, 2014 and 2013 are as follows:

<u>(dollars in thousands)</u>	<u>2014</u>	<u>2013</u>
Revenues (costs and estimated earnings) recognized on uncompleted contracts	\$ 91,141	\$ 78,741
Less: Billings to date on uncompleted contracts	(56,114)	(32,262)
	<u>\$ 35,027</u>	<u>\$ 46,479</u>
 <u>Included in the accompanying balance sheets under the following captions:</u>		
Costs and estimated earnings in excess of billings on uncompleted contracts	\$ 46,763	\$ 53,331
Billings in excess of costs and estimated earnings on uncompleted contracts	(11,736)	(6,852)
	<u>\$ 35,027</u>	<u>\$ 46,479</u>
 <u>Receivables from the U.S. government:</u>		
Billed receivables from the U.S. government	\$ 6,709	\$ 7,106
Unbilled receivables from the U.S. government (current)	3,689	—
Unbilled receivables from the U.S. government (non-current)	3,513	3,104
Less: allowance for doubtful accounts	—	—
Total	<u>\$ 13,911</u>	<u>\$ 10,210</u>

**Note 6 — Earnings Per Share and Capital Stock**

In accordance with the accounting guidance for participating securities and earnings per share (“EPS”), Registrant uses the “two-class” method of computing EPS. The “two-class” method is an earnings allocation formula that determines EPS for each class of common stock and participating security. AWR has participating securities related to restricted stock units that earn dividend equivalents on an equal basis with AWR’s Common Shares that have been issued under AWR’s 2000 and 2008 employee plans and the 2003 and 2013 directors plans. In applying the “two-class” method, undistributed earnings are allocated to both common shares and participating securities.

The following is a reconciliation of Registrant’s net income and weighted average Common Shares outstanding for calculating basic net income per share reflecting the two-for-one stock split effective September 3, 2013:

<u>Basic</u> <u>(in thousands, except per share amounts)</u>	<u>For The Years Ended December 31,</u>		
	<u>2014</u>	<u>2013</u>	<u>2012</u>
Net income	\$ 61,058	\$ 62,686	\$ 54,148
Less: (a) Distributed earnings to common shareholders	32,125	29,366	24,129
Distributed earnings to participating securities	177	171	171
Undistributed earnings	<u>28,756</u>	<u>33,149</u>	<u>29,848</u>
(b) Undistributed earnings allocated to common shareholders	28,599	32,958	29,638
Undistributed earnings allocated to participating securities	157	191	210
Total income available to common shareholders, basic (a)+(b)	<u>\$ 60,724</u>	<u>\$ 62,324</u>	<u>\$ 53,767</u>
Weighted average Common Shares outstanding, basic	<u>38,658</u>	<u>38,639</u>	<u>37,998</u>
<b>Basic earnings per Common Share:</b>	<u>\$ 1.57</u>	<u>\$ 1.61</u>	<u>\$ 1.42</u>

Diluted EPS is based upon the weighted average number of Common Shares, including both outstanding shares and shares potentially issuable in connection with stock options and restricted stock units granted under AWR’s 2000 and 2008 employee plans, and the 2003 and 2013 directors plans, and net income. At December 31, 2014, there were 222,580 stock options outstanding under these Plans. At December 31, 2014, there were also 221,302 restricted stock units outstanding including performance shares awarded to officers of the Registrant.

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The following is a reconciliation of Registrant's net income and weighted average Common Shares outstanding for calculating diluted net income per share reflecting the two-for-one stock split effective September 3, 2013:

<u>Diluted</u> (in thousands, except per share amounts)	For The Years Ended December 31,		
	2014	2013	2012
Common shareholders earnings, basic	\$ 60,724	\$ 62,324	\$ 53,767
Undistributed earnings for dilutive stock options and restricted stock units	157	191	210
Total common shareholders earnings, diluted	<u>\$ 60,881</u>	<u>\$ 62,515</u>	<u>\$ 53,977</u>
Weighted average Common Shares outstanding, basic	38,658	38,639	37,998
Stock-based compensation (1)	222	230	264
Weighted average Common Shares outstanding, diluted	<u>38,880</u>	<u>38,869</u>	<u>38,262</u>
Diluted earnings per Common Share	<u>\$ 1.57</u>	<u>\$ 1.61</u>	<u>\$ 1.41</u>

- (1) In applying the treasury stock method of reflecting the dilutive effect of outstanding stock-based compensation in the calculation of diluted EPS, 222,580 stock options and 221,302 restricted stock units, including performance awards, at December 31, 2014 were deemed to be outstanding in accordance with accounting guidance on earnings per share.

During the years ended December 31, 2014, 2013 and 2012, AWR issued Common Shares totaling 74,145, 114,821 and 77,038, respectively, under AWR's Common Share Purchase and Dividend Reinvestment Plan ("DRP"), the 2000 and 2008 employee plans and the 2003 and 2013 directors plans. As of December 31, 2014, there are 1,055,948 and 387,300 Common Shares authorized for issuance directly by AWR but unissued under the DRP and the 401(k) Plan, respectively. Shares reserved for the 401(k) Plan are in relation to AWR's matching contributions and investment by participants. In addition, during the years ended December 31, 2014, 2013 and 2012, AWR issued 37,006, 131,448 and 819,400 Common Shares for approximately \$589,000, \$2,111,000 and \$13,295,000, respectively, as a result of the exercise of stock options. During 2014, 2013 and 2012, no cash proceeds received by AWR as a result of the exercise of stock options were distributed to any subsidiaries of AWR.

On March 27, 2014, AWR's Board of Directors approved a stock repurchase program, authorizing AWR to repurchase up to 1.25 million shares of its Common Shares from time to time through June 30, 2016. Pursuant to this program, Registrant repurchased 545,218 Common Shares on the open market during the year ended December 31, 2014. The repurchase of Common Shares is restricted by California law under the same standards which apply to dividend distributions. See Note 7 (Dividend Limitations) of *Notes to Consolidated Financial Statements*.

In August 2012, AWR filed a Registration Statement with the Securities and Exchange Commission ("SEC") for the sale from time to time of debt and equity securities. As of December 31, 2014, \$115 million was available for issuance of additional securities under this registration statement. This Registration Statement expires in August 2015.

GSWC's outstanding Common Shares are owned entirely by its parent, AWR. To the extent GSWC does not reimburse AWR for stock-based compensation awarded under various stock compensation plans, such amounts increase the value of GSWC's common shareholder's equity.

**Note 7 — Dividend Limitations**

GSWC is subject to contractual restrictions on its ability to pay dividends. GSWC's maximum ability to pay dividends is restricted by certain Note Agreements to the sum of \$21.0 million plus 100% of consolidated net income from various dates plus the aggregate net cash proceeds received from capital stock offerings or other instruments convertible into capital stock from various dates. Under the most restrictive of the Note Agreements, \$367.7 million was available to pay dividends to AWR as of December 31, 2014. GSWC is also prohibited from paying dividends if, after giving effect to the dividend, its total indebtedness to capitalization ratio (as defined) would be more than 0.6667 to 1. Dividends in the amount of \$52.0 million, \$29.4 million and \$10.2 million were paid to AWR by GSWC during the years ended December 31, 2014, 2013 and 2012, respectively. ASUS paid a dividend of \$6.7 million to AWR in 2012.

The ability of AWR, ASUS and GSWC to pay dividends is also restricted by California law. Effective January 1, 2012, California revised the legal standards applicable to a California corporation seeking to distribute dividends. Under the

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revised law, AWR, GSWC and ASUS are each permitted to distribute dividends to its shareholders so long as the Board of Directors determines, in good faith, that either: (i) the value of the corporation's assets equals or exceeds the sum of its total liabilities immediately after the dividend, or (ii) its retained earnings equals or exceeds the amount of the distribution. Under the least restrictive of the California tests, approximately \$253.6 million was available to pay dividends to AWR's shareholders at December 31, 2014. Approximately \$199.6 million was available for GSWC to pay dividends to AWR at December 31, 2014. Approximately \$41.3 million was available for ASUS to pay dividends to AWR at December 31, 2014.

**Note 8 — Bank Debt**

AWR has access to a syndicated credit facility which was amended on May 23, 2013 to, among other things, extend the expiration date of the syndicated credit facility to May 23, 2018, reduce the amount of interest and fees paid by AWR, and update certain representations and covenants in the credit agreement. AWR may, under the terms of the fourth amendment, elect to increase the aggregate commitment by up to an additional \$50.0 million. The aggregate effective amount that may be outstanding under letters of credit is \$25.0 million. AWR has obtained letters of credit, primarily for GSWC, in the aggregate amount of \$11.2 million, with fees of 0.65% including: (i) a \$6.7 million letter of credit representing a percentage of the outstanding American Recovery and Reinvestment Act ("ARRA") funds received by GSWC for reimbursement of capital costs related to the installation of meters in GSWC's Arden-Cordova water system; (ii) letters of credit in an aggregate amount of \$340,000 as security for GSWC's business automobile insurance policy; (iii) a letter of credit, in an amount of \$585,000 as security for the purchase of power; (iv) a \$15,000 irrevocable letter of credit pursuant to a franchise agreement with the City of Rancho Cordova, and (v) an irrevocable letter of credit in the amount of \$3.6 million, pursuant to a settlement agreement with Southern California Edison Company to cover GSWC's commitment to pay the settlement amount. Letters of credit outstanding reduce the amount that may be borrowed under the revolving credit facility. There were no compensating balances required.

Loans can be obtained at the option of AWR and bear interest at rates based on credit ratings and Euro rate margins. In July 2014, Standard & Poor's Ratings Services ("S&P") revised its rating outlook on AWR and GSWC from stable to positive. S&P also affirmed the 'A+' corporate credit rating on both AWR and GSWC. S&P debt ratings range from AAA (highest rating possible) to D (obligation is in default). In December 2014, Moody's Investors Service ("Moody's") affirmed its 'A2' rating with a stable outlook for GSWC.

At December 31, 2014, there were no borrowings outstanding under this facility. At times, AWR borrows under this facility and provides loans to its subsidiaries in support of their operations, on terms that are similar to that of the credit facility.

AWR's short-term borrowing activities (excluding letters of credit) for the last three years were as follows:

(in thousands, except percent)	December 31,		
	2014	2013	2012
Balance Outstanding at December 31,	\$ —	\$ —	\$ —
Interest Rate at December 31,	0.82%	0.82%	1.41%
Average Amount Outstanding	\$ 6,181	\$ —	\$ 885
Weighted Average Annual Interest Rate	0.81%	1.02%	1.49%
Maximum Amount Outstanding	\$ 24,000	\$ —	\$ 6,000

All of the letters of credit are issued pursuant to the syndicated revolving credit facility. The syndicated revolving credit facility contains restrictions on prepayments, disposition 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 Moody's Investor Service or S&P debt rating of Baa3 or BBB-, respectively. As of December 31, 2014, 2013 and 2012, AWR was in compliance with these requirements. As of December 31, 2014, AWR had an interest coverage ratio of 7.52 times interest expense, a debt ratio of 0.40 to 1.00 and a debt rating of A+ by S&P.

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**Note 9 — Long-Term Debt**

Registrant's long-term debt consists primarily of Notes and Debentures of GSWC. Registrant summarizes its long-term debt in the Statements of Capitalization. GSWC does not currently have any outstanding mortgages or other encumbrances on its properties. GSWC's leases and other similar financial arrangements are not material.

As of December 31, 2014, GSWC had \$100.0 million available for issuance of debt securities under a Registration Statement filed with the SEC. This Registration Statement expires in August 2015.

Private placement notes issued by GSWC in the amount of \$28 million contain restrictions on the payment of dividends, minimum interest coverage requirements, a maximum debt to capitalization ratio and a negative pledge. Pursuant to the terms of these agreements, GSWC must maintain a minimum interest coverage ratio of two times interest expense. As of December 31, 2014, GSWC had an interest coverage ratio of over four times interest expense.

On July 15, 2014, GSWC redeemed its \$5,000,000, 6.87% Medium-Term Notes Series A due 2023, and \$10,000,000, 7.00% Medium-Term Notes Series A, also due 2023. The notes were redeemed at a price of 100% of the outstanding principal amount of the notes, plus interest. In December 2014, GSWC replaced these notes with lower interest rate debt and issued \$15,000,000 in 3.45% Senior Notes due December 23, 2029. Pursuant to the terms of these notes, GSWC must maintain a total indebtedness to capitalization ratio (as defined) of less than 0.6667 to 1 and a total indebtedness to earnings before income taxes, depreciation and amortization (EBITDA) of less than 8 to 1. As of December 31, 2014, GSWC had a total indebtedness to capitalization ratio of 0.4367 to 1 and a total indebtedness to EBITDA of 2.4 to 1.

Certain long-term debt issues outstanding as of December 31, 2014 can be redeemed, in whole or in part, at the option of GSWC subject to redemption schedules embedded in the agreements particular to each redeemable issue. With the exception of the 9.56% Notes and Senior Notes issued to Co-Bank, the redemption premiums in effect for 2014 range up to 0.383% of par value. The 9.56% Notes are subject to a make-whole premium based on 55 basis points above the applicable Treasury Yield if redeemed prior to 2021. After 2021, the maximum redemption premium is 3% of par value. The Senior Notes with Co-Bank are subject to a make-whole premium based on the difference between Co-Bank's cost of funds on the date of purchase and Co-Bank's cost of funds on the date of redemption, plus 0.5%. The \$15,000,000, 3.45% Senior Notes due December 23, 2029 have similar redemption premiums.

In October 2009, GSWC entered into an agreement with the California Department of Health ("CDPH") whereby CDPH agreed to provide funds to GSWC of up to \$9.0 million under the American Recovery and Reinvestment Act. Proceeds from the funds received were used to reimburse GSWC for capital costs incurred to install water meters to convert customers in GSWC's Arden-Cordova district from non-metered service to metered service. GSWC received a total of \$8.6 million in reimbursements from the CDPH, half of which was recorded as a contribution in aid of construction and the other half as long-term debt in accordance with the terms of the agreement. The loan portion bears interest at a rate of 2.5% and is payable over 20 years beginning in 2013. A surcharge to recover from customers the debt service cost on this loan was approved by the CPUC and implemented in 2013. Pursuant to the agreement, GSWC also issued letters of credit to CDPH equal to 80% of the amount loaned to GSWC. As of December 31, 2014, GSWC has a total of \$6.7 million in letters of credit issued to CDPH.

Annual maturities of all long-term debt, including capitalized leases, are as follows for each fiscal year through December 31, 2019 and thereafter (in thousands):

	<b>Maturity as of December 31,</b>
2015	\$ 292
2016	311
2017	328
2018	322
2019	40,319
Thereafter	284,518
Total	<u>\$ 326,090</u>



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**Note 10 — Taxes on Income**

Registrant provides deferred income taxes for temporary differences under the accounting guidance for income taxes for certain transactions which are recognized for income tax purposes in a period different from that in which they are reported in the financial statements. The most significant items are the tax effects of differences in asset basis (including accelerated depreciation and capitalization methods), certain regulatory balancing accounts and advances for, and contributions in aid of construction. The accounting guidance for income taxes also requires that rate-regulated enterprises record deferred income taxes for temporary differences given flow-through treatment at the direction of a regulatory commission. The resulting deferred tax assets and liabilities are recorded at the expected cash flow to be reflected in future rates. Given that the CPUC has consistently permitted the recovery of flowed-through tax effects, GSWC has established regulatory liabilities and assets offsetting such deferred tax assets and liabilities (Note 2). Deferred investment tax credits (“ITC”) are amortized ratably to deferred tax expense over the lives of the property giving rise to the credits.

GSWC is included in AWR’s consolidated federal income tax and combined California state franchise tax returns. California unitary apportionment provides a benefit or detriment to AWR’s state taxes, depending on a combination of the profitability of AWR’s non-California activities as well as the proportion of its California sales to total sales. Consistent with the method adopted for regulatory purposes, GSWC’s tax expense is computed as if GSWC were autonomous and files separate returns. Given that all of GSWC’s activities are conducted within California, GSWC’s state tax expense does not reflect apportionment of its income.

As a regulated utility, GSWC treats certain temporary differences as flow-through adjustments in computing its income tax provision consistent with the income tax approach approved by the CPUC for ratemaking purposes. Flow-through adjustments increase or decrease tax expense in one period, with an offsetting decrease or increase occurring in another period. Giving effect to these temporary differences as flow-through adjustments typically results in a greater variance between the effective tax rate (“ETR”) and the statutory federal income tax rate in any given period than would otherwise exist if GSWC were not required to account for its income taxes as a regulated enterprise. The GSWC ETRs deviate from the statutory rate primarily due to state taxes and differences between book and taxable income that are treated as flow-through adjustments in accordance with regulatory requirements (principally plant-, rate-case- and compensation-related items). The ETR at the AWR consolidated level also fluctuates as a result of ASUS’s state income taxes, which vary among the jurisdictions in which it operates, and certain permanent differences.

**Changes in Tax Law**

During the fourth quarter of 2014, the Company reflected a change in its tax method of accounting for certain repair and maintenance expenditures pursuant to regulations issued by the U.S. Treasury Department in September 2013. The Company will file an application for an automatic change in tax accounting method with the Internal Revenue Service (“IRS”) for the 2014 tax year to implement the new method effective January 1, 2014. The tax accounting method change will also include a cumulative adjustment for 2013 and prior years, and will permit the expensing of certain utility asset replacement costs that were previously being capitalized and depreciated for book and tax purposes. As a result of the change, the Company will deduct a significant amount of linear asset costs, which consist primarily of water mains and connections.

During the fourth quarter of 2014, the Company completed its analysis of the cumulative adjustment for 2013 and prior years, and recorded a deferred income tax liability of \$22.5 million for federal and state repair-and-maintenance deductions of \$47 million and \$107 million, respectively. In addition, the 2014 deduction for both federal and state purposes was \$20.3 million, creating an \$8.3 million deferred income tax liability. Although this change reduced AWR’s current taxes payable, it did not reduce its total 2014 income tax expense or ETR. Furthermore, as a result of the repair-and-maintenance deductions, AWR and GSWC generated state net operating losses (“NOLs”) and, as of December 31, 2014, such NOL carryforwards total \$3.6 million and \$9.3 million, respectively, which will expire in 2034. The Company believes that it is more likely than not that the benefit from the state income tax NOL carryforwards will be realized and therefore requires no valuation allowance.

In December 2014, the Tax Increase Prevention Act of 2014 extended 50% bonus depreciation for qualifying property through 2014. Although this change in law reduced AWR’s current taxes payable, it did not reduce its total income tax expense or ETR.

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The significant components of the deferred tax assets and liabilities as reflected in the balance sheets at December 31, 2014 and 2013 are:

(dollars in thousands)	AWR		GSWC	
	December 31,		December 31,	
	2014	2013	2014	2013
<b>Deferred tax assets:</b>				
Regulatory-liability-related: ITC	\$ 1,001	\$ 1,049	\$ 1,001	\$ 1,049
Regulatory-liability-related: California Corp Franchise Tax	4,328	4,337	4,328	4,337
Other non-property-related	2,395	4,125	2,136	3,292
Contributions and advances	8,335	8,655	8,335	8,655
	\$ 16,059	\$ 18,166	\$ 15,800	\$ 17,333
<b>Deferred tax liabilities:</b>				
Fixed assets	\$ (163,232)	\$ (131,534)	\$ (164,724)	\$ (131,548)
Regulatory-asset-related: depreciation and other	(22,941)	(21,575)	(22,941)	(21,575)
California Corp Franchise Tax	(4,069)	(2,120)	(4,831)	(1,749)
Other property-related	(59)	(155)	(59)	(155)
Balancing and memorandum accounts	(4,071)	(6,663)	(4,071)	(6,663)
Deferred charges	(5,461)	(6,064)	(5,461)	(6,064)
	(199,833)	(168,111)	(202,087)	(167,754)
Accumulated deferred income taxes - net	\$ (183,774)	\$ (149,945)	\$ (186,287)	\$ (150,421)

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

(dollars in thousands)	AWR		
	Year Ended December 31,		
	2014	2013	2012
<b>Current</b>			
Federal	\$ 5,595	\$ 13,741	\$ 15,585
State	137	5,930	5,273
Total current tax expense	\$ 5,732	\$ 19,671	\$ 20,858
<b>Deferred</b>			
Federal	\$ 24,815	\$ 14,769	\$ 13,088
State	7,501	1,343	1,999
Total deferred tax expense	32,316	16,112	15,087
Total income tax expense	\$ 38,048	\$ 35,783	\$ 35,945
<b>GSWC</b>			
(dollars in thousands)	Year Ended December 31,		
	2014	2013	2012
	<b>Current</b>		
Federal	\$ 408	\$ 10,768	\$ 7,957
State	(2,754)	6,315	3,830
Total current tax expense	\$ (2,346)	\$ 17,083	\$ 11,787
<b>Deferred</b>			
Federal	\$ 24,373	\$ 14,691	\$ 12,670
State	9,979	1,360	2,043
Total deferred tax expense	34,352	16,051	14,713
Total income tax expense	\$ 32,006	\$ 33,134	\$ 26,500

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The reconciliations of the effective tax rates to the federal statutory rate are as follows:

(dollars in thousands, except percent)	AWR		
	Year Ended December 31,		
	2014	2013	2012
Federal taxes on pretax income at statutory rate	\$ 34,687	\$ 34,464	\$ 31,533
Increase (decrease) in taxes resulting from:			
State income tax, net of federal benefit	4,781	5,111	4,957
Flow-through on fixed assets	651	646	636
Flow-through on pension costs	(507)	612	10
Flow-through on removal costs	(1,571)	(2,141)	(943)
Domestic production activities deduction	(643)	(2,944)	(553)
Investment tax credit	(91)	(91)	(91)
Other – net	741	126	396
Total income tax expense from operations	<u>\$ 38,048</u>	<u>\$ 35,783</u>	<u>\$ 35,945</u>
Pretax income from operations	<u>\$ 99,106</u>	<u>\$ 98,469</u>	<u>\$ 90,093</u>
Effective income tax rate	<u>38.4%</u>	<u>36.3%</u>	<u>39.9%</u>
(dollars in thousands, except percent)	GSWC		
	Year Ended December 31,		
	2014	2013	2012
Federal taxes on pretax income at statutory rate	\$ 27,952	\$ 28,622	\$ 23,002
Increase (decrease) in taxes resulting from:			
State income tax, net of federal benefit	4,693	5,372	4,048
Flow-through on fixed assets	651	646	636
Flow-through on pension costs	(507)	612	10
Flow-through on removal costs	(1,571)	(2,141)	(943)
Domestic production activities deduction	(55)	(1,316)	(553)
Investment tax credit	(91)	(91)	(91)
Other – net	934	1,430	391
Total income tax expense from operations	<u>\$ 32,006</u>	<u>\$ 33,134</u>	<u>\$ 26,500</u>
Pretax income from operations	<u>\$ 79,863</u>	<u>\$ 81,776</u>	<u>\$ 65,720</u>
Effective income tax rate	<u>40.1%</u>	<u>40.5%</u>	<u>40.3%</u>

AWR and GSWC had no unrecognized tax benefits at December 31, 2014, 2013 and 2012. Registrant’s policy is to classify interest on income tax over/underpayments in interest income/expense and penalties in “other operating expenses.”

At December 31, 2014, AWR and GSWC included \$504,000 and \$472,000, respectively, of net interest receivables from taxing authorities in other current and noncurrent assets. AWR and GSWC recognized \$19,000 and \$14,000, respectively, of interest income from taxing authorities during the year ended December 31, 2014. At December 31, 2013, AWR and GSWC included \$757,000 and \$704,000, respectively, of net interest receivables from taxing authorities in other current and noncurrent assets. AWR and GSWC recognized \$99,000 and \$21,000 respectively, of interest income from taxing authorities during the year ended December 31, 2013. At December 31, 2012, AWR and GSWC included \$2,838,000 and \$2,775,000, respectively, of net interest receivables from taxing authorities in other current and noncurrent assets. AWR and GSWC recognized \$473,000 and \$461,000, respectively, of interest income from taxing authorities during the year ended December 31, 2012.

At December 31, 2014, 2013 and 2012, Registrant had no significant accruals for income-tax-related penalties and did not recognize any significant income-tax-related penalties during the years ended December 31, 2014, 2013 and 2012.

Registrant files federal and various state income tax returns. During 2014, the Internal Revenue Service (“IRS”) completed its examination of 2007 and 2008 refund claims and issued refunds for both. AWR’s federal 2010 refund claim came under exam in 2014, and its 2011-2013 tax years remain subject to examination by the IRS. AWR has filed protective refund claims with the applicable state taxing authority for the 2002 through 2008 tax years in connection with the matters on the federal claims for these years and other state tax matters. During 2012, the California Franchise Tax Board commenced examining these claims. The 2009-2013 tax years remain subject to examination by state taxing authorities.

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**Note 11 — Employee Benefit Plans**

**Pension and Post-Retirement Medical Plans:**

Registrant maintains a defined benefit pension plan (the “Pension Plan”) that provides eligible employees (those aged 21 and older, hired before January 1, 2011) monthly benefits upon retirement based on average salaries and length of service. The eligibility requirement to begin receiving these benefits is 5 years of vested service. The normal retirement benefit is equal to 2% of the five highest consecutive years’ average earnings multiplied by the number of years of credited service, up to a maximum of 40, reduced by a percentage of primary social security benefits. There is also an early retirement option. Annual contributions are made to the Pension Plan, which comply with the funding requirements of the Employee Retirement Income Security Act (“ERISA”). At December 31, 2014, Registrant had 977 participants in the Pension Plan.

In January 2011, the Board of Directors approved an amendment to the Pension Plan, closing the plan to new employees hired after December 31, 2010. Employees hired or rehired after December 31, 2010 are eligible to participate in a defined contribution plan. Registrant's existing 401(k) Investment Incentive Program was amended to include this defined contribution plan. Under this plan, Registrant provides a contribution of 5.25% of eligible pay each pay period into investment vehicles offered by the plan’s trustee. Participants will be fully vested in this plan once the employee attains three years of service. Employees hired before January 1, 2011 continue to participate in and accrue benefits under the terms of the defined benefit plan.

Registrant also provides post-retirement medical benefits for all active employees hired before February of 1995, through a medical insurance plan. Eligible employees, who retire prior to age 65, and/or their spouses, are able to retain the benefits under the plan for active employees until reaching age 65. Eligible employees upon reaching age 65, and those eligible employees retiring at or after age 65, and/or their spouses, receive coverage through a Medicare supplement insurance policy paid for by Registrant subject to an annual cap limit. Registrant’s post-retirement medical plan does not provide prescription drug benefits to Medicare-eligible employees and is not affected by the Medicare Prescription Drug Improvement and Modernization Act of 2003.

In accordance with the accounting guidance for the effects of certain types of regulation, Registrant has established a regulatory asset for its underfunded position in its pension and post-retirement medical plans that is expected to be recovered through rates in future periods. The changes in actuarial gains and losses, prior service costs and transition assets or obligations pertaining to the regulatory asset are recognized as an adjustment to the regulatory asset account as these amounts are recognized as components of net periodic pension costs each year.

The following table sets forth the Pension Plan’s and post-retirement medical plan’s funded status and amounts recognized in Registrant’s balance sheets and the components of net pension cost and accrued liability at December 31, 2014 and 2013:

(dollars in thousands)	Pension Benefits		Post-Retirement Medical Benefits	
	2014	2013	2014	2013
<b>Change in Projected Benefit Obligation:</b>				
Projected benefit obligation at beginning of year	\$ 152,680	\$ 163,230	\$ 11,388	\$ 12,296
Service cost	5,643	6,967	348	407
Interest cost	7,520	6,907	495	439
Actuarial loss (gain)	24,339	(19,918)	437	(1,340)
Benefits/expenses paid	(4,998)	(4,506)	(342)	(414)
Projected benefit obligation at end of year	\$ 185,184	\$ 152,680	\$ 12,326	\$ 11,388
<b>Changes in Plan Assets:</b>				
Fair value of plan assets at beginning of year	\$ 127,534	\$ 107,638	\$ 9,873	\$ 8,359
Actual return on plan assets	9,816	17,846	951	1,320
Employer contributions	8,209	6,556	241	608
Benefits/expenses paid	(4,998)	(4,506)	(342)	(414)
Fair value of plan assets at end of year	\$ 140,561	\$ 127,534	\$ 10,723	\$ 9,873
<b>Funded Status:</b>				
Net amount recognized as accrued pension cost	\$ (44,623)	\$ (25,146)	\$ (1,603)	\$ (1,515)

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(in thousands)	Pension Benefits		Post-Retirement Medical Benefits	
	2014	2013	2014	2013
<b>Amounts recognized on the balance sheets:</b>				
Current liabilities	\$ —	\$ —	\$ —	\$ —
Non-current liabilities	(44,623)	(25,146)	(1,603)	(1,515)
Net amount recognized	\$ (44,623)	\$ (25,146)	\$ (1,603)	\$ (1,515)
<b>Amounts recognized in regulatory assets consist of:</b>				
Initial net obligation	\$ —	\$ —	\$ —	\$ 417
Prior service cost (credit)	167	285	(234)	(433)
Net (gain) loss	39,003	15,581	(2,891)	(3,159)
<b>Regulatory assets (liabilities)</b>	39,170	15,866	(3,125)	(3,175)
Unfunded accrued pension cost	5,453	9,280	4,728	4,690
Net liability recognized	\$ 44,623	\$ 25,146	\$ 1,603	\$ 1,515
<b>Changes in plan assets and benefit obligations recognized in regulatory assets:</b>				
Regulatory asset at beginning of year	\$ 15,866	\$ 49,052	\$ (3,175)	r\$ (685)
Net loss (gain)	23,422	(30,190)	(61)	(2,278)
Amortization of initial net obligation	—	—	(419)	(419)
Amortization of prior service (cost) credit	(118)	(118)	200	200
Amortization of net gain (loss)	—	(2,878)	330	7
Total change in regulatory asset	23,304	(33,186)	50	(2,490)
Regulatory asset (liability) at end of year	\$ 39,170	\$ 15,866	\$ (3,125)	\$ (3,175)
Net periodic pension costs	\$ 4,383	\$ 9,296	\$ 278	\$ 676
Change in regulatory asset	23,304	(33,186)	50	(2,490)
Total recognized in net periodic pension cost and regulatory asset (liability)	\$ 27,687	\$ (23,890)	\$ 328	\$ (1,814)
<b>Estimated amounts that will be amortized from regulatory asset over the next fiscal year:</b>				
Initial net obligation	\$ —	\$ —	\$ —	\$ (418)
Prior service (cost) credit	\$ (118)	\$ (118)	\$ 200	\$ 200
Net gain (loss)	\$ (1,878)	\$ (29)	\$ 213	\$ 262
<b>Additional year-end information for plans with an accumulated benefit obligation in excess of plan assets:</b>				
Projected benefit obligation	\$ 185,184	\$ 152,680	\$ 12,326	\$ 11,388
Accumulated benefit obligation	\$ 160,510	\$ 131,580	N/A	N/A
Fair value of plan assets	\$ 140,561	\$ 127,534	\$ 10,723	\$ 9,873
<b>Weighted-average assumptions used to determine benefit obligations at December 31:</b>				
Discount rate	4.25%	5.10%	3.80%	4.65%
Rate of compensation increase	4.00%	4.00%	N/A	N/A

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Consistent with decisions from the CPUC and in accordance with regulatory accounting principles, Registrant capitalizes a portion of its pension and other post-retirement costs in the overhead pool included in Utility Plant. The components of net periodic pension and post-retirement benefits cost, before allocation to the overhead pool, for 2014, 2013 and 2012 are as follows:

(dollars in thousands, except percent)	Pension Benefits			Post-Retirement Medical Benefits		
	2014	2013	2012	2014	2013	2012
<b>Components of Net Periodic Benefits Cost:</b>						
Service cost	\$ 5,643	\$ 6,967	\$ 6,675	\$ 348	\$ 407	\$ 419
Interest cost	7,520	6,907	6,657	495	439	534
Expected return on plan assets	(8,898)	(7,574)	(6,540)	(453)	(382)	(357)
Amortization of transition	—	—	—	418	419	419
Amortization of prior service cost (credit)	118	118	118	(200)	(200)	(200)
Amortization of actuarial (gain) loss	—	2,878	3,035	(330)	(7)	—
Net periodic pension cost under accounting standards	\$ 4,383	\$ 9,296	\$ 9,945	\$ 278	\$ 676	\$ 815
Regulatory adjustment - over/(under) collection	1,622	(1,920)	(2,305)	—	—	—
Total expense recognized, before allocation to overhead pool	\$ 6,005	\$ 7,376	\$ 7,640	\$ 278	\$ 676	\$ 815

**Weighted-average assumptions used to determine net periodic cost:**

Discount rate	5.10%	4.30%	4.65%	4.65%	3.75%	4.45%
Expected long-term return on plan assets	7.00%	7.00%	7.00%	*	*	*
Rate of compensation increase	4.00%	4.00%	4.00%	N/A	N/A	N/A

\*7.0% for union plan, 4.2% for non-union, net of income taxes in 2014, 2013 and 2012.

Regulatory Adjustment:

As previously discussed in Note 2, the CPUC authorized GSWC to track differences between the forecasted annual pension expenses adopted in rates for its water regions and the general office and the actual annual expense to be recorded by GSWC in accordance with the accounting guidance for pension costs. During the year ended December 31, 2014, GSWC's actual expense was \$1.6 million lower than the amounts included in water and electric customer rates. During the years ended December 31, 2013 and 2012, GSWC's actual expense under the accounting standard was greater than the amounts included in customer rates by \$1.9 million and \$2.3 million, respectively. These over and under-collections have been recorded in the two-way pension balancing accounts included in regulatory assets. As of December 31, 2014, the pension balancing account had a \$2.7 million net under-collection included in regulatory assets.

Plan Funded Status:

Registrant's pension and post-retirement plans were underfunded at December 31, 2014 and 2013. Registrant's market related value of plan assets is equal to the fair value of plan assets. Past volatile market conditions have affected the value of GSWC's trust established to fund its future long-term pension benefits. These benefit plan assets and related obligations are measured annually using a December 31 measurement date. Changes in the plan's funded status will affect the assets and liabilities recorded on the balance sheet in accordance with accounting guidance on employers' accounting for defined benefit pension and other post-retirement plans. Due to Registrant's regulatory recovery treatment, the recognition of the funded status is offset by a regulatory asset pursuant to guidance on accounting for the effects of certain types of regulation.

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Plan Assets:

The assets of the pension and post-retirement medical plans are managed by a third party trustee. The investment policy allocation of the assets in the trust was approved by Registrant's Administrative Committee (the "Committee") for the pension and post-retirement medical funds, which has oversight responsibility for all retirement plans. The primary objectives underlying the investment of the pension and post-retirement plan assets are: (i) attempt to maintain a fully funded status with a cushion for unexpected developments, possible future increases in expense levels, and/or a reduction in the expected return on investments; (ii) seek to earn long-term returns that compare favorably to appropriate market indexes, peer group universes and the policy asset allocation index; (iii) seek to provide sufficient liquidity to pay current benefits and expenses; (iv) attempt to limit risk exposure through prudent diversification, and (v) seek to limit costs of administering and managing the plans.

The Committee recognizes that risk and volatility are present to some degree with all types of investments. High levels of risk may be avoided through diversification by asset class, style of each investment manager and sector and industry limits. Investment managers are retained to manage a pool of assets and allocate funds in order to achieve an appropriate, diversified and balanced asset mix. The Committee's strategy balances the requirement to maximize returns using potentially higher return generating assets, such as equity securities, with the need to control the risk of its benefit obligations with less volatile assets, such as fixed income securities.

The Committee approves the target asset allocations. Registrant's pension and post-retirement plan weighted-average asset allocations at December 31, 2014 and 2013, by asset category are as follows:

Asset Category	Pension Benefits		Post-Retirement Medical Benefits	
	2014	2013	2014	2013
<b>Actual Asset Allocations:</b>				
Equity securities	61%	61%	60%	61%
Debt securities	39%	37%	38%	38%
Cash equivalents	—%	2%	2%	1%
Total	100%	100%	100%	100%

Equity securities did not include AWR's stock as of December 31, 2014 and 2013.

Target Asset Allocations for 2015:	Pension Benefits	Post-retirement Medical Benefits
Equity securities	60%	60%
Debt securities	40%	40%
Total	100%	100%

As previously discussed in Note 4, accounting guidance for fair value measurements establishes a framework for measuring fair value and requires fair value measurements to be classified and disclosed in one of three levels. As required by the accounting guidance, assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. All equity investments in the pension and post-retirement plans are Level 1 investments in mutual funds. The fixed income category includes corporate bonds and notes. The majority of fixed income investments range in maturities from less than one to twenty years. The fair values of these investments are based on quoted market prices in active markets.

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The following tables set forth by level, within the fair value hierarchy, the pension and post-retirement plans' investment assets measured at fair value as of December 31, 2014 and 2013:

(dollars in thousands)	Fair Value as of December 31, 2014			
	Level 1	Level 2	Level 3	Total
<b>Fair Value of Pension Plan Assets:</b>				
Cash equivalents	\$ 497	—	—	\$ 497
Fixed income securities	54,865	—	—	54,865
<u>Equity securities:</u>				
U.S. small cap stocks	7,546	—	—	7,546
U.S. mid cap stocks	14,779	—	—	14,779
U.S. large cap stocks	42,886	—	—	42,886
International funds	11,318	—	—	11,318
Real estate funds	8,670	—	—	8,670
Total equity securities	85,199	—	—	85,199
Total investments measured at fair value	\$ 140,561	—	—	\$ 140,561

<b>Fair Value of Post-Retirement Plan Assets:</b>				
Cash equivalents	\$ 185	—	—	\$ 185
Fixed income	4,105	—	—	4,105
U.S. equity securities (large cap stocks)	6,433	—	—	6,433
Total investments measured at fair value	\$ 10,723	—	—	\$ 10,723

(dollars in thousands)	Fair Value as of December 31, 2013			
	Level 1	Level 2	Level 3	Total
<b>Fair Value of Pension Plan Assets:</b>				
Cash equivalents	\$ 2,096	—	—	\$ 2,096
Fixed income securities	47,627	—	—	47,627
<u>Equity securities:</u>				
U.S. small cap stocks	6,576	—	—	6,576
U.S. mid cap stocks	13,119	—	—	13,119
U.S. large cap stocks	39,280	—	—	39,280
International funds	12,501	—	—	12,501
Real estate funds	6,335	—	—	6,335
Total equity securities	77,811	—	—	77,811
Total investments measured at fair value	\$ 127,534	—	—	\$ 127,534

<b>Fair Value of Post-Retirement Plan Assets:</b>				
Cash equivalents	\$ 142	—	—	\$ 142
Fixed income	3,731	—	—	3,731
U.S. equity securities (large cap stocks)	6,000	—	—	6,000
Total investments measured at fair value	\$ 9,873	—	—	\$ 9,873

Plan Contributions:

During 2014, Registrant contributed \$8.2 million and \$241,000 to its pension and post-retirement medical plans, respectively. Registrant currently expects to contribute at least \$6.0 million to its pension in 2015. Registrant's policy is to fund the plans annually at a level which is deductible for income tax purposes and is consistent with amounts recovered in customer rates.



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Benefit Payments:

Registrant's estimated future benefit payments at December 31, 2014 for the next five years and thereafter are as follows (in thousands):

	<u>Pension Benefits</u>	<u>Post-Retirement Medical Benefits</u>
2015	\$ 5,468	\$ 566
2016	5,938	601
2017	6,489	680
2018	7,030	774
2019	7,569	866
Thereafter	48,446	5,247
Total	<u>\$ 80,940</u>	<u>\$ 8,734</u>

Assumptions:

Certain actuarial assumptions, such as the discount rate, long-term rate of return on plan assets, life expectancy, and the healthcare cost trend rate have a significant effect on the amounts reported for net periodic benefit cost as well as the related benefit obligation amounts.

*Discount Rate* — The assumed discount rate for pension and post-retirement medical plans reflects the market rates for high-quality corporate bonds currently available. Registrant's discount rates were determined by considering the average of pension yield curves constructed of a large population of high quality corporate bonds. The resulting discount rate reflects the matching of plan liability cash flows to the yield curves.

*Expected Long-Term Rate of Return on Assets* — The long-term rate of return on plan assets represents an estimate of long-term returns on an investment portfolio consisting of a mixture of equities, fixed income and other investments. To develop the expected long-term rate of return on assets assumption for the pension plan, Registrant considered the historical returns and the future expectations for returns for each asset class, as well as the target asset allocation of the pension portfolio. Registrant's policy is to fund the medical benefit trusts based on actuarially determined amounts as allowed in rates approved by the CPUC. Registrant has invested the funds in the post-retirement trusts that will achieve a desired return and minimize amounts necessary to recover through rates. The mix is expected to provide for a return on assets similar to the Pension Plan and to achieve Registrant's targeted allocation. This resulted in the selection of the 7.0% long-term rate of return on assets assumption for the union plan and 4.2% (net of income taxes) for the non-union plan portion of the post retirement plan.

*Mortality* — Mortality assumptions are a critical component of benefit obligation amounts and a key factor in determining the expected length of time for annuity payments. In 2014, the Society of Actuaries released new mortality tables for pension plans. The benefit obligation amounts as of December 31, 2014 assumed a longer life expectancy of participants as a result of the actuarial update to mortality tables, resulting in an increase of approximately 3% in the related benefit obligation amounts.

*Healthcare Cost Trend Rate* — A sliding scale for assumed health care cost increases was used for the periods presented. In 2014, health care cost increases started at 6.8% grading down to 5.6% in 10 years for those under age 65, and at 7.0% grading down to 5.1% in 10 years for those 65 and over. In 2013, health care cost increases started at 7.8% grading down to 6.3% in 10 years for those under age 65, and at 7.0% grading down to 5.7% in 10 years for those 65 and over. In 2012, health care cost increases started at 8.0% grading down to 7.2% in 10 years for those under age 65, and at 7.0% grading down to 5.8% in 10 years for those 65 and over. Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects on the post-retirement medical plan:

<u>(dollars in thousands)</u>	<u>1-Percentage-Point Increase</u>	<u>1-Percentage-Point Decrease</u>
Effect on total of service and interest cost components	\$ 80	\$ (70)
Effect on post-retirement benefit obligation	\$ 1,438	\$ (1,232)

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**Supplemental Executive Retirement Plan:**

Registrant has a supplemental executive retirement plan (“SERP”) that provides additional retirement benefits to certain key employees and officers of Registrant by making up benefits, which are limited by Sections 415 and 401(a)(17) of the Internal Revenue Code of 1986, as amended, and certain additional benefits. The Board of Directors approved the establishment of a Rabbi Trust created for the SERP. Assets in a Rabbi Trust can be subject to the claims of creditors; therefore, they are not considered as an asset for purposes of computing the SERP’s funded status. As of December 31, 2014, the balance in the Rabbi Trust totaled \$8.8 million and is included in Registrant’s other property and investments.

All equity investments in the Rabbi Trust are Level 1 investments in mutual funds. The fixed income category includes corporate bonds and notes. The fair values of these investments are based on quoted market prices in active markets. The following tables set forth by level, within the fair value hierarchy, the Rabbi Trust investment assets measured at fair value as of December 31, 2014 and 2013.

(dollars in thousands)	Fair Value as of December 31, 2014			
	Level 1	Level 2	Level 3	Total
<b>Fair Value of Assets held in Rabbi Trust:</b>				
Cash equivalents	\$ 29	—	—	\$ 29
Fixed income securities	3,454	—	—	3,454
Equity securities	5,282	—	—	5,282
Total investments measured at fair value	\$ 8,765	—	—	\$ 8,765
(dollars in thousands)	Fair Value as of December 31, 2013			
	Level 1	Level 2	Level 3	Total
<b>Fair Value of Assets held in Rabbi Trust:</b>				
Cash equivalents	\$ 27	—	—	\$ 27
Fixed income securities	2,587	—	—	2,587
Equity securities	4,202	—	—	4,202
Total investments measured at fair value	\$ 6,816	—	—	\$ 6,816

The following provides a reconciliation of benefit obligations, funded status of the SERP, as well as a summary of significant estimates at December 31, 2014 and 2013:

(dollars in thousands)	2014	2013
<b>Change in Benefit Obligation:</b>		
Benefit obligation at beginning of year	\$ 12,296	\$ 12,406
Service cost	768	803
Interest cost	615	514
Actuarial (gain) loss	2,497	(1,198)
Benefits paid	(250)	(229)
Benefit obligation at end of year	\$ 15,926	\$ 12,296
<b>Changes in Plan Assets:</b>		
Fair value of plan assets at beginning of year	—	—
Fair value of plan assets at end of year	—	—
<b>Funded Status:</b>		
Net amount recognized as accrued cost	\$ (15,926)	\$ (12,296)

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(in thousands)	2014	2013
<b>Amounts recognized on the balance sheets:</b>		
Current liabilities	\$ (379)	\$ (230)
Non-current liabilities	(15,547)	(12,066)
Net amount recognized	<u>\$ (15,926)</u>	<u>\$ (12,296)</u>
<b>Amounts recognized in regulatory assets consist of:</b>		
Prior service cost	\$ 153	\$ 314
Net loss	4,530	2,172
<b>Regulatory assets</b>	<u>4,683</u>	<u>2,486</u>
Unfunded accrued cost	11,243	9,810
Net liability recognized	<u>\$ 15,926</u>	<u>\$ 12,296</u>
<b>Changes in plan assets and benefit obligations recognized in regulatory assets consist of:</b>		
Regulatory asset at beginning of year	\$ 2,486	\$ 4,184
Net (gain) loss	2,497	(1,199)
Amortization of prior service credit	(161)	(161)
Amortization of net loss	(139)	(338)
Total change in regulatory asset	<u>2,197</u>	<u>(1,698)</u>
Regulatory asset at end of year	<u>\$ 4,683</u>	<u>\$ 2,486</u>
Net periodic pension cost	\$ 1,683	\$ 1,817
Change in regulatory asset	2,197	(1,698)
Total recognized in net periodic pension and net income	<u>\$ 3,880</u>	<u>\$ 119</u>
<b>Estimated amounts that will be amortized from regulatory asset over the next fiscal year:</b>		
Initial net asset (obligation)	—	—
Prior service cost	\$ (117)	\$ (161)
Net loss	(431)	(139)
<b>Additional year-end information for plans with an accumulated benefit obligation in excess of plan assets:</b>		
Projected benefit obligation	\$ 15,926	\$ 12,296
Accumulated benefit obligation	13,992	10,116
Fair value of plan assets	—	—
<b>Weighted-average assumptions used to determine benefit obligations:</b>		
Discount rate	4.15%	5.05%
Rate of compensation increase	4.00%	4.00%

The components of SERP expense, before allocation to the overhead pool, for 2014, 2013 and 2012 are as follows:

(dollars in thousands, except percent)	2014	2013	2012
<b>Components of Net Periodic Benefits Cost:</b>			
Service cost	\$ 768	\$ 803	\$ 731
Interest cost	615	514	488
Amortization of prior service cost	161	161	161
Amortization of net loss	139	339	307
Net periodic pension cost	<u>\$ 1,683</u>	<u>\$ 1,817</u>	<u>\$ 1,687</u>
<b>Weighted-average assumptions used to determine net periodic cost:</b>			
Discount rate	5.05%	4.20%	4.65%
Rate of compensation increase	4.00%	4.00%	4.00%

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Benefit Payments: Registrant's estimated future benefit payments for the SERP at December 31, 2014 for the next ten years are as follows (in thousands):

2015	\$	379
2016		391
2017		472
2018		614
2019		712
Thereafter		5,402
Total	\$	7,970

**401(k) Investment Incentive Program:**

Registrant has a 401(k) Investment Incentive Program under which employees may invest a percentage of their pay, up to a maximum investment prescribed by law, in an investment program managed by an outside investment manager. Registrant's cash contributions to the 401(k) are based upon a percentage of individual employee contributions and totaled \$1.9 million for each of the years ended December 31, 2014, 2013 and 2012. In 2011, this program was amended to incorporate the defined contribution plan previously discussed. Contributions to the defined contribution plan for the years ended December 31, 2014, 2013 and 2012 were \$568,000, \$394,000 and \$254,000, respectively.

**Affordable Care Act:**

In 2010, the Patient Protection and Affordable Care Act ("Affordable Care Act") was passed and was to become effective in 2014. In July 2013, compliance with the employer mandate and certain reporting requirements under the Affordable Care Act were delayed until 2015. Registrant's health care plan meets the current requirements of the Affordable Care Act. Registrant continues to assess the impact of the Affordable Care Act on its health care benefit costs, but does not expect it to have a material impact in the near future on the Registrant's consolidated financial position, results of operations or cash flows.

**Note 12 — Stock-Based Compensation Plans**

**Summary Description of Stock Incentive Plans**

AWR currently has four stock incentive plans: the 2000 and 2008 employee plans for its employees, and the 2003 and 2013 directors plans for directors, each more fully described below.

*2000 and 2008 Employee Plans* — AWR adopted the 2000 and 2008 employee plans to provide stock-based incentive awards in the form of stock options, restricted stock units and restricted stock to employees as a means of promoting the success of Registrant by attracting, retaining and more fully aligning the interests of employees with those of shareholders generally. The 2008 Employee Plan also provides for the grant of performance awards. No additional grants may be made under the 2000 employee plan.

For stock options, Registrant's Compensation Committee of the Board of Directors ("Compensation Committee") determines, among other things, the date of grant, the form, term, option exercise price, vesting and exercise terms of each option. Stock options granted by AWR have been in the form of nonqualified stock options, expire ten years from the date of grant, vest over a period of three years and are subject to earlier termination as provided in the form of option agreement approved by the Compensation Committee. The option price per share is determined by the Compensation Committee at the time of grant, but may not be less than the fair market value of Common Shares on the date of grant.

For restricted stock unit awards, the Compensation Committee determines the specific terms, conditions and provisions relating to each restricted stock unit. Each employee who has been granted a time-vested restricted stock unit is entitled to dividend equivalent rights in the form of additional restricted stock units until vesting of the time-vested restricted stock units. In general, time-vested restricted stock units vest over a period of three years. Each restricted stock unit is non-voting and entitles the holder of the restricted stock unit to receive one Common Share.

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The Compensation Committee also has the authority to determine the size, number, amount or value of performance awards, the duration of the performance period or performance periods applicable to the award and the performance criteria applicable to each performance award for each performance period. The grant and or vesting of the performance awards are contingent, in whole or in part, upon the attainment of specified performance criteria or the occurrence of any event or events involving a change in control event, death or total disability as the Compensation Committee may determine. In its discretion, the Compensation Committee may grant dividend equivalent rights on performance awards upon the terms and conditions set forth in the award agreement. Each outstanding performance award granted by the Compensation Committee has been in the form of restricted stock units that generally vest over a period of three years as provided in the performance award agreement. Each employee who has been granted a performance award is entitled to dividend equivalent rights in the form of additional restricted stock units until payment of the performance award.

*2003 and 2013 Directors Plans* — The Board of Directors and shareholders of AWR have approved the 2003 and 2013 directors plans in order to provide the non-employee directors with supplemental stock-based compensation to encourage them to increase their stock ownership in AWR. No more grants may be made under the 2003 directors plan.

Commencing in 2009, non-employee directors have received restricted stock units equal to two times the annual retainer. One-third of the restricted stock units granted in 2009-2012 are payable to each non-employee director at the earlier of the first, second and third anniversaries of the date of grant and the date of termination of service as a director. Each non-employee director is entitled to receive restricted stock units granted after 2012 ninety days after the grant date. Restricted stock units credited to each non-employee director's restricted stock unit account are at all times fully vested and non-forfeitable.

The stock options granted under the 2003 directors plan are nonqualified stock options which must be exercised within ten years after the date of grant. The exercise price of the stock options is equal to the fair market value of Common Shares on the date of grant. Stock options granted under the 2003 directors plan are fully vested and exercisable upon the date of grant. Restricted stock units with respect to dividend equivalent rights on stock options credited to the non-employee director are payable in Common Shares on the earlier of the date on which the stock option is exercised and three years from the date of grant of the stock option. No stock options have been granted to directors since AWR's 2006 annual meeting and no stock options may be granted to directors under the 2013 directors plan.

All stock options, restricted stock units and performance awards have been granted with dividend equivalent rights payable in the form of additional restricted stock units.

**Recognition of Compensation Expense**

Registrant recognizes compensation expense related to the fair value of stock-based compensation awards. Share-based compensation cost is measured by the Registrant at the grant date, based on the calculated fair value of the award, and is recognized as an expense over the employee's requisite service period (generally the vesting period of the equity grant). Immediate vesting does occur if the employee is at least 55 years old and the sum of the employee's age and years of employment is equal to or greater than 75. Registrant assumes that forfeitures will be minimal, and recognizes forfeitures as they occur, which results in a reduction in compensation expense.

The following table presents share-based compensation expenses for the years ended December 31, 2014, 2013 and 2012. These expenses resulting from stock options, restricted stock units and performance awards are included in administrative and general expenses in AWR and GSWC's statements of income:

(in thousands)	AWR			GSWC		
	For The Years Ended December 31,			For The Years Ended December 31,		
	2014	2013	2012	2014	2013	2012
Stock-based compensation related to:						
Stock options	\$ —	\$ 9	\$ 150	\$ —	\$ 8	\$ 147
Restricted stock units	1,354	1,507	1,729	1,113	1,266	1,468
Performance awards	868	493	52	635	373	52
Total stock-based compensation expense	\$ 2,222	\$ 2,009	\$ 1,931	\$ 1,748	\$ 1,647	\$ 1,667

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Equity-based compensation cost, capitalized as part of utility plant for the years ended December 31, 2014, 2013 and 2012 was \$255,000, \$334,000 and \$259,000, respectively, for both AWR and GSWC.

Registrant amortizes stock-based compensation over the requisite (vesting) period for the entire award. Options issued pursuant to the 2000 employee plan vest and are exercisable in installments of 33% the first two years and 34% in the third year, starting one year from the date of the grant and expire 10 years from the date of the grant. No stock options have been granted under the 2008 plan. Time-vesting restricted stock units vest and become nonforfeitable in installments of 33% the first two years and 34% in the third year, starting one year from the date of the grant. Outstanding performance awards vest and become nonforfeitable in installments of 33% the first two years and 34% in the third year, and are distributed at the end of the performance period if the performance criteria set forth in the award agreement are satisfied.

*Stock Options* — There were no stock options granted during the years 2014, 2013 or 2012. A summary of stock option activity as of December 31, 2014 and changes during the year ended December 31, 2014, are presented below:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Options outstanding at January 1, 2014	264,596	\$ 17.16		
Granted	—			
Exercised	(37,006)	15.93		
Forfeited or expired	(5,010)	12.77		
Options outstanding at December 31, 2014	222,580	\$ 17.47	3	\$ 4,494,733
Options exercisable at December 31, 2014	222,580	\$ 17.47	3	\$ 4,494,733

The aggregate intrinsic value in the table above represents the total pretax intrinsic value (i.e., the difference between the closing price of the Common Shares on the last trading day of the 2014 calendar year and the exercise price, times the number of shares) that would have been received by the option holders had all option holders exercised their option on December 31, 2014. This amount changes if the fair market value of the Common Shares changes. The total intrinsic value of options exercised during the years ended December 31, 2014, 2013 and 2012 was approximately \$596,000, \$1,402,000 and \$4,125,000, respectively.

During the years ended December 31, 2014, 2013 and 2012, Registrant received approximately \$589,000, \$2,111,000 and \$13,295,000, respectively, in cash proceeds from the exercise of its stock options and realized approximately \$533,000, \$1,026,000 and \$890,000, respectively, of tax benefit for the tax deduction from awards exercised. An immaterial amount of compensation cost related to outstanding stock options was recognized in 2014.

*Restricted Stock Units* — A restricted stock unit (“RSU”) represents the right to receive a share of AWR’s Common Shares and are valued based on the fair market value of AWR’s Common Shares on the date of grant. The fair value of RSUs were determined based on the closing trading price of Common Shares on the grant date. A summary of the status of Registrant’s outstanding RSUs, excluding performance awards, to employees and directors as of December 31, 2014, and changes during the year ended December 31, 2014, is presented below:

	Number of Restricted Share Units	Weighted Average Grant-Date Value
Restricted share units at January 1, 2014	197,036	\$ 19.04
Granted	56,059	29.05
Vested	(103,580)	20.62
Forfeited	(4,040)	25.08
Restricted share units at December 31, 2014	145,475	\$ 21.61

As of December 31, 2014, there was approximately \$666,000 of total unrecognized compensation cost related to restricted stock units granted under AWR’s employee and director’s stock plans. That cost is expected to be recognized over a remaining period ranging from 0.08 to 2.82 years.

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*Performance Awards* – During the years ended December 31, 2014 and 2013, the Compensation Committee granted performance awards in the form of restricted stock units to officers of the Registrant. A performance award represents the right to receive a share of AWR's Common Shares if specified performance goals are met over the performance period specified in the grant (generally three years), subject to certain exceptions through the performance period. Each grantee of any outstanding performance award may earn between 0% and 200% of the target amount depending on Registrant's performance against performance goals, which are determined by the Compensation Committee on the date of grant. A summary of the status of Registrant's outstanding performance awards to officers as of December 31, 2014, and changes during the year ended December 31, 2014, is presented below:

	Number of Performance awards	Weighted Average Grant-Date Value
Performance awards at January 1, 2014	40,920	\$ 25.63
Granted	38,948	29.10
Vested	(4,041)	18.68
Performance awards at December 31, 2014	75,827	\$ 27.78

A portion of the fair value of performance awards was estimated at the grant date based on the probability of satisfying the market-based conditions. The portion of the fair value of the performance awards associated with performance-based conditions was based on the fair market value of AWR's stock at the grant date. The fair value of each outstanding performance award grant is amortized into compensation expense in installments of 33% the first two years and 34% in the third year of their respective vesting periods, which is generally over 3 years unless earlier vested pursuant to the terms of the agreement. The accrual of compensation costs is based on the estimate of the final expected value of the award, and is adjusted as required for the portion based on the performance-based condition. As of December 31, 2014, \$635,000 of unrecognized compensation costs related to performance awards is expected to be recognized over a weighted average period ranging from 0.41 to 2.08 years.

*Restricted Stock* - AWR has no restricted stock outstanding as of December 31, 2014.

**Note 13 - Commitments**

**GSWC's Water Supply:**

GSWC obtains its water supply from its operating wells and purchases from others, principally member agencies of the Metropolitan Water District of Southern California ("MWD"). MWD is a public agency and quasi-municipal corporation created in 1928 by a vote of the electorates of several Southern California cities. MWD's primary purpose was and is to provide a supplemental supply of water for domestic and municipal uses and purposes at wholesale rates to its member public agencies. GSWC has connections to MWD's water distribution facilities and those of other member water agencies. MWD's principal sources of water are the State Water Project and the Colorado River.

GSWC has contracts to purchase water or water rights for an aggregate amount of \$5.3 million as of December 31, 2014. Included in the \$5.3 million is a commitment of \$3.1 million to lease water rights from a third party under an agreement which expires in 2028. The remaining \$2.2 million are commitments for purchased water with other third parties which expire through 2038.

GSWC's estimated future minimum payments under these purchased water supply commitments at December 31, 2014 are as follows (in thousands):

2015	\$	447
2016		319
2017		319
2018		319
2019		319
Thereafter		3,541
Total	\$	5,264

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**Bear Valley Electric:**

Generally, GSWC's electric division purchases power at a fixed cost, under long-term purchased power contracts, depending on the amount of power and the period during which the power is purchased under such contracts. During 2014, GSWC's power purchases were based on month-to-month arrangements, as the previous long-term purchase power contract expired in 2013. However, in December 2014 the CPUC approved an application that allowed GSWC to immediately execute new purchased power contracts with energy providers on December 9, 2014. GSWC began taking power effective January 1, 2015 at a fixed cost over three and five year terms depending on the amount of power and period during which the power is purchased under the contracts. As of December 31, 2014, GSWC's commitment under these contracts totaled approximately \$31.1 million.

The minimum load at GSWC's BVES customer service area has been approximately 11 MWs. The average winter load has been 20 MWs with a winter peak of 45 MWs when the snowmaking machines at the ski resorts are operating. In addition to the purchased power contracts, GSWC buys additional energy to meet demand on the spot market. GSWC owns a natural gas-fueled 8.4 MW generation facility, which assists GSWC in meeting peak demand.

The ability of GSWC to deliver purchased power to customers in its BVES service area is limited by the ability of the transmission facilities owned by Southern California Edison Company to transmit this power.

**Operating Leases:**

Registrant leases equipment and facilities primarily for its Regional and District offices and ASUS operations under non-cancelable operating leases with varying terms, provisions and expiration dates. Rent expense for leases that contain scheduled rent increases are recorded on a straight-line basis. During 2014, 2013 and 2012, Registrant's consolidated rent expense was approximately \$2,982,000, \$2,982,000 and \$3,098,000, respectively. Registrant's future minimum payments under long-term non-cancelable operating leases at December 31, 2014 are as follows (in thousands):

2015	\$	2,345
2016		2,130
2017		1,895
2018		1,508
2019		1,232
Thereafter		1,904
Total	<u>\$</u>	<u>11,014</u>

There is no material difference between the consolidated operations of AWR and the operations of GSWC in regards to the future minimum payments under long-term non-cancelable operating leases.

**Note 14 - Contingencies**

**Condemnation of Properties:**

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 necessary and in the public interest. In addition, these laws provide: (i) that the owner of utility property may contest whether the condemnation is actually necessary and in the public interest, and (ii) that the owner is entitled to receive the fair market value of its property if the property is ultimately taken.

**Claremont System:**

On November 4, 2014, voters in the City of Claremont approved a measure authorizing the issuance of \$135.0 million in water revenue bonds by the City to finance the acquisition of the Claremont water system. On December 9, 2014, the City filed an eminent domain lawsuit against GSWC. GSWC has the ability to legally challenge the government's right to take its property. GSWC does not believe the seizure is necessary and intends to vigorously defend against the potential condemnation. At this time, management cannot predict the outcome of the eminent domain proceeding. The Claremont water system has a net book value of approximately \$47.7 million. GSWC serves approximately 11,000 customers in Claremont.



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*Ojai System:*

In March 2013, Casitas Municipal Water District ("CMWD") passed resolutions under the Mello-Roos Community Facilities District Act of 1982 ("Mello-Roos Act") authorizing the establishment of a Community Facilities District, and the issuance of bonds to finance the potential acquisition of GSWC's Ojai system by eminent domain. In August 2013, Ojai residents approved the levying of a special tax to satisfy the planned bond obligations. GSWC filed a petition in the Superior Court, Ventura County, which, among other things, challenged the legality of CMWD's effort to utilize the Mello-Roos Act to acquire property by eminent domain and to fund legal and expert costs of the planned condemnation. Ojai FLOW ("Friends of Locally Owned Water") members filed a motion with the Superior Court asking that all residents of GSWC's Ojai service area be certified as class defendants in GSWC's pending action. They contend that the class would later be entitled to sue GSWC for damages if GSWC's challenge is denied. Without deciding whether such a lawsuit would be permitted, the Court granted the motion for class certification. On March 13, 2014, the Court denied GSWC's petition. On April 9, 2014, GSWC filed a Notice of Appeal. GSWC is unable to predict the outcome of the appeal at this time. GSWC serves approximately 3,000 customers in Ojai.

*Apple Valley System:*

In recent years the Town of Apple Valley has considered a potential condemnation of the water systems serving its area, including GSWC's Apple Valley system. In August 2014, Apple Valley's Town Council issued a request for proposal for an updated feasibility study on the potential acquisition of the water systems. The feasibility study has been completed, however, the Town of Apple Valley has not taken any action against GSWC. GSWC serves approximately 2,900 customers in the Town of Apple Valley.

*Artesia System:*

On October 13, 2014, the City of Artesia's City Council approved the funding of a feasibility study on the potential acquisition of GSWC's water system in Artesia. GSWC serves approximately 3,300 customers in Artesia.

***Environmental Clean-Up and Remediation:***

GSWC has been involved in environmental remediation and clean-up at a plant site ("Chadron Plant") that contained an underground storage tank which was used to store gasoline for its vehicles. This tank was removed from the ground in July 1990 along with the dispenser and ancillary piping. Since then, GSWC has been involved in various remediation activities at this site. Recent analysis indicates that offsite monitoring wells may also be necessary to document effectiveness of remediation.

As of December 31, 2014, the total spent to clean-up and remediate GSWC's plant facility was approximately \$4.5 million, of which \$1.5 million has been paid by the State of California Underground Storage Tank Fund. Amounts paid by GSWC have been included in rate base and approved by the CPUC for recovery. As of December 31, 2014, GSWC has a regulatory asset and an accrued liability for the estimated additional cost of \$1.4 million to complete the clean-up at the site. The estimate includes costs for two years of continued activities of groundwater cleanup and monitoring, future soil treatment and site closure related activities. The ultimate cost may vary as there are many unknowns in remediation of underground gasoline spills and this is an estimate based on currently available information. Management also believes it is probable that the estimated additional costs will be approved in rate base by the CPUC.

***Other Litigation:***

Registrant is also subject to other ordinary routine litigation incidental to its business. Management believes that the opportunity for rate recovery, 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. Registrant is unable to predict an estimate of the loss, if any, resulting from any pending suits or administrative proceedings.

**Note 15 - Construction Program**

GSWC maintains an ongoing water distribution main replacement program throughout its customer service areas based on the age and type of distribution system materials, priority of leaks detected, remaining productive life of the distribution system and an underlying replacement schedule. In addition, GSWC upgrades its electric and water supply facilities in accordance with industry standards, local requirements and CPUC requirements. As of December 31, 2014, GSWC has unconditional purchase obligations for capital projects of approximately \$19.5 million.

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**Note 16 - Business Segments**

AWR has 3 reportable segments, water, electric and contracted services, whereas GSWC has 2 segments, water and electric. AWR has no material assets other than its investments in its subsidiaries on a stand-alone basis.

All activities of GSWC, a rate-regulated utility, are geographically located within California. Activities of ASUS and its subsidiaries are conducted in California, Georgia, Maryland, New Mexico, North Carolina, South Carolina, Texas and Virginia. Each of ASUS's wholly-owned subsidiaries is regulated by the state in which the subsidiary primarily conducts water and/or wastewater operations. Fees charged for operations and maintenance and renewal and replacement services are based upon the terms of the contracts with the U.S. government which have been filed with the commissions in the states in which ASUS's subsidiaries are incorporated.

The tables below set forth information relating to GSWC's operating segments, ASUS and its subsidiaries and other matters. Total assets by segment are not presented below, as certain of Registrant's assets are not tracked by segment. The utility plants are net of respective accumulated provisions for depreciation. Capital additions reflect capital expenditures paid in cash and exclude government-funded capital expenditures for ASUS and property installed by developers and conveyed to GSWC.

(dollars in thousands)	As Of And For The Year Ended December 31, 2014				
	GSWC		ASUS	AWR	Consolidated
	Water	Electric	Contracts (2)	Parent	AWR
Operating revenues	\$ 326,672	\$ 34,387	\$ 104,732	\$ —	\$ 465,791
Operating income (loss)	94,014	5,728	19,351	(48)	119,045
Interest expense, net	19,370	1,260	142	(82)	20,690
Utility Plant	953,678	45,202	4,640	—	1,003,520
Depreciation and amortization expense (1)	38,388	1,466	1,219	—	41,073
Income tax expense/(benefit)	30,410	1,596	7,038	(996)	38,048
Capital additions	66,304	4,584	1,665	—	72,553

(dollars in thousands)	As Of And For The Year Ended December 31, 2013				
	GSWC		ASUS	AWR	Consolidated
	Water	Electric	Contracts	Parent	AWR
Operating revenues	\$ 320,131	\$ 38,409	\$ 113,537	\$ —	\$ 472,077
Operating income (loss)	95,932	6,411	16,737	(8)	119,072
Interest expense, net	20,236	1,436	264	(228)	21,708
Utility Plant	936,386	40,908	4,183	—	981,477
Depreciation and amortization expense (1)	36,636	2,316	1,138	—	40,090
Income tax expense/(benefit)	30,679	2,455	4,911	(2,262)	35,783
Capital additions	94,581	2,124	674	—	97,379

(dollars in thousands)	As Of And For The Year Ended December 31, 2012				
	GSWC		ASUS	AWR	Consolidated
	Water	Electric	Contracts	Parent	AWR
Operating revenues	\$ 305,898	\$ 37,033	\$ 123,977	\$ —	\$ 466,908
Operating income (loss)	78,104	8,501	24,608	(119)	111,094
Interest expense, net	19,783	1,533	179	(63)	21,432
Utility Plant	871,756	41,381	4,654	—	917,791
Depreciation and amortization expense (1)	37,905	2,292	1,188	—	41,385
Income tax expense	24,231	2,269	9,437	8	35,945
Capital additions	62,500	4,331	1,273	—	68,104

**AMERICAN STATES WATER COMPANY AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

The following table reconciles total utility plant (a key figure for rate-making) to total consolidated assets (in thousands):

	December 31,		
	2014	2013	2012
Total utility plant	\$ 1,003,520	\$ 981,477	\$ 917,791
Other assets	374,778	328,706	363,152
Total consolidated assets	\$ 1,378,298	\$ 1,310,183	\$ 1,280,943

- (1) Depreciation computed on GSWC's transportation equipment is recorded in other operating expenses and totaled \$678,000, \$877,000 and \$1.8 million for the years ended December 31, 2014, 2013 and 2012, respectively.
- (2) ASUS recorded approximately \$1.6 million of additional revenues during the fourth quarter of 2014 in conjunction with the close-out of a large construction project.

**Note 17 — Allowance for Doubtful Accounts**

The table below presents Registrant's provision for doubtful accounts charged to expense and accounts written off, net of recoveries. Provisions included in 2014, 2013 and 2012 for AWR and GSWC are as follows:

(dollars in thousands)	AWR		
	December 31,		
	2014	2013	2012
Balance at beginning of year	\$ 1,187	\$ 1,228	\$ 1,048
Provision charged to expense	991	1,145	1,710
Accounts written off, net of recoveries	(1,286)	(1,186)	(1,530)
Balance at end of year	\$ 892	\$ 1,187	\$ 1,228
Allowance for doubtful accounts related to accounts receivable-customer	\$ 803	\$ 755	\$ 797
Allowance for doubtful accounts related to receivable from U.S. government	—	—	8
Allowance for doubtful accounts related to other accounts receivable	89	432	423
Total allowance for doubtful accounts	\$ 892	\$ 1,187	\$ 1,228
	<b>GSWC</b>		
	December 31,		
	2014	2013	2012
Balance at beginning of year	\$ 1,114	\$ 1,177	\$ 1,005
Provision charged to expense	1,055	1,056	1,668
Accounts written off, net of recoveries	(1,277)	(1,119)	(1,496)
Balance at end of year	\$ 892	\$ 1,114	\$ 1,177
Allowance for doubtful accounts related to accounts receivable-customer	\$ 803	\$ 755	\$ 797
Allowance for doubtful accounts related to other accounts receivable	89	359	380
Total allowance for doubtful accounts	\$ 892	\$ 1,114	\$ 1,177

**AMERICAN STATES WATER COMPANY AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 18 — Supplemental Cash Flow Information**

The following table sets forth non-cash financing and investing activities and other cash flow information (in thousands).

	AWR			GSWC		
	December 31,			December 31,		
	2014	2013	2012	2014	2013	2012
<b>Taxes and Interest Paid:</b>						
Income taxes paid	\$ 15,984	\$ 10,880	\$ 19,411	\$ 16,500	\$ 7,083	\$ 11,027
Interest paid, net of capitalized interest	22,236	22,144	22,495	22,184	22,144	22,495
<b>Non-Cash Transactions:</b>						
Accrued payables for investment in utility plant	\$ 13,147	\$ 19,515	\$ 12,113	\$ 13,141	\$ 19,515	\$ 12,113
Property installed by developers and conveyed	800	2,819	2,069	800	2,819	2,069

## Report of Independent Registered Public Accounting Firm

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

In our opinion, the consolidated financial statements listed in the accompanying index present fairly, in all material respects, the financial position of American States Water Company and its subsidiaries (“the Company”) at December 31, 2014 and December 31, 2013, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2014 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in Item 15(a)(2) presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on criteria established in *Internal Control - Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for these financial statements and financial statement schedule, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in Management's Report on Internal Control over Financial Reporting under Item 9A. Our responsibility is to express opinions on these financial statements, on the financial statement schedule, and on the Company's internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

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

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

/s/ PricewaterhouseCoopers LLP  
Los Angeles, California  
February 25, 2015

## **Report of Independent Registered Public Accounting Firm**

To the Board of Directors and  
Shareholder of Golden State Water Company

In our opinion, the financial statements listed in the accompanying index present fairly, in all material respects, the financial position of Golden State Water Company (the “Company”) at December 31, 2014 and December 31, 2013, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2014 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP  
Los Angeles, California  
February 25, 2015

## Report from Management on the Responsibility for Financial Statements

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

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

Registrant's independent registered public accounting firm, PricewaterhouseCoopers LLP, is engaged to audit the consolidated financial statements included in this report in accordance with the standards of the Public Company Accounting Oversight Board (United States) and to express an opinion on whether those consolidated financial statements fairly present, in all material respects, Registrant's results of operations, financial position and cash flows. In addition, the effectiveness of AWR's internal control over financial reporting as of December 31, 2014 has been audited by PricewaterhouseCoopers LLP. The result of their work is expressed in their Report of Independent Registered Public Accounting Firm.

/s/ ROBERT J. SPROWLS

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Robert J. Sprowls  
President and Chief Executive Officer

/s/ EVA G. TANG

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Eva G. Tang  
Chief Financial Officer,  
Senior Vice President - Finance,  
Treasurer and Corporate Secretary

February 25, 2015

### Selected Quarterly Financial Data (Unaudited)

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

(in thousands, except per share amounts)	AWR				
	For The Year Ended December 31, 2014				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter (1)	Year
Operating revenues	\$ 101,945	\$ 115,641	\$ 138,327	\$ 109,878	\$ 465,791
Operating income	22,768	31,000	39,895	25,382	119,045
Net income	11,021	15,354	21,171	13,512	61,058
Basic earnings per share*	0.28	0.39	0.54	0.35	1.57
Diluted earnings per share *	0.28	0.39	0.54	0.35	1.57

(in thousands)	GSWC				
	For The Year Ended December 31, 2014				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Operating revenues	\$ 81,213	\$ 94,560	\$ 105,314	\$ 79,972	\$ 361,059
Operating income	20,430	28,575	32,346	18,391	99,742
Net income	9,347	13,456	16,079	8,975	47,857

(in thousands, except per share amounts)	AWR				
	For The Year Ended December 31, 2013				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Operating revenues	\$ 110,552	\$ 120,695	\$ 130,914	\$ 109,916	\$ 472,077
Operating income	27,963	33,294	36,164	21,651	119,072
Net income	13,465	16,602	20,839	11,780	62,686
Basic earnings per share	0.34	0.43	0.54	0.30	1.61
Diluted earnings per share*	0.34	0.43	0.53	0.30	1.61

(in thousands)	GSWC				
	For The Year Ended December 31, 2013				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Operating revenues	\$ 79,967	\$ 92,466	\$ 102,781	\$ 83,326	\$ 358,540
Operating income	23,596	28,958	32,284	17,505	102,343
Net income	10,705	13,814	16,613	7,510	48,642

\* The sum of the quarterly 2014 basic earnings per share amounts and the 2013 and 2014 diluted earnings per share amounts do not agree to the yearly totals due to rounding.

- (1) ASUS recorded approximately \$1.6 million of additional revenues during the fourth quarter of 2014 in conjunction with the close-out of a large construction project.



## **Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

### **Item 9A. Controls and Procedures**

#### **(a) Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures**

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) or 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Based on this evaluation, our principal executive officer and our principal financial officer concluded that the disclosure controls and procedures of AWR and GSWC were effective as of the end of the period covered by this annual report.

#### **(b) Management’s Report on Internal Control over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control - Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our evaluation under the framework in *Internal Control - Integrated Framework*, our management concluded that the internal control over financial reporting of AWR and GSWC was effective as of December 31, 2014.

#### **(c) Attestation Report of the Independent Registered Public Accounting Firm**

The effectiveness of our internal control over financial reporting of AWR as of December 31, 2014 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which is included herein.

#### **(d) Changes in Internal Control over Financial Reporting**

There have been no changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) or 15d(f) under the Exchange Act) of AWR and GSWC that occurred during the fourth quarter of 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

### **Item 9B. Other Information**

None.

## PART III

### Item 10. Directors, Executive Officers and Corporate Governance

Information responsive to Part III, Item 10 is included in the Proxy Statement, to be filed by AWR with the SEC pursuant to Regulation 14A, under the captions therein entitled: (i) “Proposal 1: Election of Directors”; (ii) “Executive Officers”; (iii) “Governance of the Company”; (iv) “Stock Ownership”; (v) “Nominating and Governance Committee”; (vi) “Audit and Finance Committee;” and (vii) “Obtaining Additional Information From Us” and is incorporated herein by reference pursuant to General Instruction G(3).

### Item 11. Executive Compensation

Information responsive to Part III, Item 11 is included in the Proxy Statement, to be filed by AWR with the SEC pursuant to Regulation 14A, under the captions therein entitled: (i) “Proposal 1: Election of Directors”; (ii) “Executive Officers;” and (iii) “Compensation Committee” and is incorporated herein by reference pursuant to General Instruction G(3).

### Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Information responsive to Part III, Item 12 is included in the Proxy Statement, to be filed by AWR with the SEC pursuant to Regulation 14A, under the caption entitled “Stock Ownership”, and is incorporated herein by reference pursuant to General Instruction G(3).

### Securities Authorized for Issuance under Equity Compensation Plans

AWR has made stock awards to its executive officers and managers under the 2000 Stock Incentive Plan and the 2008 Stock Incentive Plan. It has also made stock awards to its non-employee directors under the 2003 Non-Employee Directors Stock Plan and the 2013 Non-Employee Directors Plan. Information regarding the securities which have been issued and which are available for issuance under these plans is set forth in the table below as of December 31, 2014. This table does not include any Common Shares that may be issued under our 401(k) plan.

<u>Plan Category</u>	<u>(a) (1) Number of securities to be issued upon exercise of outstanding options, warrants and rights</u>	<u>(b)(1) Weighted-average exercise price of outstanding options, warrants and rights</u>	<u>(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in</u>
Equity compensation plans approved by shareholders	222,580	\$ 17.47	2,025,567
Equity compensation plans not approved by shareholders	—	—	—
Total	222,580	\$ 17.47	2,025,567

(1) Amounts shown in columns (a) and (b) are only for options granted. At December 31, 2014, there were 85,759 restricted stock units outstanding that had been granted to employees under the 2000 and 2008 employee plans, and 59,716 restricted stock units outstanding that had been granted to directors under the directors’ plans. There was also a target amount totaling 75,827 performance awards in the form of restricted stock units granted to the officers of AWR and its subsidiaries under the 2008 employee plan. Each grantee of any outstanding performance award may earn between 0% and 200% of the target amount depending on Registrant’s performance against the performance goals. Each restricted stock unit was issued with dividend equivalent rights until the restricted stock unit vests or is terminated earlier pursuant to the terms of the grant. Each performance award was issued with dividend equivalent rights with respect to the performance awards that will be determined by the Compensation Committee of the Board of Directors to have been earned as of the end of the performance period. We may not grant restricted stock units with respect to more than 1,000,000 of our Common Shares under the 2013 directors plan. No additional grants may be made under either the 2000 employee plan or the 2003 directors plan.

### Item 13. Certain Relationships and Related Transactions, and Director Independence

Information responsive to Part III, Item 13 is included in the Proxy Statement, to be filed by AWR with the SEC pursuant to Regulation 14A, under the caption therein entitled “Governance of the Company” and is incorporated herein by reference pursuant to General Instruction G(3).

### Item 14. Principal Accounting Fees and Services

Information responsive to Part III, Item 14 is included in the Proxy Statement, to be filed by AWR with the SEC pursuant to Regulation 14A, under the caption therein entitled “Proposal 4: Ratification of Auditors” and is incorporated herein by reference pursuant to General Instruction G(3).

## PART IV

### **Item 15. Exhibits, Financial Statement Schedules**

**(a) The following documents are filed as a part of this Annual Report on Form 10-K:**

1. Reference is made to the Financial Statements incorporated herein by reference to Part II, Item 8 hereof.
2. Schedule I — Condensed Financial Information of AWR. Schedules II, III, IV, and V are omitted as they are not applicable.
3. Reference is made to Item 15(b) of this Annual Report on Form 10-K.

**(b) Exhibits:**

- 3.1 By-Laws of American States Water Company incorporated by reference to Exhibit 3.1 of Registrant's Form 8-K, filed May 13, 2011
- 3.2 By-laws of Golden State Water Company incorporated by reference to Exhibit 3.1 of Registrant's Form 8-K filed May 13, 2011
- 3.3 Amended and Restated Articles of Incorporation of American States Water Company incorporated by reference to Exhibit 3.1 of Registrant's Form 8-K filed June 19, 2013 (File No. 1-14431)
- 3.4 Restated Articles of Incorporation of Golden State Water Company, as amended, incorporated herein by reference to Exhibit 3.1 of Registrant's Form 10-Q for the quarter ended September 30, 2005 (File No. 1-14431)
- 4.1 Indenture, dated September 1, 1993 between Golden State Water Company and The Bank of New York Mellon Trust Company, N.A., as successor trustee, as supplemented, incorporated herein by reference to Exhibit 4.01 of Golden State Water Company Form S-3 filed December 12, 2008
- 4.2 Note Purchase Agreement dated as of October 11, 2005 between Golden State Water Company and Co-Bank, ACB incorporated by reference to Exhibit 4.1 of Registrant's Form 8-K filed October 13, 2005 (File No. 1-14431)
- 4.3 Note Purchase Agreement dated as of March 10, 2009 between Golden State Water Company and Co-Bank, ACB, incorporated herein by reference to Exhibit 10.16 to Registrant's Form 10-K filed on March 13, 2009
- 4.4 Indenture dated as of December 1, 1998 between American States Water Company and The Bank of New York Mellon Trust Company, N.A., as supplemented by the First Supplemental Indenture dated as of July 31, 2009 incorporated herein by reference to Exhibit 4.1 of American States Water Company's Form 10-Q for the quarter ended June 30, 2009
- 10.1 Second Sublease dated October 5, 1984 between Golden State Water Company and Three Valleys Municipal Water District incorporated herein by reference to Registrant's Registration Statement on Form S-2, Registration No. 33-5151
- 10.2 Note Agreement dated as of May 15, 1991 between Golden State Water Company and Transamerica Occidental Life Insurance Company incorporated herein by reference to Registrant's Form 10-Q with respect to the quarter ended June 30, 1991 (File No. 1-14431)
- 10.3 Schedule of omitted Note Agreements, dated May 15, 1991, between Golden State Water Company and Transamerica Annuity Life Insurance Company, and Golden State Water Company and First Colony Life Insurance Company incorporated herein by reference to Registrant's Form 10-Q with respect to the quarter ended June 30, 1991 (File No. 1-14431)
- 10.4 Loan Agreement between California Pollution Control Financing Authority and Golden State Water Company, dated as of December 1, 1996 incorporated by reference to Exhibit 10.7 of Registrant's Form 10-K for the year ended December 31, 1998 (File No. 1-14431)
- 10.5 Agreement for Financing Capital Improvement dated as of June 2, 1992 between Golden State Water Company and Three Valleys Municipal Water District incorporated herein by reference to Registrant's Form 10-K with respect to the year ended December 31, 1992 (File No. 1-14431)

- 10.6 Water Supply Agreement dated as of June 1, 1994 between Golden State Water Company and Central Coast Water Authority incorporated herein by reference to Exhibit 10.15 of Registrant's Form 10-K with respect to the year ended December 31, 1994 (File No. 1-14431)
- 10.7 2003 Non-Employee Directors Stock Purchase Plan, as amended, incorporated herein by reference to Exhibit 10.1 to Registrant's Form 8-K filed on January 30, 2009 (2)
- 10.8 Dividend Reinvestment and Common Share Purchase Plan incorporated herein by reference to American States Water Company Registrant's Form S-3D filed November 12, 2008
- 10.90 Form of Amended and Restated Change in Control Agreement between American States Water Company or a subsidiary and certain executives incorporated herein by reference to Exhibit 10.4 to Registrant's Form 8-K filed on November 11, 2014 (2)
- 10.1 Golden State Water Company Pension Restoration Plan, as amended, incorporated herein by reference to Exhibit 10.1 to the Registrant's Form 8-K filed on May 21, 2009 (2)
- 10.11 American States Water Company 2000 Stock Incentive Plan, as amended, incorporated by reference to Exhibit 10.2 of Registrant's Form 8-K filed May 23, 2008 (2)
- 10.12 Amended and Restated Credit Agreement between American States Water Company dated June 3, 2005 with Wells Fargo Bank, N.A., as Administrative Agent, as amended, incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K filed March 27, 2014
- 10.13 Form of Indemnification Agreement for executive officers incorporated by reference to Exhibit 10.21 to Registrant's Form 10-K for the year ended December 31, 2006 (File No. 1-14431) (2)
- 10.14 Form of Non-Qualified Stock Option Plan Agreement for officers and key employees for the 2000 Stock Incentive Plan incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K filed on January 7, 2005 (File No. 1-14431) (2)
- 10.15 Form of Non-Qualified Stock Option Plan Agreement for officers and key employees for the 2000 Stock Incentive Plan incorporated by reference to Exhibit 10.1 of Registrant's Form 10-Q for the period ended March 31, 2006 (File No. 1-14431) (2)
- 10.16 Form of Director's Non-Qualified Stock Option Agreement incorporated by reference to Exhibit 10.1 to Registrant's Form 10-Q for the period ended September 30, 2006 (File No. 1-14431) (2)
- 10.17 Form of Restricted Stock Unit Award Agreement for officers and key employees under the 2008 Stock Incentive Plan for restricted stock unit awards prior to January 1, 2011 but before January 1, 2015 incorporated by reference to Exhibit 10.4 of Registrant's Form 8-K filed on November 5, 2008 (2)
- 10.18 2008 Stock Incentive Plan, as amended, incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K filed March 21, 2014 (2)
- 10.19 Form of Nonqualified Stock Option Agreement for officers and key employees for the 2008 Stock Incentive Plan incorporated herein by reference to Exhibit 10.3 to Registrant's Form 8-K filed November 21, 2014 (2)
- 10.20 Policy Regarding the Recoupment of Certain Performance-Based Compensation Payments incorporated herein by reference to Exhibit 10.3 to the Registrant's Form 8-K filed on April 2, 2014 (2)
- 10.21 Performance Incentive Plan incorporated herein by reference to Exhibit 10.4 to the Registrant's Form 8-K filed on July 31, 2009 (2)
- 10.22 Officer Relocation Policy incorporated herein by reference to Exhibit 10.5 to the Registrant's Form 8-K filed on July 31, 2009 (2)
- 10.23 Form of Non-Qualified Stock Option Award Agreement for officers and key employees under the 2008 Stock Incentive Plan for stock options granted after December 31, 2010 but prior to January 1, 2015 incorporated by reference to Exhibit 10.2 of Registrant's Form 8-K filed on February 4, 2011 (2)
- 10.24 Form of Restricted Stock Unit Award Agreement for officers and key employees under the 2008 Stock Incentive Plan for restricted stock unit awards after December 31, 2010 but prior to January 1, 2015 incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K filed on February 4, 2011 (2)
- 10.25 Performance Award Agreement for Robert J. Spowls, dated as of May 29, 2012, incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K dated June 4, 2012 (2)
- 10.26 Form of Indemnification Agreement for directors incorporated by reference to Exhibit 10.35 to Registrant's Form 10-K for the period ended December 31, 2012 (1)(2)
- 10.27 2013 Short-Term Incentive Program incorporated by reference herein to Exhibit 10.1 to Registrant's Form 8-K filed on March 28, 2013 (2)

- 10.28 Form of 2013 Short-Term Incentive Award Agreement incorporated by reference to Exhibit 10.2 to the Registrant's Form 8-K filed March 28, 2013 (2)
- 10.29 Form of 2013 Performance Award Agreement incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K filed on March 15, 2013 (2)
- 10.30 Form of 2014 Performance Award Agreement incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K filed January 1, 2014 (2)
- 10.31 2013 Non-Employee Directors Plan incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K filed May 22, 2014 (2)
- 10.32 2014 Short-Term Incentive Program incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K filed on April 2, 2014 (2)
- 10.33 Form of 2014 Short-Term Incentive Agreement incorporated by reference to Exhibit 10.2 to Registrant's Form 8-K filed April 2, 2014 (2)
- 10.34 Form of Restricted Stock Unit Agreement for grants after December 31, 2014 incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K filed November 21, 2014 (2)
- 10.35 Form of 2015 Performance Award Agreement incorporated by reference to Exhibit 10.1 to Registrant's Form 8-K filed January 30, 2015 (2)
- 21 Subsidiaries of Registrant (1)
- 23.1 Consent of Independent Registered Public Accounting Firm for AWR (1)
- 23.1.1 Consent of Independent Registered Public Accounting Firm for GSWC (1)
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for AWR (1)
- 31.1.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for GSWC (1)
- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for AWR (1)
- 31.2.1 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for GSWC (1)
- 32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (3)
- 32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (3)
- 101.INS XBRL Instance Document (3)
- 101.SCH XBRL Taxonomy Extension Schema (3)
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase (3)
- 101.DEF XBRL Taxonomy Extension Definition Linkbase (3)
- 101.LAB XBRL Taxonomy Extension Label Linkbase (3)
- 101.PRE XBRL Taxonomy Extension Presentation Linkbase (3)

**(c) See Item 15(a)(2)**

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

**SIGNATURES**

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

**AMERICAN STATES WATER COMPANY (“AWR”):**

By: /s/ EVA G. TANG

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Eva G. Tang  
Senior Vice President-Finance, Chief Financial  
Officer, Treasurer and Corporate Secretary

**GOLDEN STATE WATER COMPANY (“GSWC”):**

By: /s/ EVA G. TANG

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Eva G. Tang  
Senior Vice President-Finance, Chief Financial  
Officer and Secretary

Date: February 25, 2015

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

Date:

/s/ LLOYD E. ROSS

Lloyd E. Ross  
Chairman of the Board and Director of AWR and GSWC

February 25, 2015

/s/ ROBERT J. SPROWLS

Robert J. Sprowls  
Principal Executive Officer, President and Chief Executive Officer of AWR and GSWC and Director of AWR and GSWC

February 25, 2015

/s/ EVA G. TANG

Eva G. Tang  
Principal Financial and Accounting Officer, Senior Vice President-Finance, Chief Financial Officer, Treasurer and Corporate Secretary of AWR; and Principal Financial and Accounting Officer, Senior Vice President-Finance, Chief Financial Officer and Secretary of GSWC

February 25, 2015

/s/ JAMES L. ANDERSON

James L. Anderson  
Director of AWR and GSWC

February 25, 2015

/s/SARAH. J. ANDERSON

Sarah. J. Anderson  
Director of AWR and GSWC

February 25, 2015

/s/ DIANA M. BONTÁ

Diana M. Bontá  
Director of AWR and GSWC

February 25, 2015

/s/ JOHN R. FIELDER

John R. Fielder  
Director of AWR and GSWC

February 25, 2015

/s/ ANNE M. HOLLOWAY

Anne M. Holloway  
Director of AWR and GSWC

February 25, 2015

/s/ JAMES F. MCNULTY

James F. McNulty  
Director of AWR and GSWC

February 25, 2015

/s/ JANICE F. WILKINS

Janice F. Wilkins  
Director of AWR and GSWC

February 25, 2015

**AMERICAN STATES WATER COMPANY**  
**SCHEDULE 1 - CONDENSED FINANCIAL INFORMATION OF PARENT**

**CONDENSED BALANCE SHEET**

(in thousands)	December 31,	
	2014	2013
<b>Assets</b>		
Cash and equivalents	\$ 31,629	\$ 107
Inter-company note receivables	1,445	21,113
Deferred tax assets	503	388
Income taxes receivable and other receivables	44	1,733
Total current assets	33,621	23,341
Investments in subsidiaries	478,677	468,568
Other assets	4,948	3,364
Total assets	\$ 517,246	\$ 495,273
<b>Liabilities and Capitalization</b>		
Note payable to GSWC	\$ —	\$ 500
Income taxes payable	9,902	1,851
Deferred taxes and other liabilities	154	84
Total current liabilities	10,056	2,435
Deferred taxes	100	146
Income taxes payable and other liabilities	289	288
Total other liabilities	389	434
Common shareholders' equity	506,801	492,404
Total capitalization	506,801	492,404
Total liabilities and capitalization	\$ 517,246	\$ 495,273

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



**AMERICAN STATES WATER COMPANY**  
**SCHEDULE 1 - CONDENSED FINANCIAL INFORMATION OF PARENT**

**CONDENSED STATEMENTS OF INCOME**

(In thousands, except per share amounts)	For the Years Ended December 31,		
	2014	2013	2012
Operating revenues and other income	\$ 81	\$ 227	\$ 64
Operating expenses and other expenses	48	8	120
Income (loss) before equity in earnings of subsidiaries and income taxes	33	219	(56)
Equity in earnings of subsidiaries	60,029	60,205	54,212
Income before income taxes	60,062	60,424	54,156
Income tax expense (benefit)	(996)	(2,262)	8
Net income	\$ 61,058	\$ 62,686	\$ 54,148
Weighted Average Number of Common Shares Outstanding	38,658	38,639	37,998
Basic Earnings Per Common Share	\$ 1.57	\$ 1.61	\$ 1.42
Weighted Average Number of Diluted Common Shares Outstanding	38,880	38,869	38,262
Fully Diluted Earnings per Common Share	\$ 1.57	\$ 1.61	\$ 1.41

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

**AMERICAN STATES WATER COMPANY**  
**SCHEDULE 1 - CONDENSED FINANCIAL INFORMATION OF PARENT**

**CONDENSED STATEMENTS OF CASH FLOWS**

(in thousands)	For the Years Ended December 31,		
	2014	2013	2012
Cash Flows From Operating Activities	\$ 61,092	\$ 32,645	\$ 16,885
Cash Flows From Investing Activities:			
Loans (made to)/repaid from, wholly-owned subsidiaries	19,668	(6,100)	(4,720)
Net cash provided (used) in investing activities	19,668	(6,100)	(4,720)
Cash Flows From Financing Activities:			
Repurchase of Common Shares	(17,180)	—	—
Proceeds from note payable to GSWC	8,300	18,236	—
Repayment of note payable to GSWC	(8,800)	(17,736)	—
Proceeds from stock option exercises	589	2,111	13,295
Net change in notes payable to banks	—	—	(2,000)
Dividends paid	(32,111)	(29,360)	(24,130)
Other	(36)	—	—
Net cash used in financing activities	(49,238)	(26,749)	(12,835)
Change in cash and equivalents	31,522	(204)	(670)
Cash and equivalents at beginning of period	107	311	981
Cash and equivalents at the end of period	\$ 31,629	\$ 107	\$ 311

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

**AMERICAN STATES WATER COMPANY**  
**NOTES TO CONDENSED FINANCIAL INFORMATION OF PARENT**

**Note 1 — Basis of Presentation**

The accompanying condensed financial statements of AWR (parent) should be read in conjunction with the consolidated financial statements and notes thereto of American States Water Company and subsidiaries (“Registrant”) included in Part II, Item 8 of this Form 10-K. AWR’s (parent) significant accounting policies are consistent with those of Registrant and its wholly-owned subsidiaries, Golden State Water Company (“GSWC”) and American States Utility Services, Inc. (“ASUS”), except that all subsidiaries are accounted for as equity method investments.

**Related Party Transactions:**

As further discussed in *Note 2 — Notes Payable to Banks*, AWR (parent) has access to a \$100.0 million syndicated credit facility. AWR (parent) borrows under this facility and provides funds to its subsidiaries, in support of their operations. Any amounts owed to AWR (parent) for borrowings under this facility are reflected as inter-company receivables on the condensed balance sheets. The interest rate charged to the subsidiaries is sufficient to cover AWR (parent)’s interest cost under the credit facility.

During 2013, AWR (parent) issued an interest bearing promissory note (the “Note”) to GSWC for \$20.0 million which expires on May 23, 2018. Under the terms of the Note, AWR (parent) may borrow from GSWC amounts up to \$20.0 million for working capital purposes. As of December 31, 2014, no amounts were outstanding under this Note.

AWR (parent) guarantees performance of ASUS’s military privatization contracts and agrees to provide necessary resources, including financing, which are necessary to assure the complete and satisfactory performance of such contracts.

**Note 2 — Note Payable to Banks**

AWR (parent) has access to a syndicated credit facility which was amended on May 23, 2013 to, among other things, extend the expiration date of the syndicated credit facility to May 23, 2018, reduce the amount of interest and fees paid by AWR, and update certain representations and covenants in the credit agreement. AWR may, under the terms of the fourth amendment, elect to increase the aggregate commitment by up to an additional \$50.0 million. The aggregate effective amount that may be outstanding under letters of credit is \$25.0 million. AWR has obtained letters of credit, primarily for GSWC, in the aggregate amount of \$11.2 million, with fees of 0.65% including: (i) a \$6.7 million letter of credit representing a percentage of the outstanding American Recovery and Reinvestment Act (“ARRA”) funds received by GSWC for reimbursement of capital costs related to the installation of meters in GSWC’s Arden-Cordova water system; (ii) letters of credit, in an aggregate amount of \$340,000 as security for GSWC’s business automobile insurance policy; (iii) a letter of credit, in an amount of \$585,000 as security for the purchase of power; (iv) a \$15,000 irrevocable letter of credit pursuant to a franchise agreement with the City of Rancho Cordova, and (v) an irrevocable letter of credit in the amount of \$3.6 million, pursuant to a settlement agreement with Southern California Edison Company to cover GSWC’s commitment to pay the settlement amount. Letters of credit outstanding reduce the amount that may be borrowed under the revolving credit facility. There were no compensating balances required.

Loans can be obtained at the option of AWR and bear interest at rates based on credit ratings and Euro rate margins. In July 2014, Standard & Poor’s Ratings Services (“S&P”) revised its rating outlook on AWR from stable to positive. S&P also affirmed the ‘A+’ corporate credit rating on AWR. S&P debt ratings range from AAA (highest rating possible) to D (obligation is in default).

At December 31, 2014, there were no borrowings outstanding under this facility. At times, AWR (parent) borrows under this facility and provides loans to its subsidiaries in support of its operations, under terms that are similar to that of the credit facility.

AWR’s (parent) short-term borrowing activities (excluding letters of credit) for the last three years were as follows:

<b>(in thousands, except percent)</b>	<b>December 31,</b>		
	<b>2014</b>	<b>2013</b>	<b>2012</b>
Balance Outstanding at December 31,	\$ —	\$ —	\$ —
Interest Rate at December 31,	0.82%	0.82%	1.41%
Average Amount Outstanding	\$ 6,181	\$ —	\$ 885
Weighted Average Annual Interest Rate	0.81%	1.02%	1.49%
Maximum Amount Outstanding	\$ 24,000	\$ —	\$ 6,000

**AMERICAN STATES WATER COMPANY**  
**NOTES TO CONDENSED FINANCIAL INFORMATION OF PARENT**

All of the letters of credit are issued pursuant to the syndicated revolving credit facility. The syndicated revolving credit facility contains restrictions on prepayments, disposition 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 from Moody's or S&P of Baa3 or BBB-, respectively. As of December 31, 2014, AWR was in compliance with these covenants with an interest coverage ratio of 7.52 times interest expense, a debt ratio of 0.40 to 1.00 and a debt rating of A+.

**Note 3 — Income Taxes**

AWR (parent) receives a tax benefit for expenses incurred at the parent-company level. AWR (parent) also recognizes the effect of AWR's consolidated California unitary apportionment, which is beneficial or detrimental depending on a combination of the profitability of AWR's consolidated non-California activities as well as the proportion of its consolidated California sales to total sales.

During the year ended December 31, 2013, AWR (parent) recorded a cumulative tax benefit of \$1.5 million related to an employee benefit plan for deductions taken on recently filed tax returns and amounts taken, and to be taken, on amended income tax returns.

**Note 4 — Dividend from Subsidiaries**

Dividends in the amount of \$52.0 million, \$29.4 million and \$16.9 million were paid to AWR (parent) by its wholly-owned subsidiaries during the years ended December 31, 2014, 2013 and 2012, respectively.

**BOARD OF DIRECTORS**

AMERICAN STATES WATER COMPANY  
AND GOLDEN STATE WATER  
COMPANY

**Lloyd E. Ross**  
(Chairman of the Board of Directors)  
Director since 1995  
Non-voting ex-officio member  
of all committees

**James L. Anderson (A,B)**  
(Chairperson of the Compensation  
Committee)  
Senior Vice President  
Americo Life Inc.  
Director since 1997

**Sarah J. Anderson (C)**  
(Chairperson of the Audit & Finance  
Committee)  
Retired, Partner  
Ernst & Young LLP  
Director since 2012

**Diana M. Bontá (A,B)**  
President & CEO  
The Bontá Group  
Director since 2007

**John R. Fielder (C,D)**  
Retired, President  
Southern California Edison Company  
Director since 2013

**Anne M. Holloway (A,B)**  
(Chairperson of the Nominating  
& Governance Committee)  
Director since 1998

**James F. McNulty (A,D)**  
(Chairperson of the ASUS Committee)  
Retired, Chairman & CEO  
Parsons Corporation  
Director since 2010

**Janice F. Wilkins (C,D)**  
Retired, Vice President of Finance  
and Director of Internal Audit  
Intel Corporation  
Director since 2011

**Robert J. Sprowls (D)**  
President and Chief Executive Officer  
Director since 2009

- (A) Member – Compensation Committee
- (B) Member – Nominating & Governance
- (C) Member – Audit & Finance Committee
- (D) Member – ASUS Committee

**OFFICERS**

AMERICAN STATES WATER COMPANY

**Robert J. Sprowls (10)**  
President and Chief Executive Officer

**Eva G. Tang (18)**  
Senior Vice President – Finance,  
Chief Financial Officer, Corporate  
Secretary and Treasurer

**Gladys M. Farrow (12)**  
Assistant Secretary

**OFFICERS**

GOLDEN STATE WATER COMPANY

**Robert J. Sprowls (10)**  
President and Chief Executive Officer

**Denise L. Kruger (22)**  
Senior Vice President – Regulated Utilities

**Eva G. Tang (18)**  
Senior Vice President – Finance,  
Chief Financial Officer and Secretary

**Gladys M. Farrow (12)**  
Vice President – Finance, Treasurer  
and Assistant Secretary

**William C. Gedney (17)**  
Vice President – Asset Management

**Patrick R. Scanlon (36)**  
Vice President – Water Operations

**Bryan K. Switzer (14)**  
Vice President – Regulatory Affairs

(#) Years of Service with Corporation

**BOARD OF DIRECTORS**

AMERICAN STATES UTILITY  
SERVICES, INC. AND SUBSIDIARIES:

**James F. McNulty**  
(Chairman of the Board of Directors)  
Director since 2010

**Lloyd E. Ross**  
Director since 1998

**Robert J. Sprowls**  
President and Chief Executive Officer  
Director since 2009

**OFFICERS**

AMERICAN STATES UTILITY  
SERVICES, INC. AND SUBSIDIARIES:

**Robert J. Sprowls (10)**  
President and Chief Executive Officer

**James C. Cotton III (6)**  
Senior Vice President and  
Procurement Officer

**Eva G. Tang (18)**  
Senior Vice President – Finance,  
Chief Financial Officer and Secretary

**James B. Gallagher (27)**  
Vice President – Management Services

**Granville R. Hodges, Jr. (36)**  
Vice President – Operations

**Gladys M. Farrow (12)**  
Treasurer and Assistant Secretary

**FOR INVESTOR INFORMATION  
FROM THE COMPANY**

CALL (877)463-6297 (INFOAWR)  
investorinfo@aswater.com

**SHAREHOLDER ASSISTANCE**

For shareholder questions related to your  
AWR shares, you should contact:

**Computershare Investor Services**  
Attn: Shareholder Relations Dept.  
250 Royal Street  
Canton, MA 02021  
Telephone (888) 816-6998

**ANNUAL MEETING**

10:00 a.m. Pacific Daylight time  
Tuesday, May 19, 2015

**The Langham Hotel**  
1401 South Oak Knoll Ave.,  
Pasadena, California 91106

**INDEPENDENT REGISTERED PUBLIC  
ACCOUNTING FIRM**

PricewaterhouseCoopers, LLP  
601 South Figueroa Street  
Los Angeles, California 90017

**STOCK EXCHANGE**

Common shares of American States Water  
Company are traded on the New York Stock  
Exchange (NYSE) under the symbol AWR.



630 East Foothill Boulevard,  
San Dimas, CA 91773 / 909 . 394 . 3600 / [aswater.com](http://aswater.com)