KENTUCKY-AMERICAN WATER COMPANY
CASE NO. 2004-00103
FORECASTED TEST PERIOD FILING REQUIREMENTS
EXHIBIT NO. 28

Description of Filing Requirement:

Annual Reports to Stockholders, 1999 – 2003

Response:

Please see attached. The Company has not yet completed its stockholders report for 2003. A copy will be provided when available.

For electronic version, see KAW_APP_EX28_043004.pdf

PRICEWATERHOUSECOOPERS

KENTUCKY-AMERICAN WATER COMPANY

Financial Statements and Other Information

December 31,1999 and 1998

KENTUCKY-AMERICAN WATER COMPANY

An American Water System Company
2300 Richmond Road
Lexington, Kentucky 40502

Board of Directors

J. James Barr, President and Chief Executive Officer
American Water Works Company, Inc.

G. C. Smith, Retired Vice President
American Water Works Company, Inc.

Ellen C. Wolf, Vice President and Chief Financial Officer
American Water Works Company, Inc.

Daniel L. Kelleher, Senior Vice President
American Water Works Service Company, Inc.

Chris E. Jarrett, (elected Chairman of the Board)
Kentucky American Water Company, April 2000

R. W. Mundy, II, President
Kentucky-American Water Company

W. L. Rouse, Jr.
Investments

W. T. Young, Jr.
W. T. Young Storage, Inc.

Paul W. Ware
Retired Chairman, Penn Fuel Gas, Inc.
(Retiring from the Board of Directors, April 2000)

Elizabeth H. Gemmill, Esq.
Managing Trustee of the Warwick Foundation

Lindsey W. Ingram, Jr., Esq.
Stoll, Keenon and Park LLP

Officers

President..R W. Mundy, II
Vice President..N. O. Rowe
Vice President & Treasurer..C. D. Bush
Comptroller..E. J. Grubb
Secretary..H. A. Miller, Jr.

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
Thirty South Seventeenth Street
Philadelphia PA 19103-4094
Telephone (215) 575 5000

Report of independent Accountants

To the Board of Directors and Stockholder of
Kentucky-American Water Company

In our opinion, the accompanying balance sheet and the related statements of income and retained earnings, of cash flows, of capitalization and of common stockholder's equity, present fairly, in all material respects, the financial position of Kentucky-American Water Company (a wholly-owned subsidiary of American Water Works Company, Inc.) at December 31, 1999 and 1998, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States. 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 auditing standards generally accepted in the United States which 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 the opinion expressed above.

PricewaterhouseCoopers LLP

January 28, 2000
Philadelphia, Pennsylvania

KENTUCKY-AMERICAN WATER COMPANY
Balance Sheet
(Dollars in thousands)

Assets

	December 31, 1999	December 31, 1998
Property, plant and equipment		
Utility plant - at original cost less accumulated depreciation	$ 183,732	$ 174,619
Utility plant acquisition adjustments, net	185	173
	183,917	174,792
Nonutility property	250	242
current assets		
Cash and cash equivalents	508	1,392
Customer accounts receivable	1,415	1,403
Allowance for uncollectible accounts	(50)	(54)
Unbilied revenues	1,902	1,795
Miscellaneous receivables	828	379
Materials and supplies	524	514
Mher	328	377
	5,455	5,806
Regulatory and other long-term assets		
Regulatory asset - inwme taxes recoverable through rates	4,222	3,883
Deferred programmed maintenance	3,133	3,095
Preliminary survey and investigation	4,154	567
Debt and preferred stock expense	414	457
Other	2,055	1,112
	13,978	9,114
	$ 203,600	$ 189,954

Capitalization end Liabilities

	1999	1998
Capitalization		
Common stock	$ 36,569	$ 36,569
Paid in capital	21	21
Retained earnings	21,686	20,252
Total wmmon stockholder's equity	58,276	56,842
Preferred stock without mandatory redemption requirements	1,570	1,570
Preferred stock with mandatory redemption requirements	5,468	5,516
Long-term debt	63,000	67,000
Total capitalization	128,314	130,928
Current liabilities		
Bank debt-pending issuance of securities	5,716	-
Current portion of long-term debt	4,000	-
Accounts payable	2,686	1,922
Taxes accrued	175	240
interest accrued	832	808
Wages and benefits accrued	352	308
Tax collection payable	236	284
Other	1,187	771
	15,184	4,333
Regulatory and other long-term liabilities		
Customer advances for construction	9,679	8,145
Deferred income taxes	23,594	21,708
Deferred investment tax credits	1,896	1,981
Accrued pension expense	1,472	1,255
Accrued postretirement benefits expense	299	299
Other	457	451
	37,397	33,839
Contributions in aid of construction	22,705	20,854
Commitments and contingencies		
	$ 203,600	$ 189,954

The accompanying notes are an integral part of these financial statements

KENTUCKY-AMERICANWATER COMPANY
Statement of Income
(Dollars in thousands)

	For the Years Ended 1999	1998
Operating revenues	$ 39,104	$ 37,744
Operating expenses		
Operation and maintenance	16,262	15,481
Depreciation and amortization	4,817	4,451
Taxes on operating income		
General	1,711	1,577
State income	1,017	965
Federal income	3,819	3,599
	27,626	26,073
Utility operating income	11,478	11,671
Other income		
Allowance for other funds used during construction	720	394
Miscellaneous other income	62	163
	12,260	12,228
Other deductions		
Miscellaneous other deductions	358	275
Taxes on other income and deductions		
State income	(24)	(8)
Federal income	(92)	(30)
	242	237
Income before interest charges	12,018	11,991
Interest charges		
Interest on long-term debt	5,192	5,205
Amortization of debt expense	42	44
Interest on bank debt	25	87
Other interest	6	6
Allowance for borrowed funds used during construction	(381)	(209)
	4,884	5,133
Net income	$ 7,134	$ 6,858

Statement of Retained Earnings

	1999	1998
Retained earnings at beginning of year	$ 20,252	$ 18,626
Net income	7,134	6,858
	27,386	25,484
Dividends		
Preferred stock	543	547
Common stock	5,157	4,685
	5,700	5,232
Retained earnings at end of year	$ 21,686	$ 20,252

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

KENTUCKY-AMERICAN WATER COMPANY
Statement of Cash Flows
(Dollars in thousands)

	For the Years Ended 1999	1998
Cash flows from operating activities		
Net income	$ 7,134	$ 6,858
Adjustments		
Depreciation and amortization	4,816	4,451
Amortization, other	568	923
Provision for deferred income taxes	1,774	1,599
Amortization of deferred investment tax credits	(85)	(85)
Provision for losses on accounts receivable	151	173
Deferred programmed maintenance	(338)	(430)
Allowance for other funds used during construction	(720)	(394)
Pension accrual in excess of funding	217	199
Other, net	(1,035)	(397)
Changes in current assets and liabilities		
Accounts receivable	(167)	(131)
Unbilied revenues	(107)	26
Other current assets	(409)	(420)
Accounts payable	764	415
Taxes accrued	47	88
Other current liabilities	436	(646)
Net cash provided by operating activities	13,046	12,229
Cash flows from investing activities		
Construction expenditures	(18,386)	(14,137)
Allowance for other funds used during construction	720	394
Cost of removal, net of salvage	(158)	(175)
Water system acquisition		(483)
Net cash used in investing activities	(17,824)	(14,401)
Cash flows from financing activities		
Proceeds from sale of common stock	-	6,000
Proceeds from long-term debt issuance		9,000
Repayment of long-term debt		(6,000)
Net repayment under line-of-credit agreement	5,716	(3,248)
Dividends paid	(5,700)	(5,232)
Customer advances and contributions, net of refunds	3,926	2,721
Debt issuance cost	-	(95)
Redemption of preferred stock	(48)	(48)
Net cash provided by financing activities	3,894	3,098
Net increase in cash and cash equivalents	(884)	926
Cash and cash equivalents at beginning of year	1,392	466
Cash and cash equivalents at end of year	$ 508	$ 1,392
Cash paid during the year for:		
Interest, net of capitalized amount	$ 4,818	$ 5,244
Income taxes	$ 2,996	$ 3,086

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

KENTUCKY-AMERICAN WATER COMPANY
Statement of Capitalization
(Dollars in thousands)

	Call Price Per Share	December 31, 1999	1998
Common Stockholder's Equity			
Common stock - no par value, authorized 2,000,000 shares, issued and outstanding 1,567,391 shares in 1999 and 1998, respectively		$ 36,569	$ 36,569
Paid-in capital		21	21
Retained earnings		21,686	20,252
		58,276	56,842
Preferred Stocks - $100 par value, authorized 25,000 shares			
Without mandatory redemption requirements			
Cumulative preferred stock			
5.75% series, 4.700 shares	$ 101.00	470	470
5.5% series, 5,000 shares	$ 100.50	500	500
5% series, 6.000 shares	$ 100.00	600	600
		1.570	1,570
With mandatory redemption requirements			
Cumulative preferred stock 80 and 160 shares issued and outstanding			
4.5% series, 80 and 160 shares outstanding in 1999 and 1998 respectively	$ 101.00	8	16
7.9% series, 9,600 and 10,000 shares issued and outstanding in 1999 and 1998, respectively	$ 100.00	960	1,000
8.47% series. 45.000 shares issued and outstanding	$ 100.00	4,500	4,500
		5,468	5,516
Long-Term Debt			
General mortgage bonds.			
9.83% series due 2000		4,000	4,000
8.36% series due 2001		13,000	13,000
7.21% series due 2002		13,000	13,000
6.79% series due 2005		5,500	5,500
9.37% series due 2019		8,000	8,000
6.96% series due 2023		7,000	7,000
7.15% series due 2027		7,500	7,500
6.99% series due 2028		9,000	9,000
		67,000	67,000
Less: Current portion of long-term debt		4,000	-
Long-term debt net of current maturities		63,000	67,000
Total capitalization		$ 128.314	$ 130,928

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

KENTUCKY-AMERICAN WATER COMPANY
Statement of Common Stockholder's Equity
(Dollars in thousands, except per share amounts)

	Common Stock		Paid-in	Retained	Common Stockholder's
	Shares	par value	Capital	Earnings	Equity
Balance at December 31,1997	1,397,082	$ 30,569	$ 21	$ 18,626	$ 49,216
Net income	-	-	-	6,858	6,858
Sale of common stock	170,309	6,000	-	-	6,000
Dividends					
Preferred stock	-	-	-	(547)	(547)
Common stock, $2.99 per share	-	-	-	(4,685)	(4,685)
Balance at December 31,1998	1,567,391	36,569	21	20,252	56,842
Net income	-	-	-	7,134	7,134
Dividends					
Preferred stock	-	-	-	(543)	(543)
Common stock, $3.29 per share	-	-	-	(5,157)	(5,157)
Balance at December 31,1999	1,567,391	$ 36,569	$ 21	$ 21,686	$ 58,276

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

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements
(Dollars in thousands, except per share amounts)

Note 1 - Organization and Operation

Kentucky-American Water Company (the Company) provides water service to approximately 96,000 customers and wastewater service to approximately 80 customers. These services are provided in 7 communities located in 7 counties in the state of Kentucky. As a public utility operating in Kentucky, the Company operates under rules and regulations prescribed by the Kentucky Public Service Commission (the Commission). The Company is a wholly-owned subsidiary of American Water Works Company, Inc. (American).

Note 2 - Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Actual results could differ from these estimates.

Regulation

The Company has incurred various costs and received various credits which have been reflected as regulatory assets and liabilities on its balance sheet. Accounting for such costs and credits as regulatory assets and liabilities is in accordance with Statement of Financial Accounting Standards No. 71, "Accounting for the Effects of Certain Types of Regulation" (SFAS No. 71). This statement sets forth the application of generally accepted accounting principles for companies whose rates are established by or are subject to approval by an independent third-party regulator. Under SFAS No. 71, regulated companies defer costs and credits on the balance sheet as regulatory assets and liabilities when it is probable that those costs and credits will be recognized in the rate setting 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.

Property, Plant and Equipment

Additions to utility plant and replacements of retirement units of property are capitalized. Costs include material, direct labor and such indirect items as engineering and supervision, payroll taxes and benefits, transportation and an allowance for funds used during construction. Repairs, maintenance and minor replacements of property are charged to current operations. The

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands, except per share amounts)

cost of property units retired in the ordinary course of business plus removal cost (net of salvage) is charged to accumulated depreciation. The cost of property, plant and equipment is depreciated using the straight line method. The depreciation rates, based on the average balance of depreciable property, were 2.54% in 1999 and 2.50% in 1998.

In accordance with the Commission's regulations, depreciation on contributed facilities is charged to contributions in aid of construction. Such depreciation amounted to $542 in 1999 and $488 in 1998.

Utility plant acquisition adjustments include the difference between the purchase price of utility plant and its original cost (less accumulated depreciation) when first devoted to public service. Commission approved utility plant acquisition adjustments have been amortized to income over 10 years.

Cash and Cash Equivalents

Substantially all of the Company's cash is invested in interest bearing accounts. The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. Cash equivalents held at December 31, 1999 were $0 and 1998 were $996.

Materials and Supplies

Materials and supplies are stated at average cost.

Regulatory and Other Long-Term Assets

The Company has recorded a regulatory asset for the additional revenues expected to be realized as the tax effects of temporary differences previously flowed through to customers reverse. These temporary differences are primarily related to the difference between book and tax depreciation on property placed in service before the adoption by the Commission of full normalization for rate making purposes. The regulatory assets for income taxes recoverable through rates is net of the reduction expected in future revenues as deferred taxes previously provided, attributable to the difference between the state and federal income tax rates under prior law and the current statutory rates, teverse over the average remaining service lives of the related assets.

Programmed maintenance costs are deferred and amortized to current operations on a straight-line basis over a period ranging between 5 and 15 years, as authorized by the Commission in their determination of rates charged for service.

Expense of rate proceedings is deferred and amortized on a straight-line basis over two years as authorized.by the Commission in their determination of rates charged for service.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands, except per share amounts)

Preliminary survey and investigation charges generally relate to future construction projects. Management believes that these costs will ultimately be recovered through rates.

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

Other Current Liabilities

Other current liabilities at December 31, 1999 and 1998 include payables to banks of $634 and $146, respectively which represent checks issued but not presented to the banks for payment, net of the related bank balance.

Advances and Contributions in Aid of Construction

The Company may receive advances and contributions to fund construction necessary to extend service to new areas. As determined by the Commission, advances for construction are refundable for limited periods of time as new customers begin to receive service. Amounts which are no longer refundable are reclassified to contributions in aid of construction.

Utility plant funded by contributions is excluded from rate base and is not depreciated for rate-making purposes. Generally, advances and contributions received during the period of January 1,1987 through June 12,1996 have been included in taxable income and the related property is depreciable for tax purposes. As a result of a tax law change, advances and contributions received subsequent to June 12, 1996 are excluded from taxable income.

Recognition of Revenues

Water service revenues for financial reporting purposes include amounts billed to customers on a cycle basis and unbilled amounts based on estimated usage from the date of the latest meter reading to the end of the accounting period.

Income Taxes

The Company, American and affiliates participate in a consolidated federal income tax return. Federal income tax expense for financial reporting purposes is provided on a separate return basis, except that the federal income tax rate applicable to the consolidated group is applied to separate company taxable income and the benefit of net operating losses, if any, is recognized currently.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands, except per share amounts)

Certain income and expense items are accounted for in different time periods for financial reporting than for income tax reporting purposes. Deferred income taxes have been provided on the difference between the tax basis of assets and liabilities and the amounts at which they are carried in the financial statements. These deferred income taxes are based on the enacted tax rates anticipated to be in effect when such temporary differences are expected to reverse. Regulatory assets and liabilities are recognized for the effect on revenues expected to be realized as the tax effects of temporary differences previously flowed through to customers reverse.

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

Allowance for Funds Used During Construction (AFUDC)

AFUDC is a noncash adjustment to income with a corresponding charge to utility plant which represents the cost of borrowed funds and a return on equity funds devoted to plant under construction. AFUDC is recorded to the extent permitted by the Commission.

Environmental Costs

Environmental expenditures that relate to current operations or provide a future benefit are expensed or capitalized, as appropriate. Remediation costs that relate to an existing condition caused by past operations are accrued when it is probable that these costs will be incurred and can be reasonably estimated. There were no remediation costs accrued at December 31, 1999 or 1998.

Asset Impairment

Long-lived assets and certain identifiable intangible assets held and used by the Company are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets, on a separate entity basis, may not be recoverable. If the sum of the future cash flows expected to result from the use of the assets and their eventual disposition is less than the carrying amount of the assets, an impairment loss is recognized. Measurement of an impairment loss is based on the fair value of the assets. A regulatory asset is charged to earnings if and when future recovery in rates of that asset is no longer probable.

Reclassifications

Certain reclassifications have been made to conform previously reported data to the current presentation.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands, except per share amounts)

Note 3 - Utility Plant

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

	1999	1998
Water plant		
Sources of supply	$ 6,777	$ 6,778
Treatment and pumping	43,738	41,747
Transmission and distribution	110,753	102,848
Services, meters, and fire hydrants	39,775	36,752
General structures and equipment	14,513	13,066
Construction work in progress	6,774	8,400
	222,330	209,591
Less - accumulated depreciation	(38,598)	(34,972)
	$ 183,732	$ 174,619

Note 4 - Preferred Stocks

Preferred stock agreements have annual sinking fund payments of $48 in 2000 and $40 in 2001 through 2004. The sinking fund payments on the 4.5% series of $8 is mandatory. The 7.9% series sinking fund payment of $40 is at the option of the Company.

Preferred stock agreements contain provisions for redemption at various prices on thirty days notice at the Company's discretion, except for the 8.47% series which is not callable prior to December 1,2001.

In the event of voluntary liquidation of the Company, the 5.5% series is redeemable at $100.50 per share; the other issues are redeemable at $100 per share.

In the event of involuntary liquidation of the Company, or government acquisition, all classes of preferred stocks are redeemable at $100 per share. All of the outstanding shares of the 8.47% series shall be redeemed on December 1,2036 at $100 per share.

Note 5 - Long-Term Debt

Maturities of long-term debt will amount to $4,000 in 2000, $13,000 in 2001, $13,000 in 2002 and zero in 2003 and 2004.

The general mortgage bond indentures contain clauses restricting the declaration of common stock dividends and other distributions on capital stock if common stockholder's equity falls below a specified amount. There were no restrictions at December 31, 1999.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands, except per share amounts)

The general mortgage bonds are issuable in series. No bonds senior to the general mortgage bonds may be issued so long as general mortgage bonds are outstanding. The amount of bonds authorized is unlimited as long as long-term debt does not exceed 65% of capitalization. Long-term debt is secured by utility plant.

Note 6 - Compensating Balances and Bank Debt

At December 31, 1999 the Company maintained a bank line of credit of $13,840. The total of the unused line of credit at December 31, 1999 was $8,124. The Company has historically financed short-term cash requirements by borrowings from banks which are repaid with the proceeds of long-term financings. Borrowings under this line of credit are payable on demand and bear interest at variable rates. The agreement with the bank has no compensating balance requirement.

The maximum amount of short-term bank borrowings outstanding during 1999 was $5,716, and the average amount outstanding during the year was $367. The weighted average annual interest rate on these borrowings during 1999 was 6.7%, and the interest rate at December 31, 1999 was 6.25%.

Note 7 - Financings

During 1998 the Company completed the following financings:

Date	Proceeds	Issue
6/17/98	$3,000	General mortgage bonds, 6.99% series due 6/1/28
6/17/98	$6,000	General mortgage bonds, 6.99% series due 6/1/28
6/17/98	$6,000	Common stock, 170,309 shares, no par value

The general mortgage bonds were sold to institutional investors at a price equal to the principal amount. The common stock was issued to American.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)

(Dollars in thousands, except per share amounts)

Note 8 - General Taxes

Components of general tax expense for the years presented in the statement of income are as follows:

	1999	1998
Gross receipts and franchise	$ 65	$ 66
Property and capital stock	1,198	1,089
Payroll	448	422
	$ 1,711	$ 1,577

Note 9 - Income Taxes

Components of income tax expense for the years presented in the statement of income are as follows:

	1999	1998
State income taxes:		
Current	$ 592	$ 586
Deferred		
Non-current	401	371
	$ 993	$ 957
Federal income taxes:		
Current	$ 2,439	$ 2,426
Deferred		
Current	4	1
Non-current	1,369	1,227
Amortization of deferred investment tax credits	(85)	(85)
	$ 3,727	$ 3,569

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands, except per share amounts)

A reconciliation of income tax expense at the statutory federal income tax rate to the actual income tax expense is as follows:

	1999	1998
Income tax at statutory rate	$4,149	$ 3,984
Increases (decreases) resulting from		
State taxes, net of federal income taxes	646	622
Flow through differences	44	31
Amortization of investment tax credits	(85)	(85)
Other, net	(34)	(26)
Actual income tax expense	$4,720	$4,526

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

	1999	1998
Deferred tax assets:		
Advances and contributions	$ 12,883	$ 11,517
Deferred investment credits	765	800
Other	875	822
	$ 14,523	$ 13,139
Deferred tax liabilities:		
Utility plant, principally due to depreciation differences	34,686	31,697
Income taxes recoverable through rates	1,704	1,567
other	1,727	1,583
	$ 38,117	$ 34,847
Net deferred tax liabilities	$23,594	$ 21,708

No valuation allowances were required on deferred **tax** assets at December 31, 1999 and 1998.

Note 10 - Rate Matters

As necessary, the Company applies to the Commission for changes in the rates charged for service. The rate increase request is based on the level of operating expenses and capital costs that are expected to be in effect when the rates become effective. The revenues requested are based on forcasted sales, operating expenses and investments for the test year selected by the Company.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)

(Dollars in thousands, except per share amounts)

Note 11 - Employee Benefit Plans

Employees' Stock Ownership Plan

The Company participates in an Employees' Stock Ownership Plan which provides for beneficial ownership of American common stock by all employees of American and its subsidiaries who are not represented by a bargaining unit. Each participating employee can elect to contribute an amount that does not exceed 2% of his or her wages for the preceding year. In addition to the employee's participation, the Company makes a contribution equivalent to 112 of 1% of each participant's qualified compensation for the preceding year and matches 100% of the contribution by each participant. The Company expensed contributions of $54 in 1999 and $56 for 1998 that it made to the plan. The trustee of the plan may purchase shares of American common stock from American at the prevailing market price, on the open market, or from a qualified stockholder.

Savings Plan for Employees

The Company participates in a 401(k) Savings Plan for Employees sponsored by American. All Associates can make contributions that are invested at the direction of the employee in one or more funds including a fund consisting entirely of American common stock. During 1999 and 1998, the Company matched 50% of the first 4% of each employee's wages contributed to the plan. The Company expensed matching contributions to the plan totaling $82 for 1999 and $84 for 1998. All of the Company's matching contributions are invested in the fund of American common stock. The trustee of the plan may purchase shares of American common stock from American at the prevailing market price from American, on the open market, or in a private transaction.

Note 12 - Postretirement and Postemployment Benefits

Pension Benefits

The Company participates in a noncontributory defined benefit pension plan covering substantially all employees of American and its subsidiaries. Benefits under the plan are based on the employee's years of service and average annual compensation for those 60 consecutive months of employment which yield the highest average. Pension cost of the Company is based on an allocation from American of the total cost related to the plan. Information regarding accumulated and projected benefit obligations is not prepared at the subsidiary level. The Company's policy is to contribute at least the minimum amount required under the Employee Retirement Income Security Act of 1974. The Company made no contributions to the plan in 1999 or 1998. The Company accrued pension costs of $217 in 1999 and $199 in 1998.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands, except per share amounts)

Postretirement Benefits Other Than Pensions

The Company participates in an American plan that provides certain life insurance benefits for retired employees and certain health care benefits for retired employees and their dependents. Substantially all employees may become eligible for these benefits if they reach retirement age while still working for the Company. Retirees and their dependents under age 65 can elect either a comprehensive medical plan under which covered expenses are paid at 80% after an annual deductible has been satisfied or, a managed care plan that requires copayments. Employees who elect to retire prior to attaining age 65 are required to make contributions toward their medical coverage until attaining age 65. Retirees and their dependents age 65 and over are covered by a Medicare supplement plan. Costs to the Company for postretirement benefits other than pensions are based on an allocation from American of the total cost related to the plan. Information regarding accumulated and projected benefit obligations is not prepared at the subsidiary level. The Company made contributions to trust funds established for these postretirement benefits of $578 in 1999 and $478 in 1998. The Company's policy is to fund postretirement benefits costs accrued.

Note 13 - Related Party Transactions

American Water Works Service Company, Inc. (Service Company), an affiliate, provides certain management services to the Company (administration, accounting, data processing, engineering, etc.) and other operating water companies in the American Water Works System on an at-cost, not-for-profit basis in accordance with a management and service agreement. Purchases of such services by the Company were accounted for as follows:

	1999	1998
Included in operation and maintenance expense as a charge against income	$ 931	$ 963
Capitalized in various balance sheet accounts	236	212
	$ 1,167	$ 1,175

The Company has three operating agreements with American Anglian Environmental Technologies, Inc. (AAET), an affiliate, for the lease of granular activated carbon at one of the Company's water treatment plants. The agreements provide for AAET to regenerate the spent carbon and return it to the water treatment plant where it originated. Under the terms of the agreement, AAET will provide carbon for a period of thirty-six months beginning in March 1997, 1998 and 1999. The carbon is scheduled for replacement at thirty-six month intervals and is warranted to perform to specific standards during that period. The Company paid $74 in 1999 and $69 in 1998 under these agreements.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands, except per share amounts)

Note 14 - Fair Values of Financial Instruments

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

Current assets and current liabilities: The carrying amount reported in the balance sheet for current assets and current liabilities approximates their fair value.

Preferred stocks with mandatory redemption requirements and long-term debt: The fair values of the Company's preferred stocks with mandatory redemption requirements and long-term debt are estimated using discounted cash flow analyses based on the Company's current incremental financing rates for similar types of securities.

The carrying amounts and fair values of the Company's financial instruments at December 31 are as follows:

	1999		1998	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Preferred stock with mandatory redemption requirements	$ 5,468	$ 5,118	$ 5,516	$ 6,237
Long-term debt, including current maturities	67,000	62,701	67,000	70,902

Note 15 - Operating Leases

The Company has entered into operating leases involving certain equipment. Rental expenses under operating leases were $85 for 1999 and $93 for 1998. The operating leases for the equipment expire over the next 5 years. Certain leases have renewal options from one year to the useful life of the equipment.

At December 31, 1999, the minimum annual future rental commitments under operating leases that have initial or remaining noncancellable lease terms in excess of one year are $84 in 2000, $68 in 2001 and $47 in 2002, $3 in 2003 and $2 in 2004.

Note 16 - Commitments and Contingencies

The Company's construction program for 2000 is estimated to cost approximately $13,250. Commitments have been made in connection with certain projects included in this program.

The Company is routinely involved in legal actions. In the opinion of management, none of these matters will have a material adverse effect, if any, on the financial position, results of operations or cash flows of the Company.

Kentucky-American Water Company

Other Information

Report of Independent Accountants

To the Board of Directors and Stockholder of
Kentucky-American Water Company

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying Historical Review is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information, except for that portion marked "unaudited," on which we express no opinion, has been subjected to auditing procedures applied in the audit of the basic financial statements; and, in our opinion, the information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

January 28,2000
Philadelphia, Pennsylvania

Kentucky-American Water Company
Historical Review
(Dollars in thousands, except per customer amounts)
For the Years Ended December 31, 1999

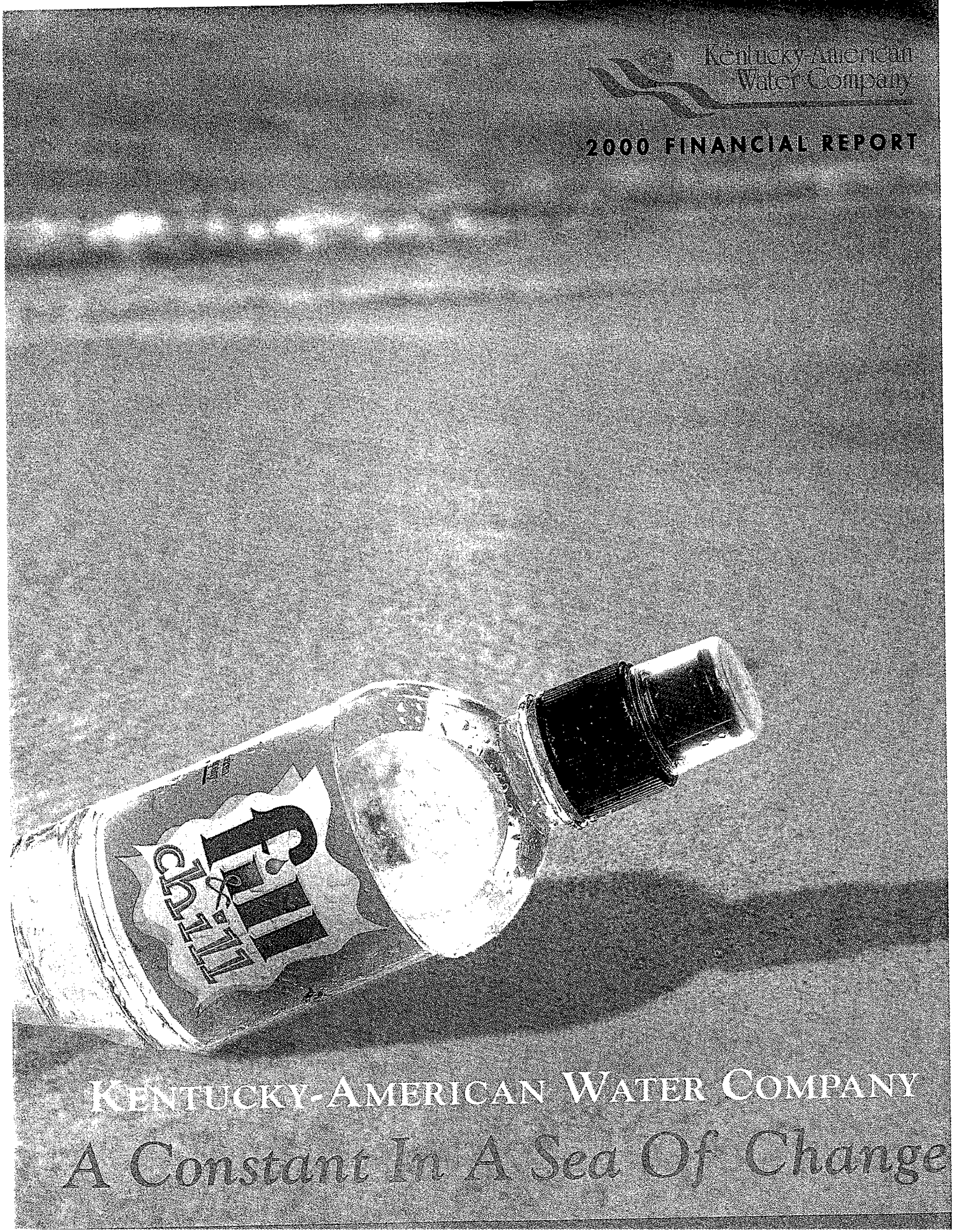
	1999	1998	1997	1996	1995	1994	1989
Utility plant (excluding CWIP)	$ 215,556	$ 201,191	$ 191,534	$ 178,692	$ 164,133	$ 158,001	$ 116,922
Accumulated depreciation	(38,597)	(34,972)	(30,895)	(27,669)	(24,908)	(22,071)	(13,343)
Net utility plant	$ 176,959	$ 166,219	$ 160,639	$ 151,023	$ 139,225	$ 135,930	$ 103,579
Net plant per customer*	$ 1,806	$ 1,787	$ 1,785	$ 1,736	$ 1,657	$ 1,638	$ 1,387
Construction expenditures	$ 18,386	$ 14,137	$ 12,721	$ 12,949	$ 12,532	$ 9,249	$ 8,757
Total assets	$ 203,600	$ 189,954	$ 178,479	$ 170,509	$ 161,861	$ 151,788	$ 112,559
Capitalization at year end							
Common equity	$ 58,276	$ 56,842	$ 49,216	$ 45,394	$ 44,112	$ 39,316	$ 26,984
Preferred stock	7,038	7,086	7,134	7,182	7,230	7,278	3,518
Long-term debt -							
includes current portion	67,000	67,000	64,000	62,500	62,500	60,000	46,280
	$ 132,314	$ 130,928	$ 120,350	$ 115,076	$ 113,842	$ 106,594	$ 76,782
Customers served							
Residential *	87	84	81	78	76	75	67
Commercial *	8	8	7	7	7	7	7
Industrial *	-	-	1	1	-	-	-
Fire service *	1	1	1	1	1	1	1
	96	93	90	87	84	83	75
Water sales (gallons)							
Residential *	5,959	5,720	5,357	5,584	5,339	5,295	4,601
Commercial *	4,336	4,251	4,075	4,181	4,120	4,199	3,640
Industrial *	1,067	1,144	1,081	981	981	905	783
Public and other*	1,998	1,860	1,759	1,772	1,780	1,801	1,651
	13,360	12,975	12,272	12,518	12,220	12,200	10,675
Annual tales per customer (gallons)'	139	140	136	144	145	147	143
Operating revenues							
Water service							
Residential	$ 19,534	$ 18,866	$ 17,437	$ 16,083	$ 15,709	$ 15,014	$ 10,344
Commercial	10,302	10,063	9,451	9,126	9,125	8,899	5,189
Industrial	1,728	1,848	1,704	1,596	1,591	1,425	828
Fire service	2,446	2,368	2,281	2,171	2,115	1,990	1,602
Public and other	4,050	3,057	2,945	3,244	3,235	3,116	1,901
Wastewater service	28	29	-	-	-	-	-
Other water revenues	1,016	1,513	1,431	444	312	199	151
	$ 39,104	$ 37,744	$ 35,249	$ 32,664	$ 32,087	$ 30,643	$ 20,015
Annual revenue per customer*	$ 407	$ 406	$ 392	$ 375	$ 382	$ 369	$ 268
Net income	$ 7,134	$ 6,858	$ 6,047	$ 5,437	$ 5,357	$ 4,607	$ 2.130
Coverage ratios							
On long-term debt interest before income taxes *	3.2	3.2	3.0	2.7	2.7	2.5	2.0
On total interest before income taxes*	3.1	3.1	2.9	2.8	2.6	2.4	1.7
On total R e d charges including preferred dividends							
Before income taxes *	2.8	2.8	2.6	2.5	2.4	2.2	1.6
After income taxes *	2.0	2.0	1.9	1.9	1.8	1.7	1.3

* Unaudited

Exhibit 28

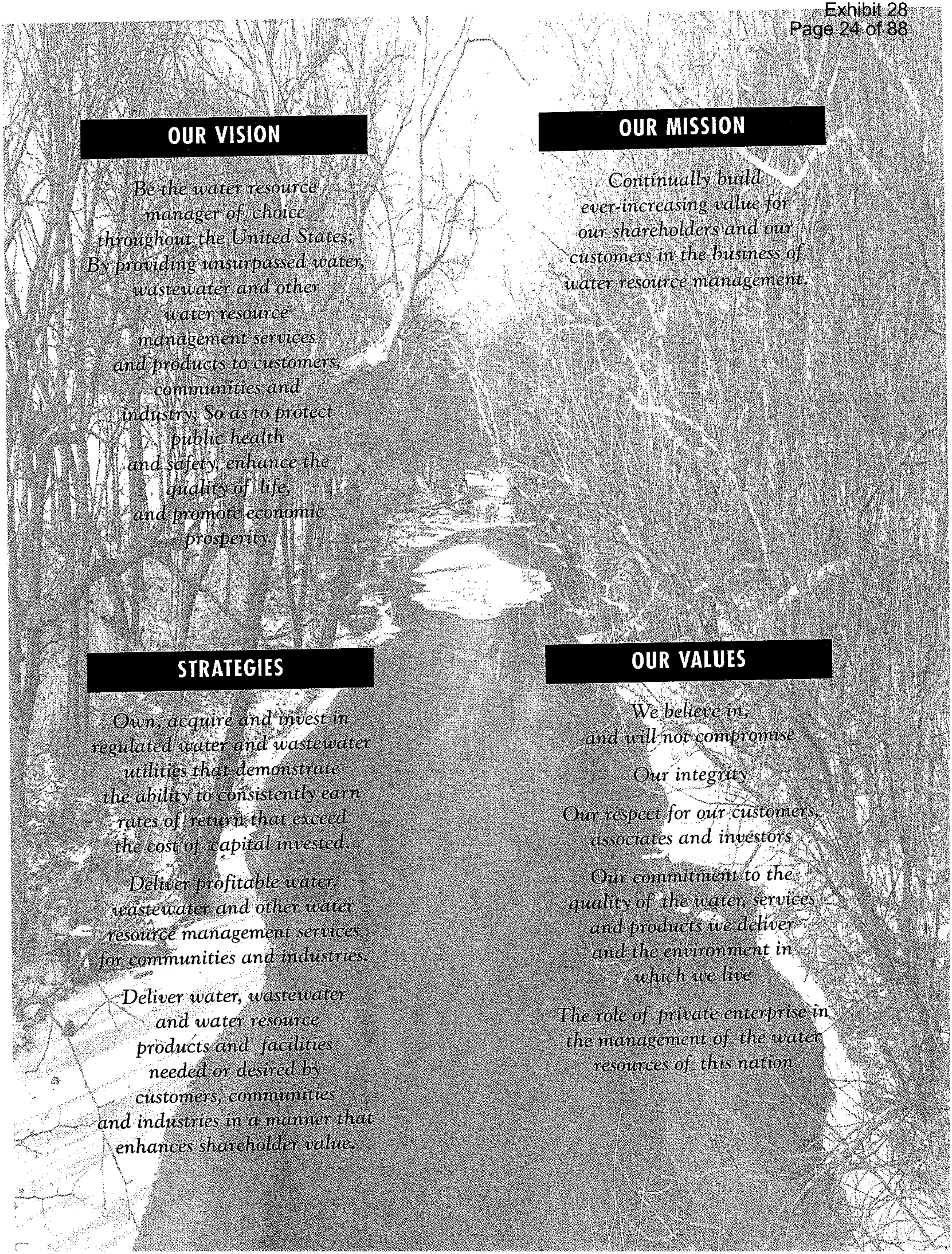
Kentucky-American Water Company

2000 FINANCIAL REPORT



KENTUCKY-AMERICAN WATER COMPANY

A Constant In A Sea Of Change



OUR VISION

Be the water resource manager of choice throughout the United States; By providing unsurpassed water, wastewater and other water resource management services and products to customers, communities and industry; So as to protect public health and safety, enhance the quality of life, and promote economic prosperity.

OUR MISSION

Continually build ever-increasing value for our shareholders and our customers in the business of water resource management.

STRATEGIES

Own, acquire and invest in regulated water and wastewater utilities that demonstrate the ability to consistently earn rates of return that exceed the cost of capital invested.

Deliver profitable water, wastewater and other water resource management services for communities and industries.

Deliver water, wastewater and water resource products and facilities needed or desired by customers, communities and industries in a manner that enhances shareholder value.

OUR VALUES

We believe in, and will not compromise

Our integrity

Our respect for our customers, associates and investors

Our commitment to the quality of the water, services and products we deliver and the environment in which we live

The role of private enterprise in the management of the water resources of this nation.

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and Stockholder of
Kentucky-American Water Company

In our opinion, the accompanying balance sheet and the related statements of income and retained earnings, of cash flows, of capitalization and of common stockholder's equity, present fairly, in all material respects, the financial position of Kentucky-American Water Company (a wholly-owned subsidiary of American Water Works Company, Inc.) at December 31, 2000 and 1999, and the results of its operations and its cash flows for the years then ended 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 auditing standards generally accepted in the United States of America which 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.

PricewaterhouseCoopers LLP

January 29, 2001
Philadelphia, Pennsylvania

KENTUCKY-AMERICAN WATER COMPANY

An American Water Works Company
2300 Richmond Road
Lexington, Kentucky 40502

BOARD OF DIRECTORS

J. James Barr, President and Chief Executive Officer
American Water Works Company, Inc.

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Managing Trustee of the Warwick Foundation

Lindsey W. Ingram, Jr., Esq.
Stoll, Keenon and Park LLP

Chris E. Jarrett, Chairman of the Board
Kentucky-American Water Company

Daniel L. Kelleher, Senior Vice President
American Water Works Service Company, Inc.

Roy W. Mundy, II, President
Kentucky-American Water Company

W. L. Rouse, Jr.
Rouse Companies

G. C. Smith, Director
American Water Works Company, Inc.

Ellen C. Wolf, Vice President and Chief Financial Officer
American Water Works Company, Inc.

W. T. Young, Jr.
W. T. Young, Inc.

OFFICERS

President	R. W. Mundy, II
Vice President	N. O Rawe
Vice President & Treasurer	C. D. Bush
Comptroller	T R. Bailey
Secretary	H. A Miller, Jr.

FINANCIAL STATEMENTS

KENTUCKY-AMERICAN WATER COMPANY - BALANCE SHEET (DOLLARS IN THOUSANDS)

ASSETS

	December 31, 2000	1999
Property, plant and equipment		
Utility plant - at original cost less accumulated depreciation	$ 189,424	$ 183,732
Utility plant acquisition adjustments, net	138	185
	189,562	183,917
Nonutility property	250	250
Current assets		
Cash and cash equivalents	803	508
Customer accounts receivable	1,768	1,415
Allowance for uncollectible accounts	(56)	(50)
Prepaid Tax	641	165
Unbilled revenues	2,085	1,902
Miscellaneous receivables	356	828
Materials and supplies	431	524
Other	321	328
	6,349	[illegible]
Regulatory and other long-term assets		
Regulatory asset - income taxes recoverable through rotes	4,405	4,222
Deferred programmed maintenance	3,340	3,133
Preliminary survey and investigation	343	4,154
Debt and preferred stock expense	835	414
Other	5,856	2,055
	14,779	13,978
	$ 210,940	$ 203,765

KENTUCKY-AMERICAN WATER COMPANY - BALANCE SHEET (DOLLARS IN THOUSANDS)

CAPITALIZATION AND LIABILITIES

	December 31, 2000	1999
Capitalization		
Common stock	$ 36,569	$ 36,569
Paid-incapital	21	21
Retained earnings	22,730	21,686
Total common stockholder's equity	59,320	58,276
Preferred stock without mandatory redemption requirements	1,570	1,570
Preferred stock with mandatory redemption requirements	5,420	5,468
Long-term debt	42,000	63,000
Total capitalization	108,310	128,314
Current liabilities		
Notes Payable to Affiliated Company	20,830	5,716
Current portion of long-term debt	13,000	4,000
Accounts payable	1,762	1,240
Taxes accrued	242	340
Interest accrued	688	832
Wages and benefits accrued	473	352
Tax collection payable	256	236
Other	421	2,633
	37,672	15,349
Regulatory and other long-term liabilities		
Customer advances for construction	9,795	9,679
Deferred income taxes	27,271	23,594
Deferred investment tax credits	1,811	1,896
Accrued pension expense	977	1,472
Accrued posfretirement benefits expense	299	299
Other	595	457
	40,748	37,397
Contributions in aid of construction	24,210	22,705
	$ 210,940	$ 203,765

The accompanying notes ore on integral port of these financial *statements*.

FINANCIAL STATEMENTS

KENTUCKY-AMERICAN WATER COMPANY - STATEMENT OF INCOME (DOLLARS IN THOUSANDS)

	For the Years Ended 2000	1999
Operating revenues	$ 38,720	$ 39,104
Operating expenses		
Operation and maintenonce	15,467	16,262
Depreciation and amortization	5,184	4,817
Taxes on operating income		
General	1,762	1.71 1
State income	942	1,017
Federal income	3,520	3,819
	26,875	27,626
Utility operating income	11,845	11,478
Other income		
Allowance for other funds used during construction	397	720
Miscellaneous other income	12	62
	12,254	12,260
Other deductions		
Miscellaneous other deductions	1,786	358
Taxes on other income and deductions		
State income	(146)	(24)
Federal income	(568)	(92)
	1,072	242
Income before interest charges	11,182	12,018
Interest charges		
interest on long-term debt	5,123	5,192
Amortization of debt expense	42	42
Interest on bank debt	538	25
Other interest	30	6
Allowance for borrowed funds used during construction	(210)	(381)
	5,523	4,884
Net income	$ 5,659	$ 7,134

STATEMENT OF RETAINED EARNINGS

	2000	1999
Retained earnings at beginning of year	$ 21,686	$ 20,252
Net income	5,659	7,134
	27,345	27,386
Dividends		
Preferred stock	540	543
Common stock	4,075	5,157
	4,6 15	5,700
Retained earnings at end of year	$ 22,730	$ 21,686

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

KENTUCKY-AMERICAN WATER COMPANY - STATEMENT OF CASH FLOWS (DOLLARS IN THOUSANDS)

	For the Years Ended 2000	1999
Cash flows from operating activities		
Net income	$ 5,659	$ 7,134
Adjustments		
Depreciation and omortizotion	5,184	4,817
Amortizotion. other	594	568
Provision for deferred income taxes	3,610	1,774
Amortization of deferred investment tax credits	(85)	(85)
Provision for losses on accounts receivable	201	151
Deferred programmed maintenance	(539)	(338)
Allowance far other funds used during construction	(397)	(720)
Pension accrual in excess of (less than) funding	(495)	217
Other, net	(439)	(1,090)
Changes in current assets and liabilities		
Accounts receivable	(548)	(167)
Unbilled revenuer	(183)	(107)
Other current assets	572	(409)
Accounts payable	522	(682)
Taxes accrued	(98)	100
Other current liabilities	(2,216)	1,883
Net cash provided by operating activities	11,342	13,046
Cash flows from investing activities		
Construction expenditures	(11,829)	(18,386)
Allowance for other funds used during construction	397	720
Cost of removal, net af salvage	313	(158)
Net cash used in inverting activities	(11,119)	(17,824)
Cash flows from financing activities		
Repayment of long-term debt	(12,000)	
Net borrowing under line-okredit agreement	15,114	5,716
Dividends paid	(4,615)	(5,700)
Customer advancer and contributions, net of refunds	1,621	3,926
Redemption of preferred stock	(48)	(48)
Net cash provided by financing activities	72	3,894
Net increase in cash and cash equivalents	295	(884)
Cash and cash equivalents at beginning of yea!	508	1,392
Corh and cash equivalents at end of year	$ 803	$ 508
Cash paid during the year for:		
Interest, net of capitalized amount	$ 5,835	$ 4,818
Income taxes	$ 704	$ 2,996

The accompanying notes ore on integrolport of these finonciol stoternents.

FINANCIAL STATEMENTS

KENTUCKY-AMERICAN WATER COMPANY - STATEMENT OF CAPITALIZATION (DOLLARS IN THOUSANDS)

	Call Price Per Share	December 31, 2000	1999
Common Stockholder's Equity			
Common stock - no par value, authorized 2,000,000 shares, issued and outstanding 1,567,391 shares in 2000 and 1999, respectively		$ 36,569	$ 36,569
Paid-in capital		21	21
Retained earnings		22,730	21,686
		59,320	58,276
Preferred Stocks - $100 par value, authorized 25,000 shares			
Without mandatory redemption requirements			
Cumulative preferred stock			
5.75% series, 4,700 shares	$101.00	470	470
5.5% series, 5,000 shares	$100.50	500	500
5% series, 6,000 shares	$100.00	600	600
		1,570	1,570
With mandatory redemption requirements			
Cumulative preferred stock			
4.5% series, 0 and 80 shares outstanding in 2000 and 1999 respectively	$101.00		8
7.9% series, 9,200 and 9,600 shares issued and outstanding in 2000 and 1999, respectively	$100.00	920	960
8.47% series, 45,000 shares issued and outstanding	$100.00	4,500	4,500
		5,420	5,468
Long-Term Debt			
General mortgage bonds,			
9.83% series due 2000			4,000
8.36% series due 2001		13,000	13,000
7.21% series due 2002		13,000	13,000
6.79% series due 2005		5,500	5,500
9.37% series due 2019		-	8,000
6.96% series due 2023		7,000	7,000
7.15% series due 2027		7,500	7,500
6.99% series due 2028		9,000	9,000
		55,000	67,000
Less: Current portion of long-term debt		13,000	4,000
Long-term debt net of current maturities		42,000	63,000
Total capitalization		$ 108,310	$ 128,314

The accompanying notes are on integral part of these financial statements.

KENTUCKY-AMERICAN WATER COMPANY - STATEMENT OF COMMON STOCKHOLDER'S EQUITY

(DOLLARS IN THOUSANDS, EXCEPI IN SHARE AMOUNTS)

	COMMON STOCK			COMMON	
	Shares	Par Value	Paid-in Capital	Retained earnings	Stockholder's Equity
Balance at December 31, 1998	$1,567,391	$36,569	$ 21	$20,252	$56,842
Net income	-	-	-	7,134	7,134
Sale of common stock	-	-	-	-	-
Dividends					
Preferred stock				(543)	(543)
Common stock, $3.29 per share				(5,157)	(5,157)
Balance at December 31, 1999	1,567,391	36,569	21	21,686	58,276
Net income				5,659	5,659
Dividends					
Preferred stock				(540)	(540)
Common stock, $2.60 per share				(4,075)	(4,075)
Balance at December 31, 2000	$1,567,391	$36,569	$ 21	$22,730	$59,320

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

Notes To Financial Statements (Dollars in thousands, except per share amounts)

NOTE 1 - ORGANIZATION AND OPERATION

Kentucky-American Water Company (the Company) provides water service to approximately 99,000 customers and wastewater service to approximately 87 customers. These services are provided in seven communities located in seven counties in the state of Kentucky. As a public utility operating in Kentucky, the Company operates under rules and regulations prescribed by the Kentucky Public Service Commission (the Commission). The Company is a wholly-owned subsidiary of American Water Works Company, Inc. (American).

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Actual results could differ from these estimates.

Regulation

The Company has incurred various costs and received various credits which have been reflected as regulatory assets and liabilities on its balance sheet. Accounting for such costs and credits as regulatory assets and liabilities is in accordance with Statement of Financial Accounting Standards No. 71, "Accounting for the Effects of Certain Types of Regulation" (SFAS No. 71). This statement sets forth the application of generally accepted accounting principles for companies whose rates are established by or are subject to approval by an independent third-party regulator. Under SFAS No. 71, regulated companies defer costs and credits on the balance sheet as regulatory assets and liabilities when it is probable that those costs and credits will be recognized in the rate setting

Notes To Financial Statements (Dollars in thousands, except per share amounts)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES *(CONTINUED)*

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.

Property, Plant and Equipment

Additions to utility plant and replacements of retirement units of property are capitalized. Costs include material, direct labor and such indirect items as engineering and supervision, payroll taxes and benefits, transportation and an allowance for funds used during construction. Repairs, maintenance and minor replacements of property are charged to current operations. The cost of property units retired in the ordinary course of business plus removal cost (net of salvage) is charged to accumulated depreciation. The cost of property, plant and equipment is depreciated using the straight line method. The depreciation rates, based on the average balance of depreciable property, were 2.61% in 2000 and 2.54% in 1999.

In accordance with the Commission's regulations, depreciation on contributed facilities is charged to contributions in aid of construction. Such depreciation amounted to $580 in 2000 and $542 in 1999.

Utility plant acquisition adjustments include the difference between the purchase price of utility plant and its original cost (less accumulated depreciation) when first devoted to public service. Commission approved utility plant acquisition adjustments have been amortized to income over 10 years.

Cash and Cash Equivalents

Substantially all of the Company's cash is invested in interest bearing accounts. The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. There were no cash equivalents held at December 31,2000 or 1999.

Materials and Supplies

Materials and supplies are stated at average cost.

Regulatory and Other Long-Term Assets

The Company has recorded a regulatory asset for the additional revenues expected to be realized as the tax effects of temporary differences previously flowed through to customers reverse. These temporary differences are primarily related to the difference between book and tax depreciation on property placed in service before the adoption by the Commission of full normalization for rate making purposes. The regulatory assets for income taxes recoverable through rates is net of the reduction expected in future revenues as deferred taxes previously provided, attributable to the difference between the state and federal income tax rates under prior law and the current statutory rates, reverse over the average remaining service lives of the related assets.

Programmed maintenance costs are deferred and amortized to current operations on a straight-line basis over a period ranging between 5 and 15 years, as authorized by the Commission in their determination of rates charged for service.

Preliminary survey and investigation charges generally relate to future construction projects. Management believes that these costs will ultimately be recovered through rates.

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

Other Current Liabilities

Other current liabilities at December 31, 2000 and 1999 include payables to banks of $0 and $634, respectively, which represent checks issued but not presented to the banks for payment, net of the related bank balance.

Notes To Financial Statements (Dollars in thousands, except per share amounts)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Advances and Contributions in Aid of Construction
The Company may receive advances and contributions to fund construction necessary to extend service to new areas. As determined by the Commission, advances for construction are refundable for limited periods of time as new customers begin to receive service. Amounts which are no longer refundable are reclassified to contributions in aid of construction.

Utility plant funded by contributions is excluded from rate base and is not depreciated for rate-making purposes. Generally, advances and contributions received during the period of January 1,1987 through June 12,1996 have been included in taxable income and the related property is depreciable for tax purposes. As a result of a tax law change, advances and contributions received subsequent to June 12, 1996 are excluded from taxable income.

On January 11, 2001, the Internal Revenue Service issued regulations that excluded Lateral service lines from its definition of contributions in aid of construction that are not included in taxable income. These customer connection fees are defined as the cost of installing a connection or service line from the Company's main lines to the lines owned by the customer. The regulations were effective immediately, and the Company is now paying tax on money or property received for these connections.

Recognition of Revenues
Water service revenues for financial reporting purposes include amounts billed to customers on a cycle basis and unbilled amounts based on estimated usage from the date of the latest meter reading to the end of the accounting period.

Income Taxes
The Company, American and affiliates participate in a consolidated federal income tax return. Federal income tax expense for financial reporting purposes is provided on a separate return basis, except that the federal income tax rate applicable to the consolidated group is applied to separate company taxable income and the benefit of net operating losses, if any, is recognized currently.

Certain income and expense items are accounted for in different time periods for financial reporting than for income tax reportingpurposes.Deferred income taxes have been provided on the difference between the tax basis of assets and liabilities and the amounts at which they are carried in the financial statements. These deferred income taxes are based on the enacted tax rates anticipated to be in effect when such temporary differencesare expected to reverse. Regulatory assets and liabilities are recognized for the effect on revenues expected to be realized as the tax effects of temporary differences previously flowed through to customers reverse.

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

Allowance for Funds Used During Construction (AFUDC)
AFUDC is a noncash adjustment to income with a corresponding charge to utility plant which represents the cost of borrowed funds and a return on equity funds devoted to plant under construction. ANDC is recorded to the extent permitted by the Commission.

Environmental Costs
Environmental expenditures that relate to current operations or provide a future benefit are expensed or capitalized, as appropriate. Remediation costs that relate to an existing condition caused by past operations are accrued when it is probable that these costs will be incurred and can be reasonably estimated. There were no remediation costs accrued at December 31, 2000 or 1999.

Asset Impairment
Long-lived assets and certain identifiable intangible assets held and used by the Company are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets, on a separate entity basis, may not be recoverable. If the sum of the future cash flows expected to result from the use

Notes To Financial Statements (Dollars in thousands, except per share amounts)

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

of the assets and their eventual disposition is less than the carrying amount of the assets, an impairment loss is recognized. Measurement of an impairment loss is based on the fair value of the assets. A regulatory asset is charged to earnings if and when future recovery in rates of that asset is no longer probable.

In 2001, the Company will adopt Statement of Financial Accounting Standards No. 133 "Accounting for Derivative Instruments and Hedging Activities" (SFAS 133), as amended. This statement establishes accounting and reporting standards for derivative instruments and hedging activities. SFAS 133 was issued by the Financial Accounting Standards Board (FASB) in June of 1998 and requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value.

This adoption of this new accounting standard is not expected to have a significant effect on the Company's financial position or results or operations. The Company's contracts that meet the definition of a derivative are for normal purchases and normal sales, are expected to result in a physical delivery, and are of quantities expected to be used or sold over a reasonable period in the normal course of business. The Company has no hedging activities.

Reclassifications
Certain reclassifications have been made to conform previously reported data to the current presentation.

NOTE 3 - UTILITY PLANT

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

	2000	1999
Water plant		
Sources of supply	$ 6,914	$ 6,777
Treatment and pumping	44,316	43,738
Transmission and distribution	117,374	110,753
Services, meters, and fire hydrants	42,843	39,775
General structures and equipment	15,430	14,513
Construction work in progress	5,309	6,774
	232,186	222,330
Less - accumulated depreciation	(42,762)	(38,598)
	$189,424	$183,732

NOTE 4 - PREFERRED STOCKS

Preferred stock agreements have annual sinking fund payments of $40 in 2001 through 2005. The 7.9% series sinking fund payment of $40 is at the option of the Company.

Preferred stock agreements contain provisions for redemption at various prices on thirty days notice at the Company's discretion, except for the 8.47% series which is not callable prior to December 1, 2001.

In the event of involuntary liquidation of the Company, or government acquisition, all classes of preferred stocks are redeemable at $100 per share. All of the outstanding shares of the 8.47% series shall be redeemed on December 1, 2036 at $100 per share.

Notes To Financial Statements (Dollars in thousands, except per share amounts)

NOTE 5 - LONG-TERM DEBT

Maturities of long-term debt will amount to $13,000 in 2001 and 2002, $0 in 2003 and 2004, and $5,500 in 2005.

The general mortgage bond indentures contain clauses restricting the declaration of common stock dividends and other distributions on capital stock if common stockholder's equity falls below a specified amount. There were no restrictions at December 31, 2000.

The general mortgage bonds are issuable in series. No bonds senior to the general mortgage bonds may be issued so long as general mortgage bonds are outstanding. The amount of bonds authorized is unlimited as long as long-term debt does not exceed 65% of capitalization. Long-term debt is secured by utility plant.

NOTE 6 - AFFILIATE BORROWINGS AND BANK DEBT

Between January and June of 2000, the Company maintained an uncommitted line of credit with a financial institution and also maintained a line of credit with one bank. On June 29, 2000, the Company eliminated these lines of credit and obtained a line of credit through American Water Capital Corp. (AWCC), an affiliate (see Note 13: Related Party Transaction). AWCC is a special purpose corporation that will serve as the primary funding vehicle for the Company. AWCC has a 364-day $600 million revolving credit agreement with a group of 12 domestic and international banks. No compensating balances are required under the agreement. AWCC may also issue commercial paper, and the revolving credit agreement also supports these borrowings.

At December 31, 2000 and 1999, there were $20,830 and $5,716 of short-term borrowings outstanding, respectively. The weighted average annual interest rate on these borrowings was 6.97% and 6.70%, respectively. The unused line of credit at December 31, 2000 was $1,010.

NOTE 7 - GENERAL TAXES

Components of general tax expense for the years presented in the statement of income are as follows:

	2000	1999
Gross receipts and franchise	$ 80	$ 65
Property and capital stock	1,239	1,198
Payroll	443	448
	$1,762	$1,711

NOTE 8 - INCOME TAXES

Components of income tax expense for the years presented in the statement of income are as follows:

	2000	1999
State income taxes:		
Current	$ 7	$ 592
Deferred	789	401
Non-current	$ 796	$ 993
Federal income taxes:		
Current	$ 216	$ 2,439
Deferred		
Current	-	4
Non-current	2,821	1,369
Amortization of deferred investment tax credits	(85)	(85)
	2,952	3,727

Notes To Financial Statements (Dollars in thousands, except per share amounts)

A reconciliation of income tax expense at the statutory federal income tax rate to the actual income tax expense is as follows:

	2000	1999
Income tax at statutory rate	$ 3,293	$ 4,149
Increases (decreases) resulting from		
State taxes, net of federal income taxes	517	646
Flow through differences	58	44
Amortization of investment tax credits	(85)	(85)
Other, net	(35)	(34)
Actual income tax expense	$3,748	$4,720

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

	2000	1999
Deferred tax assets:		
Advances and contributions	$13,533	$12,883
Deferred investment credits	731	765
Other	648	875
	$14,912	$14,523
Deferred tax liabilities:		
Utility plant, principally due to depreciation differences	36,791	34,686
Income taxes recoverable through rates	1,778	1,704
Other	3,614	1,727
	$42,183	$38,117
Net deferred tax liabilities	$27,271	$23,594

No valuation allowances were required on deferred tax assets at December 31, 2000 and 1999.

NOTE 9 - RATE MATTERS

As necessary, the Company applies to the Commission for changes in the rates charged for service. The rate increase request is based on the level of operating expenses and capital costs that are expected to be in effect when the rates become effective. The revenues requested are based on forecasted sales, operating expenses and investments for the test year selected by the Company.

The Company has received approval from the Commission to increase its rates for service as follows:

Effective Dates	Requested Annual Effect on Revenues	Estimated Annual Effect on Revenues Granted	Estimated Revenue Realized in 2000
11/27/2000	$2,171	$2,171	$208

On April 28, 2000, the Company filed a rate application with the Public Service Commission of the Commonwealth of Kentucky ("Commission"), requesting $5.034 million in additional annual revenues that was subsequently revised to $4.685 million or 11.69%.

On December 12, 2000, the Commission issued an Order adjusting its original Order dated November 27, 2000. The Adjusted Order corrected errors in certain elements of cost of service used in calculating the rates and reduced the approved annual increase from $2.518 million to $2.171 million or an increase in rates of 5.43%.

Both the Company and Attorney General's Office have filed petitions and received Commission approval for rehearing on specific issues, addressed in their respective petitions. The Commission has issued a procedural schedule identifying the time frame for filing; (1) written testimony, (2) submitting requests for information, (3) responding to information requests, (4) requests for a hearing, and (5) written briefs. The written briefs are to be filed no later than April 30, 2001.

The rates, producing the $2.171 million increase in annual revenues, were effective for service rendered on and after November 27, 2000. Revenues realized in 2000 from this increase are estimated at $.208 million.

NOTE 10 - EMPLOYEE BENEFIT PLANS

Employees' Stock Ownership Plan
The Company participates in an Employees' Stock Ownership Plan which provides for beneficial ownership of American common stock by all employees of American and its subsidiaries who are not represented by a bargaining unit. Each participating employee can elect to contribute an amount that does not exceed 2% of his or her wages for the preceding year. In addition to the employee's participation, the Company makes a contribution equivalent to 1/2 of 1% of each participant's qualified compensation for the preceding year and matches 100% of the contribution by each participant. The Company expensed contributions of $69 in 2000 and $54 for 1999 that it made to the plan. The trustee of the plan may purchase shares of American common stock from American at the prevailing market price, on the open market, or from a qualified stockholder.

Savings Plan for Employees
The Company participates in a 401(k) Savings Plan for Employees sponsored by American. All Associates can make contributions that are invested at the direction of the employee in one or more funds including a fund consisting entirely of American common stock. During 2000 and 1999, the Company matched 50% of the first 4% of each employee's wages contributed to the plan. The Company expensed matching contributions to the plan totaling $83 for 2000 and $82 for 1999. All of the Company's matching contributions are invested in the fund of American common stock. The trustee of the plan may purchase shares of American common stock from American at the prevailing market price from American, on the open market, or in a private transaction.

NOTE 11 - POSTRETIREMENT AND POSTEMPLOYMENT BENEFITS

Pension Benefits
The Company participates in a noncontributory defined benefit pension plan covering substantially all employees of American and its subsidiaries. Benefits under the plan are based on the employee's years of service and average annual compensation for those 60 consecutive months of employment which yield the highest average. Pension cost of the Company is based on an allocation from American of the total cost related to the plan. Information regarding accumulated and projected benefit obligations is not prepared at the subsidiary level. The Company's policy is to contribute at least the minimum amount required under the Employee Retirement Income Security Act of 1974. The Company made no contributions to the plan in 2000 or 1999. The Company accrued pension costs of $119 in 2000 and $217 in 1999.

During 2000 the Company recognized a net settlement gain of $523 relating to the transfer of annuities from the Plan to a separate third-party life insurance company.

Postretirement Benefits Other Than Pensions
The Company participates in an American plan that provides certain life insurance benefits for retired employees and certain health care benefits for retired employees and their dependents. Substantially all employees may become eligible for these benefits if they reach retirement age while still working for the Company. Retirees and their dependents under age 65 can elect either a comprehensive medical plan under which covered expenses are paid at 80% after an annual deductible has been satisfied or, a managed care plan that requires copayments. Employees who elect to retire prior to attaining age 65 are required to make contributions toward their medical coverage until attaining age 65. Retirees and their dependents age 65 and over are covered by a Medicare supplement plan. Costs to the Company for postretirement benefits other than pensions are based on an allocation from American of the total cost related to the plan. Information regarding accumulated and projected benefit obligations is not prepared at the subsidiary level. The Company made contributions to trust funds established for these postretirement benefits of $499 in 2000 and $578 in 1999. The Company's policy is to fund postretirement benefits costs accrued.

Notes To Financial Statements (Dollars in thousands, except per share amounts)

NOTE 12 - RELATED PARTY TRANSACTIONS

The Company provides certain billing, inserting, and information services at cost to AWWS, which amounted to $1,429 in 2000. At December 31, 2000, no amounts were receivable from this affiliate for these services.

The Company began providing workspace and information support system support for associates for the Southeast Region of AWWS in 2000. Charges for direct costs and indirect overhead costs associated with these associates are billed to AWWS on an at-cost, not-for-profit basis, which amounted to $9 in 2000. At December 31, 2000, net amounts receivable from this affiliate for these services were $1.

Some of the company's associates have performed services at cost to AWWS relating to the establishment by American of consolidated customer and shared administrative service centers. The total amount of these services was $115 in 2000. At December 31, 2000, net amounts receivable from this affiliate for these services were $14.

The Company has three operating agreements with American Water Services (AWS), an affiliate, for the lease of granular activated carbon at one of the Company's water treatment plants. The agreements provide for AWS to regenerate the spent carbon and return it to the water treatment plant where it originated. Under the terms of the agreement, AWS will provide carbon for a period of thirty-six months beginning in March 1998, 1999 and 2000. The carbon is scheduled for replacement at thirty-six month intervals and is warranted to perform to specific standards during that period. The Company paid $75 in 2000 and $74 in 1999 under these agreements.

On June 29, 2000 the Company obtained a line of credit through American Water Capital Corporation (AWCC), an affiliate. The company paid AWCC $39 for fees, $23 for preliminary costs of long-term financings and $443 for interest on short-term borrowings.

NOTE 13 - FAIR VALUES OF FINANCIAL INSTRUMENTS

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

Current assets and current liabilities: The carrying amount reported in the balance sheet for current assets and current liabilities approximates their fair value.

Preferred stocks with mandatory redemption requirements and long-term debt: The fair values of the Company's preferred stocks with mandatory redemption requirements and long-term debt are estimated using discounted cash flow analysis based on the Company's current incremental financing rates for similar types of securities.

The carrying amounts and fair values of the Company's financial instruments at December 31 are as follows:

	2000 CARRYING Amount	Fair Value	1999 CARRYING Amount	Fair Value
Preferred stock with mandatory redemption requirements	$ 5,420	$ 5,504	$ 5,468	$ 5,118
Long-term debt, including current maturities	55,000	52,135	67,000	62,701

NOTE 14 - OPERATING LEASES

The Company has entered into operating leases involving certain equipment. Rental expenses under operating leases were $81 for 2000 and $85 for 1999. The operating leases for the equipment expire over the next 3 years. Certain leases have renewal options from one year to the useful life of the equipment.

At December 31, 2000, the minimum annual future rental commitments under operating leases that have initial or remaining noncancelable lease terms in excess of one year are $66 in 2001, $43 in 2002, $3 in 2003, $2 in 2004 and $0 in 2005.

NOTE 15 - COMMITMENTS AND CONTINGENCIES

The Company's construction program for 2001 is estimated to cost approximately $14,331. Commitments have been made in connection with certain projects included in this program.

The Company is routinely involved in legal actions. In the opinion of management, none of these matters will have a material adverse effect, if any, on the financial position, results of operations or cash flows of the Company.

FINANCIAL STATEMENTS

KENTUCKY-AMERICAN WATER COMPANY - HISTORICAL REVIEW

[DOLLARS IN THOUSANDS EXCEPT PER CUSTOMER AMOUNTS)
FOR THE YEARS ENDED DECEMBER 31, 2000

	2000	1999	1998	1997	1996	1995	1990
Utility plant (excluding CWIP)	$ 226,877	$ 215,556	$ 201,191	$ 191,534	$ 178,692	$ 164,133	$ 121,781
Accumulated depreciation	(42,762)	(38,597)	(34,972)	(30,895)	(27,669)	(24,908)	(14,459)
Net utility plant	$ 184,115	$ 176,959	$ 166,219	$ 160,639	$ 151,023	$ 139,225	$ 107,322
Net plant per customer*	$ 1,860	$ 1,806	$ 1,787	$ 1,785	$ 1,736	$ 1,657	
Construction expenditures	$ 11,829	$ 18,386	$ 14,137	$ 12,721	$ 12,949	$ 12,532	$ 6,504
Total assets	$ 210,299	$ 203,600	$ 189,954	$ 178,479	$ 170,509	$ 161,861	$ 119,541
Capitalization ot year end							
Common equity	$ 59,320	$ 58,276	$ 56,842	$ 49,216	$ 45,394	$ 44,112	$ 31,113
Preferred stock	6,990	7,038	7,086	7,134	7,182	7,230	3,470
Long-term debt -							
includes current portion	55,000	67,000	67,000	64,000	62,500	62,500	50,160
	$ 121,310	$ 132,314	$ 130,928	$ 120,350	$ 115,076	$ 113,842	$ 84,743

Customers sewed (000)

Residential *	89	87	84	81	78	76	68
Commercial *	8	8	8	7	7	7	7
Industrial *				1	1		
Fire service & other *	2	1	1	1	1	1	1
	99	96	93	90	87	84	76

Water sales (million gallons)

Residential *	5,825	5,959	5,720	5,357	5,584	5,339	4,743
Commercial •	4,234	4,336	4,251	4,075	4,181	4,120	3,807
Industrial *	973	1,067	1,144	1,081	981	981	852
Public and other*	1,822	1,998	1,860	1,759	1,772	1,780	1,687
	12,854	13,360	12,975	12,272	12,518	12,220	11,089
Annual sales per customer (million gallons)*	130	139	140	136	144	145	146

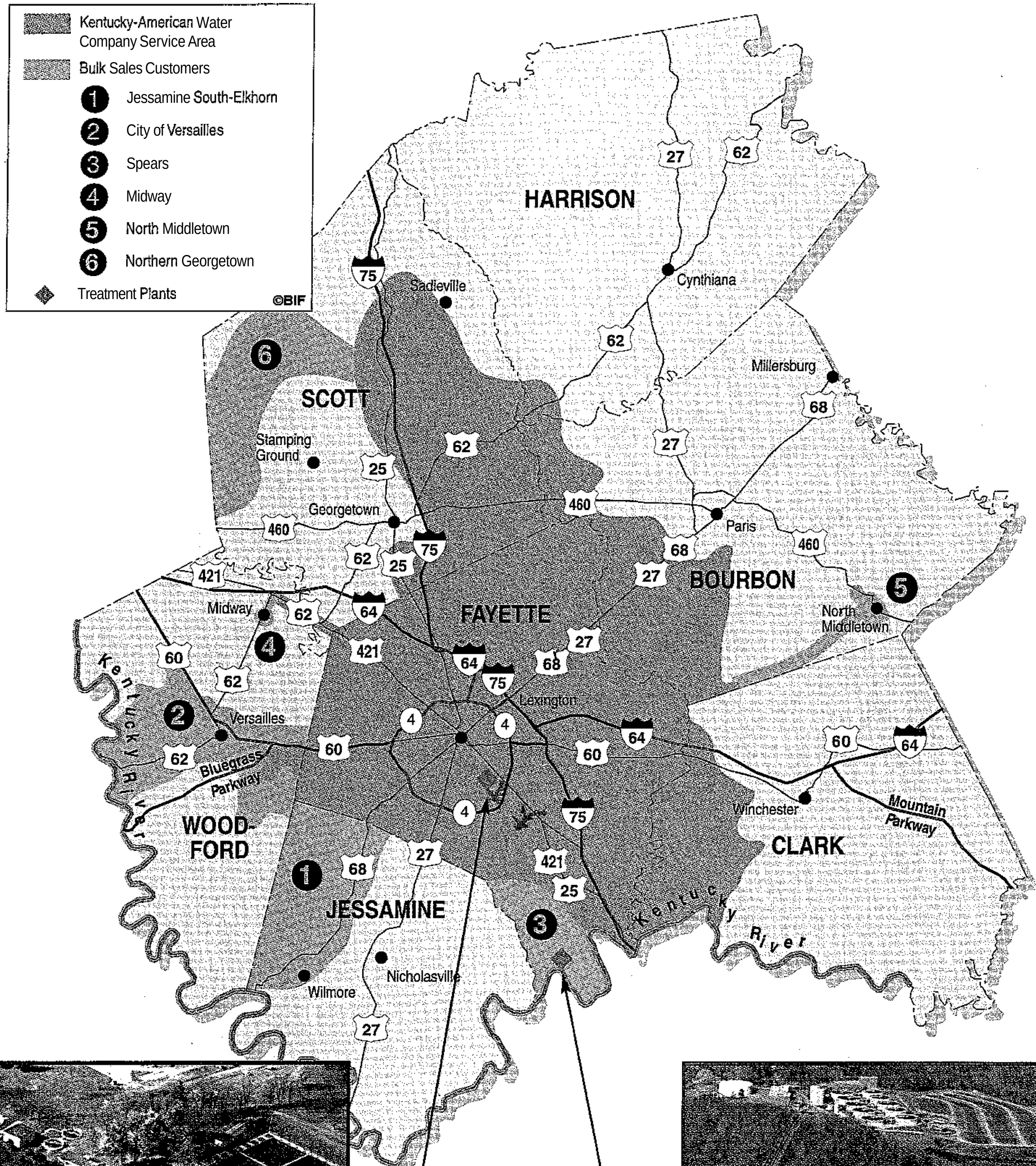
KENTUCKY-AMERICAN WATER COMPANY - HISTORICAL REVIEW (CONTINUED)

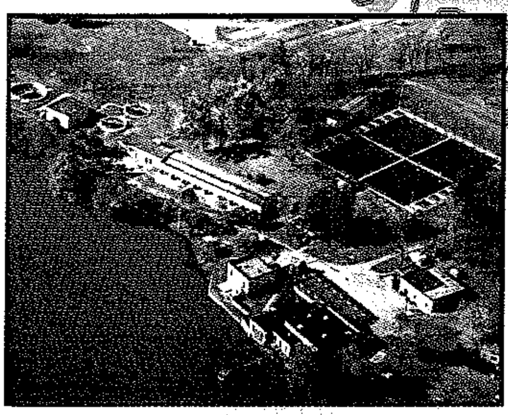
(DOLLARS IN THOUSANDS EXCEPT PER CUSTOMER AMOUNTS)
FOR THE YEARS ENDED DECEMBER 31, 2000

	2000	1999	1998	1997	1996	1995	1990
Operating revenues							
Water service							
Residential	$ 19,577	$ 19,534	$ 18,866	$ 17,437	$ 16,083	$ 15,709	$ 11,628
Commercial	10,155	10,302	10,063	9,451	9,126	9,125	6,463
Industrial	1,583	1,728	1,848	1,704	1,596	1,591	1,068
Fire service	2,519	2,446	2,368	2,281	2,171	2,115	1,694
Public and other	3,739	4,050	3,057	2,945	3,244	3,235	2,364
Wastewater service	31	28	29	-	-	-	-
Other water revenues	1,116	1,016	1,513	1,431	444	312	153
	$ 38,720	$ 39,104	$ 37,744	$ 35,249	$ 32,664	$ 32,087	$ 23,370
Annual revenue per customer*	$ 391	$ 407	$ 406	$ 392	$ 375	$ 382	$ 308
Net income	$ 5,659	$ 7,134	$ 6,858	$ 6,047	$ 5,437	$ 5,357	$ 3,312
Coverage ratios							
On long-term debt interest before income taxer *	2.9	3.2	3.2	3.0	2.7	2.7	2.1
On total interest before income taxer*	2.6	3.1	3.1	2.9	2.8	2.6	2.1
On total fixed charges including preferred dividends							
Before income taxes *	2.3	2.8	2.8	2.6	2.5	2.4	2.0
After income taxes *	1.7	2.0	2.0	1.9	1.9	1.8	1.6

* Unaudited

Kentucky-American Water Company
Service Area





Richmond Road Treatment Plant

Kentucky River Treatment Plant

PRICEWATERHOUSECOOPERS

KENTUCKY-AMERICAN WATER COMPANY

Financial Statements

December 31, 2001 and 2000

KENTUCKY-AMERICAN WATER COMPANY

An American Water System Company
2300 Richmond Road
Lexington, Kentucky 40502

Board of Directors

J. James Barr, President & Chief Executive Officer
American Water Works Company, Inc.

G. C. Smith, Director
American Water Works Company, Inc.

Ellen C. Wolf, Vice President & Chief Financial Officer
American Water Works Company, Inc.

Daniel L. Kelleher, Senior Vice President
American Water Works Service Company, Inc.

Chris E. Jarrett, Chairman of the Board
Kentucky-American Water Company

R. W. Mundy, II, President
Kentucky-American Water Company

W. L. Rouse, Jr.
Rouse Companies

W. T. Young, Jr.
W. T. Young, Inc.

Elizabeth H. Gemmill, Esq., Managing Trustee
Warwick Foundation

Lindsey W. Ingram, Jr., Esq.
Stoll, Keenon and Park LLP

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Vice President	Nick O. Rowe
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Vice President and Secretary	Herbert A. Miller, Jr.
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Assistant Treasurer	James R. Hamilton
Assistant Treasurer and Assistant Secretary	Nancy M. Strickland
Assistant Secretary	Stephen N. Chambers
Assistant Comptroller	Thomas R. Bailey
Assistant Comptroller	Rachel S. Cole
Assistant Comptroller	Jonathan G. Easlick
Assistant Comptroller	D o n e S. Hobbs
Assistant Comptroller	F r S. Impagliazzo
Assistant Comptroller	Benjamin J. Tartaglia, Jr.
Assistant Comptroller	R o b N. Quinn

PRICEWATERHOUSECOOPERS

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Philadelphia PA 19103-7042
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Report of Independent Accountants

To the Board of Directors and Stockholder of
Kentucky-American Water Company

In our opinion, the accompanying balance sheet and the related statement of income, of retained earnings, of cash flows, of capitalization and of common stockholder's equity present fairly, in all material respects, the financial position of Kentucky-American Water Company (a wholly-owned subsidiary of American Water Works Company, Inc.) at December 31, 2001 and 2000, and the results of its operations and its cash flows for the years then ended 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 auditing standards generally accepted in the United States of America, which 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.

PricewaterhouseCoopers LLP

February 1, 2002

KENTUCKY-AMERICANWATER COMPANY

Balance Sheet
(Dollars in thousands)

	December 31, 2001	2000
Assets		
Property, plant and equipment		
Utility plant - at original cost less accumulated depreciation	$ 200,792	$ 189,424
Utility plant acquisition adjustments, net	359	138
	201,151	189,562
Non utility property	250	250
Current assets		
Cash	1,453	803
Customer accounts receivable	1,568	1,768
Allowance for uncollectible accounts	(58)	(56)
Unbilled revenues	2,137	2,085
Prepaid tax	-	641
Materials and supplies	361	431
Deferred vacation pay	252	219
Other	258	458
	5,971	6,349
Regulatory and other long-term assets		
Deferred business service project expense	1,360	164
Regulatory asset-income taxes recoverable through rates	4,523	4,405
Debt and preferred stock expense	871	835
Deferred programmed maintenance	3,193	3,340
Preliminary survey and investigation	430	179
Other	5,802	5,856
	16,179	14,779
	$ 223,551	$ 210,940
Capitalization and Liabilities		
Capitalization		
Common stock	$ 36,569	$ 36,569
Paid-in capital	21	21
Retained earnings	24,407	22,730
Total common stockhoider's equity	60,997	59,320
Preferred stock		
With mandatory redemption requirements	5,380	5,420
Without mandatory redemplion requirements	1,570	1,570
Long-term debt	44,500	42,000
Total capitalization	112,447	108,310
Current liabilities		
Affiliate borrowings	24,668	20,830
Current portion of long-term debt	13,000	13,000
Accounts payable	967	1,762
Taxes accrued	261	242
Interest accrued	853	688
Tax collections payable	215	256
Accrued vacation pay	252	219
Other	2,035	675
	42,251	37,672
Regulatory and other long-term liabilities		
Customer advances for construction	9,365	9,795
Deferred income taxes	28,192	27,271
Deferred investment tax credits	1,726	1,811
Accrued pension expense	1,362	977
Accrued postretirement benefits expense	299	299
Other	392	595
	41,336	40,748
Contributions in aid of construction	27,517	24,210
	$ 223,551	$ 210,940

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

KENTUCKY-AMERICAN WATER COMPANY

Statement of Income
(Dollars in thousands)

	Years Ended December 31, 2001	2000
Operating revenues	$ 41,478	$ 38,720
Operating expenses		
Operation and maintenance	17,800	15,467
Depreciation and amortization	5,981	5,184
General Taxes	1,831	1,762
	25,612	22,413
Utility operating income	15,866	16,307
Other income (deductions)		
Allowance for other funds used during construction	300	397
Miscellaneous other income	785	12
Miscellaneous other deductions	-	(1,786)
Income before interest charges and income taxes	16,951	14,930
Interest charges		
Interest on long-term debt	4,767	5,123
Interest on bank debt	486	538
Amortization of debt expense	79	42
Other interest	55	30
Allowance for borrowed funds used during construction	(149)	(210)
Income before income taxes	11,713	9,407
Provision for income taxes		
Federal income taxes	3,711	3,374
State income taxes	992	374
Net income	$ 7,010	$ 5,659

Consolidated Statement of Retained Earnings
(Dollars in thousands)

	2001	2000
Retained earnings at beginning of year	$ 22,730	$ 21,686
Net income	7,010	5,659
	29,740	27,345
Dividends		
Preferred stock	537	540
Common stock	4,796	4,075
	5,333	4,615
Retained earnings at end of year	$ 24,407	$ 22,730

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

KENTUCKY-AMERICAN WATER COMPANY

Statement of Cash Flows
(Dollars in thousands)

	Years Ended December 31, 2001	2000
Cash flows from operating activities		
Net income	$ 7,010	$ 5,659
Adjustments		
Depreciation and amortization	5,981	5,184
Amortization, other	1,031	594
Provision for deferred income taxes	899	3,610
Amortization of deferred investment tax credits	(85)	(85)
Provision for losses on accounts receivable	200	201
Allowance for other funds used during construction	(300)	(397)
Pension expense in excess of funding	385	(495)
Deferred regulatory assets	(1,212)	(375)
Other, net	(3,071)	(603)
Changes in current assets and liabilities		
Accounts receivable	2	(548)
Unbilled revenues	(52)	(183)
Materials and supplies	70	93
Other current assets	167	479
Accounts payable	(795)	522
Taxes accrued	69	(98)
Interest accrued	165	(144)
Other current liabilities	1,352	(2,072)
Net cash provided by operating activities	11,816	11,342
Cash flows from investing activities		
Construction expenditures	(13,794)	(11,829)
Allowance for other funds used during construction	300	397
Cost of removal, net of salvage	289	313
Payment for acquisition of public service district assets	(1,686)	-
Net cash used in investing activities	(14,891)	(11,119)
Cash flows from financing activities		
Proceeds from long-term debt issuance	15,500	-
Net borrowings (repayments) under line-of-credit agreement	3,837	15,114
Repayment of long-term debt	(13,000)	(12,000)
Customer advances and contributions, net of refunds	2,878	1,621
Redemption of preferred stock	(40)	(48)
Dividends paid	(5,333)	(4,615)
Debt issuance cost	(117)	-
Net cash provided by financing activities	3,725	72
Net increase (decrease) in cash and cash equivalents	650	295
Cash and cash equivalents at beginning of year	803	508
Cash and cash equivalents at end of year	$ 1,453	$ 803
Cash paid during the year for:		
Interest, net of capitalized amount	$ 5,144	$ 5,835
Income taxes	$ 3,240	$ 704

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

KENTUCKY-AMERICAN WATER COMPANY

Statement of Capitalization
(Dollars in thousands)

	Call Price Per Share	December 31, 2001	2000
Common stockholder's equity			
Common stock - no par value, authorized			
2,000,000 shares, issued and outstanding 1,567,391 shares			
in 2001 and 2000		$ 36,569	36,569
Paid in capital		21	21
Retained earnings		24,407	22,730
		60,997	59,320
Preferred stocks - $100 par value, authorized 25,000 shares			
Without mandatory redemption requirements			
Cumulative preferred stock			
5.75% series, 4,700 shares issued and outstanding	$ 101.00	470	470
5.5% series, 5,000 shares issued and outstanding	$ 100.50	500	500
5.% series, 6,000 shares issued and outstanding	$ 101.00	600	600
		1,570	1,570
With mandatory redemption requirements			
Cumulative preferred stock			
7.9% series, 8,800 and 9,200 shares issued and outstanding			
in 2001 and 2000, respectively	$ 100.00	880	920
8.47% series, 45,000 shares issued and outstanding	$ 100.00	4,500	4,500
		5,380	5,420
Long-term debt			
General mortgage bonds			
8.36% series due 2001		-	13,000
7.21% series due 2002		13,000	13,000
6.79% series due 2005		5,500	5,500
6.96% series due 2023		7,000	7,000
7.15% series due 2027		7,500	7,500
6.99% series due 2028		9,000	9,000
Senior notes			
6.87% series due 2011		15,500	-
		57,500	55,000
Less: Current portion of long-term debt and capital lease obligation		13,000	13,000
Long-term debt net of current maturities		44,500	42,000
Total capitalization		$ 112,447	$ 108,310

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

KENTUCKY-AMERICAN WATER COMPANY

Statement of Common Stockholder's Equity
(Dollars in thousands)

	Common Stock		Paid-in	Retained	Stockholder's
	Shares	Par Value	Capital	Earnings	Equity
Balance at December **31, 1999**	1,567,391	$ 36,569	$ 21	$ 21,686	$ 58,276
Net income				5,659	5,659
Sale of common stock					
Dividends					
Preferred stock				(540)	(540)
Common stock, $2.60 per share				(4,075)	(4,075)
Balance at December **31,2000**	1,567,391	36,569	21	22,730	59,320
Net income				7.010	7,010
Sale of common stock					
Dividends					
Preferred stock				(537)	(537)
Common stock, $3.06 per share				(4,796)	(4,796)
Balance at December **31,2001**	1,567,391	$ 36,569	$ 21	$ 24.407	$ 60.997

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

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements
(Dollars in thousands)

Note 1 - Organization and Operation

Kentucky-American Water Company (the Company) provides water service to approximately 103,000 customers and wastewater service to approximately 88 customers. These services are provided in 10 communities located in 10 counties in the state of Kentucky. As a public utility operating in Kentucky, the Company functions under rules and regulations prescribed by the Kentucky Public Service Commission (the Commission). The Company is a wholly-owned subsidiary of American Water Works Company, Inc. (American).

Note 2 - Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Actual results could differ from these estimates.

Regulation

The Company has incurred various costs and received various credits, which have been reflected as regulatory assets and liabilities on its balance sheet. Accounting for such costs and credits as regulatory assets and liabilities is in accordance with Statement of Financial Accounting Standards No. 71, "Accounting for the Effects of Certain Types of Regulation" (SFAS No. 71). This statement sets forth the application of generally accepted accounting principles for those companies whose rates are established by or are subject to approval by an independent third-party regulator. Under SFAS No. 71, regulated companies defer costs and credits on the balance sheet as regulatory assets and liabilities when it is probable that those costs and credits will be recognized in the rate-making process in a period different from the period in which they would have been reflected in income by an unregulated company. These deferred regulatory assets and liabilities are then reflected in the income statement in the period in which the same amounts are reflected in the rates charged for service.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

Property, Plant and Equipment

Additions to utility plant and replacements of retirement units of property are capitalized. Costs include material, direct labor and such indirect items as engineering and supervision, payroll taxes and benefits, transportation and an allowance for funds used during construction. The costs incurred to acquire and internally develop computer software for internal use are capitalized as a unit of property. Repairs, maintenance and minor replacements of property are charged to current operations. The cost of property units retired in the ordinary course of business plus removal cost (net of salvage) is charged to accumulated depreciation. The cost of property, plant and equipment is depreciated using the straight-line method. The depreciation rates, based on the average balance of depreciable property, were 2.69% in 2001 and 2.61% in 2000.

In accordance with the Commission's regulations, depreciation on contributed facilities is charged to contributions in aid of construction. Such depreciation amounted to $642 in 2001 and $580 in 2000.

Cash and Cash Equivalents

Substantially all of the Company's cash is invested in interest bearing accounts. The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. There were no cash equivalents held at December 31,2001 or 2000.

Materials and Supplies

Materials and supplies are stated at average cost.

Regulatory and long-Term Assets

Deferred business services project expenses consist of reengineering and start-up activities for consolidated customer and shared administrative service centers that are being established by American. These costs are being deferred as it is expected that these costs will be recovered in the rates charged for utility service in the future.

The Company has deferred the cost of increased security measures that were implemented to secure facilities after the terrorist attacks on September 11, 2001. These costs are being deferred as it is expected that these costs will be recovered in the rates charged for utility service in the future.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

The Company has recorded a regulatory asset for the additional revenues expected to be realized as the tax effects of temporary differences previously flowed through to customers reverse. These temporary differences are primarily related to the difference between book and tax depreciation on property placed in service before the adoption by the Commission of full normalization for rate-making purposes.

The regulatory asset for income taxes recoverable through rates is net of the reduction expected in future revenues as deferred taxes previously provided, attributable to the difference between the state and federal income tax rates under prior law and the current statutory rates, reverse over the average remaining service lives of the related assets.

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

Preliminary survey and investigation charges generally relate to future construction projects. Management believes these costs will ultimately be recovered through rates.

Programmed maintenance costs are deferred and amortized to current operations on a straight-line basis over a period ranging between five and fifteen years, as authorized by the Commission in their determination of rates charged for service.

Other Current Liabilities

Other current liabilities at December 31,2001 and 2000 include payables of $929 and $0, respectively, which represent checks issued but not presented to the bank for payment.

Advances and Contributions in Aid of Construction

The Company may receive advances and contributions to fund construction necessary to extend service to new areas. As determined by the Commission, advances for construction are refundable for limited periods of time as new customers begin to receive service. 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 and is not depreciated for rate-making purposes. Generally, advances and contributions received during the period of January 1, 1987 through June 12, 1996 have been included in taxable income and the related property is depreciable for tax purposes. As a result of a tax law change, advances and

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

contributions received subsequent to June 12, 1996 are excluded from taxable income and the related property is not depreciable for tax purposes.

On January 11,2001 the Internal Revenue Service issued regulations that excluded lateral service lines from its definition of contributions in aid of construction that are not included in taxable income. These customer connection fees are defined as the cost of installing a connection or service line from the Company's main lines to the lines owned by the customer. The regulations were effective immediately, but the Company does not have customer connection fees.

Recognition of Revenues

Water service revenues for financial reporting purposes include amounts billed to customers on a cycle basis and unbilled amounts based on estimated usage from the date of the latest meter reading to the end of the accounting period.

Income Taxes

The Company, its parent and affiliates participate in a consolidated federal income tax return. Federal income tax expense for financial reporting purposes is provided on a separate return basis, except that the federal income tax rate applicable to the consolidated group is applied to separate company taxable income and the benefit of net operating losses, if any, is recognized currently.

Certain income and expense items are accounted for in different time periods for financial reporting than for income tax reporting purposes. Deferred income taxes have been provided on the difference between the tax bases of assets and liabilities and the amounts at which they are carried in the financial statements. These deferred income taxes are based on the enacted tax rates anticipated to be in effect when such temporary differences are expected to reverse. Regulatory assets and liabilities are recognized for the effect on revenues expected to be realized as the tax effects of temporary differences previously flowed through to customers reverse.

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

Allowance for Funds Used During Construction (AFUDC)

AFUDC is a non-cash adjustment to income with a corresponding charge to utility plant, which represents the cost of borrowed funds and a return on equity funds devoted to plant under construction. AFUDC is recorded to the extent permitted by the Commission.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

Environmental Costs

Environmental expenditures that relate to current operations or provide a future benefit are expensed or capitalized as appropriate. Remediation costs that relate to an existing condition caused by past operations are accrued when it is probable that these costs will be incurred and can be reasonably estimated. There were no remediation costs accrued at December 31,2001 and 2000.

Asset Impairment

Long-lived assets and certain identifiable intangible assets held and used by the Company are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets, on a separate entity basis, may not be recoverable. If the sum of the future cash flows expected to result from the use of the assets and their eventual disposition is less than the carrying amount of the assets, an impairment loss is recognized. Measurement of an impairment loss would be based on the fair value of the assets. A regulatory asset is charged to earnings if and when future recovery in rates of that asset is no longer probable.

New Accounting Standards

On January 1,2001, the Company adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS 133), as amended. This statement establishes accounting and reporting standards for derivative instruments and hedging activities. SFAS 133 was issued by the Financial Accounting Standards Board (FASB) in June of 1998 and requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. This new accounting standard did not have any effect on the Company's financial position or results of operations. The Company's contracts that meet the definition of a derivative are for normal purchases and normal sales, are expected to result in a physical delivery, and are of quantities expected to be used or sold over a reasonable period in the normal course of business. The Company has no hedging activities.

In June of 2001, the FASB issued Statements of Financial Accounting Standards No. 141, "Business Combinations" (SFAS 141) and No. 142, "Goodwill and Other Intangible Assets" (SFAS 142). SFAS 141 requires all business combinations initiated after June 30,2001 to be accounted for using the purchase method. Under SFAS 142, goodwill and intangible assets with indefinite lives are no longer amortized but are reviewed annually (or more frequently if impairment indicators arise) for impairment. Separable intangible assets that are not deemed to have indefinite lives will continue to be amortized over their useful lives. The amortization

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

provisions of SFAS 142 apply to goodwill and intangible assets acquired after June 30, 2001. With respect to goodwill and intangible assets acquired prior to July 1,2001, the Company is required to adopt SFAS 142 effective January 1,2002. The Company is currently evaluating the effect that adoption of the provisions of SFAS 142 that are effective January 1,2002 will have on its results of operations and financial position.

Also in June of 2001, the FASB issued Statement of Financial Accounting Standard No. 143, "Accounting for Asset Retirement Obligations," (SFAS 143) on the accounting for obligations associated with the retirement of long-lived assets. SFAS 143 requires a liability to be recognized in the financial statements for retirement obligations meeting specific criteria. Measurement of the initial obligation is to approximate fair value with an equivalent amount recorded as an increase in the value of the capitalized asset.

The asset will be depreciable in accordance with normal depreciation policy and the liability will be increased, with a charge to the income statement, until the obligation is settled. SFAS 143 is effective for fiscal years beginning after June 15,2002. The Company is currently evaluating the effect that adoption of the provisions of SFAS 143 will have on its results of operations and financial position.

In August of 2001, the FASB issued Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," (SFAS 144) that replaces Statement of Financial Accounting Standards No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of." SFAS 144 requires that one accounting model be used for long-lived assets to be disposed of by sale and broadens discontinued operations to include more disposal transactions. Under SFAS 144, operating losses of discontinued operations are recognized in the period in which they occur, instead of accruing future operating losses before they occur. SFAS 144 is effective for fiscal years beginning after December 15,2001. The Company is currently evaluating the effect that adoption of the provisions of SFAS 144 will have on its results of operations and financial position.

Reclassifications

Certain reclassifications have been made to conform previously reported data to the current presentation.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

Note 3 - Utility Plant

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

	2001	2000
Water plant		
Sources of supply	$ 6,926	$ 6,914
Treatment and pumping	45,017	44,316
Transmission and distribution	125,485	117,374
Services, meters, and fire hydrants	47,024	42,843
General structures and equipment	16,167	15,430
Construction work in progress	8,954	5,309
	249,573	232,186
Less - accumulated depreciation	48,781	42,762
	$ 200,792	$ 189,424

Note 4 - Preferred Stocks

Preferred stock agreements have annual minimum sinking fund payments of $40 in 2002 through 2006. The 7.9% series sinking fund payment of $40 is at the option of the Company.

Note 5 - Long-Term Debt

Maturities of long-term debt will amount to $13,000 in 2002, $0 in 2003 and 2004, $5,500 in 2005, and $0 in 2006.

The general mortgage bond indentures, as supplemented, contain clauses restricting the declaration of common stock dividends and other distributions on capital stock if common stockholder's equity falls below a specified amount. There were no restrictions at December 31, 2001.

The general mortgage bonds are issuable in series. No bonds senior to the general mortgage bonds may be issued so long as the general mortgage bonds are outstanding. The amount of bonds authorized is unlimited as long as long-term debt does not exceed 65% of capitalization. Long-term debt is secured by utility plant.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

Note *6* - Affiliate Borrowings

During 2001, the Company maintained a line of credit through American Water Capital Corp. (AWCC), an affiliate (see Note 13: Related Party Transaction). AWCC is a special purpose corporation that serves as the primary funding vehicle for the Company. AWCC has a 364-day $500 million revolving credit agreement with a group of 10 domestic and international banks. No compensating balances are required under the agreement. AWCC also issues commercial paper, and the revolving credit agreement also supports these borrowings.

At December 31,2001 and 2000, there were $24,668 and $20,830 of short-term borrowings outstanding, respectively. The weighted average annual interest rate on these borrowings was 5.60% and 6.97% respectively. The unused line of credit at December 31,2001 was $0.

Note 7 - **Financings**

During 2001 and 2000 the Company completed the following financings:

Date	Proceeds	Issue
03/29/01	$15,500	Senior Note, 6.87% due 2011

The senior note is unsecured and was issued to AWCC for the principal amount. AWCC provided the funding for this note by itself issuing $140 million of senior notes to institutional investors at a price equal to the principal amount.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

Note 8 - General Taxes

Components of general tax expense for the years presented in the statement of income are as follows:

	2001	2000
Gross receipts and franchise	$ 74	$ 80
Property and capital stock	1,313	1,239
Payroll	444	443
	$ 1,831	$ 1,762

Note 9 - Income Taxes

Components of income tax expense for the years presented in the statement of income are as follows:

	2001	2000
State income taxes:		
Current	$ 782	$ 7
Deferred		
Non-current	210	789
	$ 992	$ 796
Federal income taxes:		
Current	$ 3,107	$ 216
Deferred		
Non-current	689	2,821
Amortization of deferred investment tax credits	(85)	(85)
	$ 3,711	$ 2,952

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

A reconciliation of income tax expense at the statutory federal income tax rate to the actual income tax expense is as follows:

	2001	2000
Income tax at statutory rate of 35%	$ 4,100	$ 3,293
Increases (decreases) resulting from -		
State taxes, net of federal income taxes	645	517
Flow though differences	72	58
Amortization of investment tax credits	(85)	(85)
Other, net	(29)	(35)
Actual income tax expense	$ 4,703	$ 3,748

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

	2001	2000
Deferred tax assets:		
Advances and contributions	$ 14,697	$ 13,533
Deferred investment credits	697	731
Other	806	648
	$ 16,200	$ 14,912
Deferred **tax** liabilities:		
Utility plant, principally due to depreciation differences	$39,052	$ 36,791
Income taxes recoverable through rates	1,826	1,778
Other	3,514	3,614
	44,392	42,183
Net deferred tax liability	$ 28,192	$ 27,271

No valuation allowances were required on deferred tax assets at December 31,2001 and 2000.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

Note 10 - Rate Matters

As necessary, the Company applies to the Commission for changes in the rates charged for service. The rate increase request is based on the level of operating expenses and capital costs that are expected to be in effect when the rates become effective. The revenues requested are based on forecasted sales, operating expenses and investments for the test year selected by the Company.

The Company has received approval from the Commission to increase its rates for service as follows:

Effective Dates	Requested Annual Effect on Revenues	Estimated Annual Effect on Revenues Granted	Estimated Revenue Realized in 2001
05/09/01	$4,685	$2,568	$2,368

On April 28,2000, the Company filed a rate application with the Public Service Commission of the commonwealth of Kentucky ("Commission"), requesting $5.034 million in additional annual revenues that was subsequently revised to $4.685 million or 11.69%.

On December 12,2000, the Commission issued an Order adjusting its original Order dated November 27,2000. The adjusted order corrected errors in the initial ruling and reduced the allowed revenue increase from $2.518 million to $2.171 million to be effective for service rendered on and after November 27,2000. Revenues realized in 2000 from this increase are estimated at $.208 million.

On May 9,2001, a final decision was issued which addressed appeals from reconsideration made by the Company and the State Attorney General. The final decision adjusted the authorized revenue increase from $2.171 to $2.568 million or 6.42% of total operating revenues.

Proposed Asset Protection *Charge Tariff*

On November 28,2001, the Company filed an application with the Commission seeking an asset protection charge tariff. The charge is comprised of two elements: (1) the projected annual increase in operating expenses since the last general rate case for the protection of assets, and (2) the revenue recovery of the capital expenditures made for the protection of assets since the last general rate case.

KENTUCKY-AMERICAN WATER COMPANY

**Notes to Financial Statements (continued)
(Dollars in thousands)**

Note 11 - Employee Benefit Plans

Employees' Stock Ownership Plan

The Company participates in an Employees' Stock Ownership Plan sponsored by American, which provides for beneficial ownership of American common stock by all associates who are not included in a bargaining unit. Each participating associate can elect to contribute an amount that does not exceed 2% of their wages. In addition to the associate's participation, the Company makes a contribution equivalent to ½% of each participant's qualified compensation, and matches 100% of the contribution by each participant. The Company expensed contributions of $62 for 2001 and $69 for 2000 that it made to the plan.

Savings Plan for Employees

The Company participates in a 401(k) Savings Plan for Employees sponsored by American. All Associates can make contributions that are invested at their direction in one or more funds including a fund consisting entirely of American common stock. The Company matches 50% of the first 4% of each associate's wages contributed to the plan. The company expensed matching contributions to the plan totaling $85 for 2001 and $83 for 2000. All of the Company's matching contributions are invested in the fund of American common stock.

Note 12 - Postretirement Benefits

Pension *Benefits*

The Company participates in a noncontributory defined benefit pension plan sponsored by American covering substantially all associates. Benefits under the plan are based on the associate's years of service and average annual compensation for those 60 consecutive months of employment, which yield the highest average. Pension cost of the Company is based on an allocation from American of the total cost related to the plan. Information regarding accumulated and projected benefit obligations is not prepared at **the** subsidiary level. The Company's funding policy is to contribute at least the minimum amount required under the Employee Retirement Income Security Act of 1974. The Company made no contribution to the plan in 2001 or 2000.

In addition, during 2000, the Company recognized a settlement gain of $523 relating to the transfer of annuities from the plan to a separate third-party life insurance company. This settlement gain has been recognized as a decrease in deferred pension costs and accrued pension costs.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

Postretirement Benefits Other Than Pensions

The Company participates in an American plan that provides certain life insurance benefits for retired associates and certain health care benefits for retired associates and their dependents. Substantially all associates may become eligible for these benefits if they reach retirement age while still working for the Company. Retirees and their dependents under age 65 are covered by a point-of-service managed care plan that requires co-payments or an HMO. Associates who elect to retire prior to attaining age 65 are generally required to make contributions towards their medical coverage until attaining age 65. Retirees and their dependents age 65 and over are covered by a Medicare supplement plan. Costs of the Company are based on an allocation from American of the total cost related to the plan. Information regarding accumulated and projected benefit obligations is not prepared at the subsidiary level. The Company made contributions to trust funds established for these postretirement benefits of $561 in 2001 and $499 in 2000. The Company's policy is to fund postretirement benefits costs accrued.

Note **13** -Related Party Transactions

American Water Works Service Company, Inc. (AWWS), an affiliate, provides certain management services to the Company (administration, accounting, data processing, engineering, etc.) and other operating water companies in the American Water Works System on an at-cost, not-for-profit basis in accordance with a management and service agreement. Purchases of such services by the Company were accounted for as follows:

	2001	2000
Included in operation and maintenance expense as a charge against income	$ 1,535	$ 1,185
Capitalized in various balance sheet accounts	765	244
	$ 2,300	$ 1,429

The Company provided workspace and information support system support for associates of the Southeast Region of AWWS. Charges for direct costs and indirect overhead costs associated with these associates are billed to AWWS on an at-cost, not for profit basis, which amounted to $43 in 2001 and $9 in 2000. At December 31,2001, net amounts receivable from this affiliate for these services were $4.

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

Some of the Company's associates have performed services at cost to AWWS relating to the establishment by American of consolidated customer and shared administrative service centers. The total amount of these services was $217 in 2001 and $115 in 2000. At December 31,2001, net amounts receivable from this affiliate for these services were $11.

The Company has three operating agreements with American Water Services, (AWS) Inc., an affiliate, for the lease of granular activated carbon (GAC) at one of the Company's water treatment plants. The agreements provide for AWS to regenerate the spent material and return it to the water treatment plant where it originated. Under the terms of the agreements, AWS will provide carbon for a period of thirty-six months beginning in March 1999,2000, and 2001. The carbon is scheduled for replacement at thirty-six month intervals and is warranted to perform to specific standards during that period. The Company paid $82 in 2001 and $75 in 2000 to AWS under these agreements.

The Company maintains a line of credit through American Water Capital Corp. (AWCC), an affiliate. The company paid AWCC fees of $47 in 2001 and $39 in 2000, preliminary costs of long-term financings of $117 in 2001 and $23 in 2000 and interest on borrowings of $486 in 2001 and $443 in 2000.

Note 14 - Fair Values of Financial Instruments

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

Current assets and current liabilities: The carrying amount reported in the balance sheet for current assets and current liabilities approximates their fair value.

Preferred stocks with mandatory redemption requirements and long-term debt: The fair values of the Company's preferred stocks with mandatory redemption requirements and long-term debt are estimated using discounted cash flow analyses based on the Company's current incremental financing rates for similar types of securities

KENTUCKY-AMERICAN WATER COMPANY

Notes to Financial Statements (continued)
(Dollars in thousands)

The carrying amounts and fair values of the Company's financial instruments at December 31 are as follows:

	2001		2000	
	Carrying Amount	**Fair Value**	**Carrying Amount**	**Fair Value**
Preferred stock with mandatory redemption requirements	$ 5,380	$ 5,805	$ 5,420	$ 5,504
Long-term debt, including current maturities other than obligations under capital leases	57,500	55,961	55,000	52,135

Note 15 - Operating Leases

The Company has entered into operating leases involving certain facilities and equipment. Rental expenses under operating leases were $134 in 2001 and $81 for 2000. The operating leases for their equipment expire over the next six years.

At December 31, 2001, the minimum annual future rental commitments under operating leases that have initial or remaining non-cancellable lease terms in excess of one year are $61 in 2003, $51 in 2004, $50 in 2005, and $34,000 in 2006.

Note 16 - Commitments and Contingencies

The Company's construction program for 2002 is estimated to cost approximately $16,633. Commitments have been made in connection with certain projects included in this program.

The Company is routinely involved in legal actions. In the opinion of management, none of these matters will have a material adverse effect, if any, on the financial position or results of operations of the Company.

KENTUCKY-AMERICAN WATER COMPANY

Other Information

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Report of Independent Accountants

To the Board of Directors and Stockholder of
Kentucky-American Water Company

In our opinion, the accompanying Historical Review, except for that portion marked "audited", on which we express no opinion, is fairly stated in all material respects in relation to the financial statements, taken as a whole, of Kentucky-American Water Company (a wholly-owned subsidiary of American Water Works Company, Inc.) for the years ended December 31, 2001 and 2000, which are covered by our reported dated February 1, 2002 presented in the first section of this document. Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The Historical Review is presented for purposes of additional analysis and is not a required part of the financial statements. Such information, except for that portion marked "audited" has been subjected to the auditing procedures applied in the audit of the basic financial statements.

PricewaterhouseCoopers LLP

February 1, 2002

KENTUCKY-AMERICAN WATER COMPANY

Historical Review

(Dollars in **thousands,** except **per customer** amounts)

For the years ended December 31,	2001	2000	1999	1998	1997	1991
Utility plant (excluding CWIP)	$ 240,619	$ 226,877	$ 215,556	$ 201,191	$ 191,534	$ 125,976
Accumulated depreciation	(48,781)	(42,762)	(38,597)	(34,972)	(30,895)	(15,913)
Net utility plant	$ 191,838	$ 184,115	$ 176,959	$ 166,219	$ 160,639	$ 110,063
Net plant per customer *	$ 1,859	$ 1,860	$ 1,806	$ 1,787	$ 1,785	$ 1,412
Construction expenditures	$ 13,794	$ 11,829	$ 18,386	$ 14,137	$ 12,721	$ 12,891
Total assets	$ 223,551	$ 210,299	$ 203,600	$ 189,954	$ 178,479	$ 128,602
Capitalization at year end						
Common equity	$ 60,997	$ 59,320	$ 58,276	$ 56,842	$ 49,216	$ 32,307
Preferred stack	6,950	6,990	7,038	7,086	7,134	3,422
Long-term debt - includes current portion	57,500	55,000	67,000	67,000	64,000	42,540
	$ 125,447	$ 121,310	$ 132,314	$ 130,928	$ 120,350	$ 78,269
Customers served						
Residential *	93	89	87	84	81	70
Commerciai *	8	8	8	8	7	7
Industrial *	-	-	-	-	1	-
Fire service &Other'	2	2	1	1	1	1
	103	99	96	93	90	78
Water sales (gallons)						
Residential *	5,916	5,825	5,959	5,720	5,357	4,848
Commercial *	4,256	4,234	4,336	4,251	4,075	3,902
Industrial *	901	973	1,067	1,144	1,081	841
Public and other *	1,803	1,822	1,998	1,860	1,759	1,787
	12,876	12,854	13,360	12,975	12,272	11,378
Annual sales per customer (gallons)^	125	130	139	140	136	146
Operating revenues						
Water service						
Residential	$ 21,512	$ 19,577	$ 19,534	$ 18,866	$ 17,437	$ 12,642
Commercial	10,789	10,155	10,302	10,063	9,451	7,671
Industrial	1,587	1,583	1,728	1,848	1,704	1,195
Fire service	2,567	2,519	2,446	2,368	2,281	1,724
Public and other	3,980	3,739	4,050	3,057	2,945	2,821
Wastewater service	31	31	28	29	-	-
Other water revenues	1,012	1,116	1,016	1,513	1,431	163
	$ 41,478	$ 38,720	$ 39,104	$ 37,744	$ 35,249	$ 26,216
Annual revenue per customer *	$ 402	$ 391	$ 407	$ 406	$ 392	$ 336
Net income		$ 5.659	$ 7.134	$ 6.858	$ 6.047	$ 4.411
Coverage ratios						
On long-term debt interest before income taxes *	3.4	2.9	3.2	3.2	3.0	2.7
On total interest before income taxes *	3.0	2.6	3.1	3.1	2.9	2.3
On total fixed charges including preferred dividends						
Before income taxes *	2.7	2.3	2.8	2.8	2.6	2.2
After income taxes *	2.0	1.7	2.0	2.0	1.9	1.7

Unaudited

Exhibit 28

PRICEWATERHOUSECOOPERS

Kentucky-American Water Company

Financial Statements

December 31, 2002 and 2001

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers LLP
Two Commerce Square, Suite 1700
2001 Market Street
Philadelphia PA 19103-7042
Telephone (267) 330 3000
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Report of Independent Accountants

To the Board of Directors and Stockholders
Kentucky-American Water Company

In our opinion, the accompanying balance sheets and the related statements of income, of capitalization, of retained earnings and stockholders' equity and of cash flows present fairly, in all material respects, the financial position of Kentucky-American Water Company (a wholly-owned subsidiary of American Water Works Company, Inc.) at December 31,2002 and 2001, and the results of its operations and its cash flows for the years then ended 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 auditing standards generally accepted in the United States of America, which 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.

PricewaterhouseCoopers LLP

February 6,2003

KENTUCKY-AMERICAN WATER COMPANY
Balance Sheet
(Dollars in thousands)

	December 31, 2002	December 31, 2001
Assets		
Property, plant and equipment		
Utility plant - at original cost less accumulated depreciation	$ 206,484	$ 200,792
Utility plant acquisition adjustments, net	450	359
	206,934	201,151
Non utility property	250	250
Current assets		
Cash	699	1,453
Customer accounts receivable	1,799	1,568
Allowance for uncollectible accounts	(67)	(58)
Unbilled revenues	2,118	2,137
Accounts receivable - associated companies	200	72
Materials and supplier	465	361
Deferred vacation pay	320	252
Other	640	215
	6,174	6,000
Regulatory and other long-term assets		
Deferred business service project expense	1,455	1,360
Regulatory asset-income taxes recoverable through rates	4,697	4,523
Debt and preferred stock expense	786	871
Deferred programmed maintenance	2,741	3,193
Preliminary survey and investigation	150	430
Other	8,305	5,802
	18,134	16,179
	$ 231,492	$ 223,580
Capitalization and Liabilities		
Capitalization		
Common stock	$ 36,569	$ 36,569
Paid-in capital	21	21
Retained earnings	25,178	24,407
Total common stockholder's equity	61,768	60,997
Preferred stock		
With mandatory redemption requirements	5,340	5,380
Without mandatory redemption requirements	1,570	1,570
Long-term debt	68,500	44,500
Total capitalization	137,178	112,447
Current liabilities		
Notes payable - associated companies	14,649	24,668
Current portion of long-term debt	-	13,000
Accounts payable	421	998
Accounts payable - associated companies	102	27
Taxes accrued	89	250
Interest accrued	1,457	853
Tar collections payable	315	215
Accrued vacation pay	320	252
Other	1,388	2,035
	18,741	42,298
Regulatory and other *long-term* liabilities		
Customer advances for construction	11,047	9,365
Deferred income taxes	31,233	28,174
Deferred investment tax credits	1,642	1,726
Accrued pension expense	1,675	1,362
Accrued postretirement benefits expense	299	299
Other	540	392
	46,436	41,318
Contributions in aid of construction		
Commitments and contingencies		
	$ 231,492	$ 223,580

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

KENTUCKY-AMERICAN WATER COMPANY
Statement of Income
(Dollars in thousands)

	Years Ended December 31,	
Operating revenues	$ 43,627	$ 41,478
Operating expenses		
Operation and maintenance	20,046	17,800
Depreciation and amortization	6,373	5,981
General taxes	2,201	1,831
	28,620	25,612
Utility operating income	15,007	15,866
Other income (deductions)		
Allowance for other funds used during construction	441	300
Miscellaneous other income	9	785
Miscellaneous other deductions	(557)	-
Income before interest charges and income taxes	14,900	16,951
Interest charges		
Interest on long-term debt	4,691	4,767
Interest on bank debt	252	486
Amortization of debt expense	87	79
Other interest	14	55
Allowance for borrowed funds used during construction	(211)	(149)
Income before income taxes	10,067	11,713
Provision for income tares		
Federal income taxes	3,186	3,711
State income taxes	859	992
Net income	6,022	7,010
Dividends on preferred stock	534	537
Net income to common stock	$ 5,488	$ 6,473

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

KENTUCKY-AMERICAN WATER COMPANY
Statement of Cash Flows
(Dollars in thousands)

	Years Ended December 31, 2002	2001
Cash flaws from operating activities		
Net income	$ 6,022	$ 7,010
Adjustments:		
Depreciation and amortization	6,373	5,981
Amortization, other	1,840	1,031
Provision for deferred income taxes	3,038	899
Amortization of deferred investment tax credits	(85)	(85)
Provision for losses on accounts receivable	258	200
Allowance for other funds used during construction	(441)	(300)
Pension expense in excess of funding	313	385
Deferred regulatory assets	(95)	(1,212)
Other, net	(2,165)	(3,071)
Changes in current assets and liabilities:		
Accounts receivable	(608)	2
Unbilled revenues	19	(52)
Materials and supplies	(104)	70
Other current assets	(493)	167
Accounts payable	(502)	(795)
Taxes accrued	(161)	69
Interest accrued	604	165
Other current liabilities	(479)	1,352
Net cash provided by operating activities	13,334	11,816
Cash flows from investing activities		
Construction expenditures	(13,904)	(13,794)
Allowance for other funds used during construction	441	300
Cost of removal, net of salvage	(400)	289
Payment for acquisition of public service district assets	-	(1,686)
Net cash used in investing activities	(13,863)	(14,891)
Cash flows from financing activities		
Proceeds from long-term debt issuance	24,000	15,500
Net borrowings (repayments) under line-of-credit agreement	(10,019)	3,837
Repayment of long-term debt	(13,000)	(13,000)
Customer advances and contributions, net of refunds	4,088	2,878
Redemption ofpreferred stock	(40)	(40)
Dividends paid	(5,251)	(5,333)
Debt issuance cost	(3)	(117)
Net cash provided by financing activities	(225)	3,725
Net increase (decrease) in cash and cash equivalents	(754)	650
Cash and cash equivalents at beginning of year	1,453	803
Cash and cash equivalents at end of year	$ 699	$ 1,453
Cash paid during the year for:		
Interest, net of capitalized amount	$ 4,353	$ 5,144
Income taxes	$ 1,217	$ 3,240

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

KENTUCKY-AMERICAN WATER COMPANY
Statement of Capitalization
(Dollars in thousands, except per share amounts)

	Call Price Per Share	December 31, 2002	2001
Common stockholder's equity			
Common stock - no par value, authorized 2,000,000 shares, issued and outstanding 1,567,391 shares in 2002 and 2001		$ 36,569	$ 36,569
Paid in capital		21	21
Retained earnings		25,178	24,407
		61,768	60,997
Preferred stocks - $100 par value, authorized 25,000 shares			
Without mandatory redemption requirements			
Cumulative preferred stock			
5.75% series, 4,700 shares issued and outstanding	$ 101.00	470	470
5.5% series, 5,000 shares issued and outstanding	$ 100.50	500	500
5.% series, 6,000 shares issued and outstanding	$ 101.00	600	600
		1,570	1,570
With mandatory redemption requirements			
Cumulative preferred stock			
7.9% series, 8,400 and 8,800 shares issued and outstanding in 2002 and 2001, respectively	$ 100.00	840	880
8.47% series, 45,000 shares issued and outstanding	$ 100.00	4,500	4,500
		5,340	5,380
Long-term debt			
General mortgage bonds			
7.21% series due 2002		-	13,000
6.79% series due 2005		5,500	5,500
6.96% series due 2023		7,000	7,000
7.15% series due 2027		7,500	7,500
6.99% series due 2028		9,000	9,000
Notes payable to affiliate			
5.65% series due 2007		24,000	-
6.87% series due 2011		15,500	15,500
		68,500	57,500
Less: Current portion of long-term debt		-	13,000
Long-term debt net of current maturities		68,500	44,500
Total capitalization		$ 137,178	$ 112,447

The accompanying notes are an integral part of these financial statements

KENTUCKY-AMERICAN WATER COMPANY
Statement of Retained Earnings and Stockholders' Equity
(Dollars in thousands, except per share amounts)

	Common Stock		Paid-in	Retained	Stockholders'
	Shares	Par Value	Capital	Earnings	Equity
Balance at December 31, 2000	1,567,391	$ 36,569	$ 21	$ 22,730	$ 59,320
Net income				7,010	7,010
Dividends					
Preferred stock	-	-		(537)	(537)
Common stock, $2.60 per share	-	-		(4,796)	(4,796)
Balance at December 31, 2001	1,567,391	36,569	21	24,407	60,997
Net income			-	6,022	6,022
Dividends					
Preferred stock			-	(534)	(534)
Common stock, $3.06 per share			-	(4,717)	(4,717)
Balance at December 31, 2002	1,567,391	$ 36,569	$ 21	$ 25,178	$ 61,768

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

KENTUCKY-AMERICAN WATER COMPANY
Notes to Financial Statements
December 31,2002 and 2001
(Dollars in thousands)

Note 1 - Organization and Operation

Kentucky-American Water Company (the Company) provides water service to approximately 105,000 customers and wastewater service to approximately 84 customers. These services are provided in 10 communities located in 10 counties in the state of Kentucky. As a public utility operating in Kentucky, the Company functions under rules and regulations prescribed by the Public Service Commission of the Commonwealth of Kentucky (the Commission). The Company is a wholly-owned subsidiary of American Water Works Company, Inc. (American).

Note 2 - Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Actual results could differ from these estimates.

Regulation

The Company has incurred various costs and received various credits, which have been reflected as regulatory assets and liabilities on its balance sheet. Accounting for such costs and credits as regulatory assets and liabilities is in accordance with Statement of Financial Accounting Standards No. 71, "Accounting for the Effects of Certain Types of Regulation" (SFAS No. 71). This statement sets forth the application of generally accepted accounting principles for those companies whose rates are established by or are subject to approval by an independent third-party regulator. Under SFAS No. 71, regulated companies defer costs and credits on the balance sheet as regulatory assets and liabilities when it is probable that those costs and credits will be recognized in the rate-making process in a period different from the period in which they would have been reflected in income by an unregulated company. These deferred regulatory assets and liabilities are then reflected in the income statement in the period in which the same amounts are reflected in the rates charged for service.

KENTUCKY-AMERICAN WATER COMPANY
Notes to Financial Statements
***December* 31,2002 and 2001**
(Dollars in thousands)

Note 2 (continued)

Property, Plant and Equipment

Additions to utility plant and replacements of retirement units of property are capitalized. Costs include material, direct labor and such indirect items as engineering and supervision, payroll taxes and benefits, transportation and an allowance for funds used during construction. The costs incurred to acquire and internally develop computer software for internal use are capitalized as a unit of property. Repairs, maintenance and minor replacements of property are charged to current operations. The cost of property units retired in the ordinary course of business plus removal cost (net of salvage) is charged to accumulated depreciation. The cost of property, plant and equipment is depreciated using the straight-line method. The depreciation rates, based on the average balance of depreciable property, were 2.63 % in 2002 and 2.69% in 2001.

In accordance with the Commission's regulations, depreciation on contributed facilities is charged to contributions in aid of construction. Such depreciation amounted to $784 in 2002 and $642 in 2001.

Cash and Cash Equivalents

Substantially all of the Company's cash is invested in interest bearing accounts. The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. There were no cash equivalents held at December 31,2002 or 2001.

Materials and Supplies

Materials and supplies are stated at average cost.

Regulatory and Long-Term Assets

Deferred business services project expenses consist of reengineering and start-up activities for consolidated customer and shared administrative service centers that are being established by American. These costs are being deferred as it is expected that these costs will be recovered in the rates charged for utility service in the future.

The Company has deferred $1,703 related to the cost of increased security measures that were implemented to secure facilities after the terrorist attacks on September 11,2001. These costs are being deferred as it is expected that these costs will be recovered in the rates charged for utility service in the future.

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

KENTUCKY-AMERICAN WATER COMPANY
Notes to Financial Statements
December 31,2002 and 2001
(Dollars in thousands)

Note 2 (continued)

tax depreciation on property placed in service before the adoption by the Commission of full normalization for rate-making purposes.

The regulatory asset for income taxes recoverable through rates is net of the reduction expected in future revenues as deferred taxes previously provided, attributable to the difference between the state and federal income tax rates under prior law and the current statutory rates, reverse over the average remaining service lives of the related assets.

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

Preliminary survey and investigation charges generally relate to future construction projects. Management believes these costs will ultimately be recovered through rates.

Programmed maintenance costs are deferred and amortized to current operations on a straight-line basis over a period ranging between five and fifteen years, as authorized by the Commission in their determination of rates charged for service.

Other Current Liabilities

Other current liabilities at December 31,2002 and 2001 include payables of $600 and $929, respectively, which represent checks issued but not presented to the bank for payment.

Advances and Contributions in Aid of Construction

The Company may receive advances and contributions to fund construction necessary to extend service to new areas. As determined by the Commission, advances for construction **are** refundable for limited periods of time as new customers begin to receive service. 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 and is not depreciated for rate-making purposes. Generally, advances and contributions received during the period of January 1, 1987 through June 12, 1996 have been included in taxable income and the related property is depreciable for tax purposes. As a result of a tax law change, advances and contributions received subsequent to June 12, 1996 are excluded from taxable income and the related property is not depreciable for tax purposes.

KENTUCKY-AMERICAN WATER COMPANY
Notes to Financial Statements
December 31,2002 and 2001
(Dollars in thousands)

Note 2 (continued)

On January 11,2001 the Internal Revenue Service issued regulations that excluded lateral service lines from its definition of contributions in aid of construction that are not included in taxable income. These customer connection fees are defined as the cost of installing a connection or service line from the Company's main lines to the lines owned by the customer. The regulations were effective immediately, but the Company does not have customer connection fees.

Recognition of Revenues

Water service revenues for financial reporting purposes include amounts billed to customers on a cycle basis and unbilled amounts based on estimated usage from the date of the latest meter reading to the end of the accounting period.

Income Taxes

The Company, its parent and affiliates participate in a consolidated federal income tax retum. Federal income tax expense for financial reporting purposes is provided on a separate retum basis, except that the federal income tax rate applicable to the consolidated group is applied to separate company taxable income and the benefit of net operating losses, if any, is recognized currently.

Certain income and expense items are accounted for in different time periods for financial reporting than for income tax reporting purposes. Deferred income taxes have been provided on the difference between the tax bases of assets and liabilities and the amounts at which they are carried in the financial statements. These deferred income taxes are based on the enacted tax rates anticipated to be in effect when such temporary differences are expected to reverse. Regulatory assets and liabilities are recognized for the effect on revenues expected to be realized as the tax effects of temporary differences previously flowed through to customers reverse.

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

Allowance for Funds Used During Construction (AFUDC)

AFUDC is a non-cash adjustment to income with a corresponding charge to utility plant, which represents the cost of borrowed funds and a retum on equity funds devoted to plant under construction. AFUDC is recorded to the extent permitted by the Commission.

KENTUCKY-AMERICAN WATER COMPANY
Notes to Financial Statements
December 31,2002 and 2001
(Dollars in thousands)

Note 2 (continued)

Environmental Costs

Environmental expenditures that relate to current operations or provide a future benefit are expensed or capitalized as appropriate. Remediation costs that relate to an existing condition caused by past operations are accrued when it is probable that these costs will be incurred and can be reasonably estimated. There were no remediation costs accrued at December 31,2002 and 2001.

Asset Impairment

Long-lived assets and certain identifiable intangible assets held and used by the Company are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets, on a separate entity basis, may not be recoverable. If the sum of the future cash flows expected to result from the use of the assets and their eventual disposition is less than the carrying amount of the assets, an impairment loss is recognized. Measurement of an impairment loss would be based on the fair value of the assets. A regulatory asset is charged to earnings if and when future recovery in rates of that asset is no longer probable.

Reclassifications

Certain reclassifications have been made to conform previously reported data to the current presentation.

Note 3 - Utility Plant

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

	2002	2001
Water plant		
Sources of supply	$ 7,344	$ 6,926
Treatment and pumping	45,561	45,017
Transmission and distribution	133,231	125,485
Services, meters, and fire hydrants	50,763	47,024
General structures and equipment	16,605	16,167
Construction work in progress	7,223	8,954
	260,727	249,573
Less - accumulated depreciation	(54,243)	(48,781)
	$206,484	$200,792

KENTUCKY-AMERICAN WATER COMPANY
Notes to Financial Statements
December 31,2002 and 2001
(Dollars in thousands)

Note 3 (continued)

Depreciation expense amounted to $5,620 in 2002 and $5,374 in 2001.

Note 4 -Preferred Stocks

Preferred stock agreements have annual minimum sinking fund payments of $40 in 2003 through 2007. The 7.9% series sinking fund payment of $40 is at the option of the Company.

Note 5 - Long-Term Debt

Maturities of long-term debt will amount to $0 in 2003 and 2004, $5,500 in 2005, $0 in 2006 and $24,000 in 2007.

The general mortgage bond indentures, as supplemented, contain clauses restricting the declaration of common stock dividends and other distributions on capital stock if common stockholder's equity falls below a specified amount. There were no restrictions at December 31, 2002.

The general mortgage bonds are issuable in series. No bonds senior to the general mortgage bonds may be issued so long as the general mortgage bonds are outstanding. The amount of bonds authorized is unlimited as long as long-term debt does not exceed 65% of capitalization. Long-term debt is secured by utility plant.

The senior notes are unsecured and were issued to American Water Capital Corp. (AWCC) for the principal amount. AWCC provided the funding for this note by itself issuing senior notes to institutional investors at a price equal to the principal amount.

***Note* 6 - Affiliate Borrowings**

During 2002, the Company maintained a line of credit through AWCC, an affiliate (see Note 12). AWCC has a 364-day $500 million revolving credit agreement with a group of 11 domestic and international banks. No compensating balances are required under the agreement. AWCC also issues commercial paper, and the revolving credit agreement also supports these borrowings.

At December 31,2002 and 2001, there were $14,649 and $24,668 of short-term borrowings outstanding, respectively. The weighted average annual interest rate on these

KENTUCKY-AMERICAN WATER COMPANY
Notes to Financial Statements
December **31,2002** and **2001**
(Dollars in thousands)

Note 6 (continued)

borrowings was 2.27% and 5.60% respectively. The unused line of credit at December 31,2002 was $7,851.

Note **7** - General Taxes

Components of general tax expense for the years presented in the statement of income are as follows:

	2002	**2001**
Gross receipts and franchise	$ 75	$ 74
Property and capital stock	1,685	1,313
Payroll	441	444
	$2,201	$1,831

Note **8** - Income Taxes

Components of income tax expense for the years presented in the statement of income are as follows:

	2002	**2001**
State income taxes:		
Current	$ 407	$ 782
Deferred		
Non-current	452	210
	$ 859	$ 992
Federal income taxes:		
Current	$ 685	$3,107
Deferred		
Non-current	2,586	689
Amortization of deferred investment tax credits	(85)	(85)
	$3,186	$3,711

KENTUCKY-AMERICAN WATER COMPANY
Notes to Financial Statements
December 31,2002 and 2001
(Dollars in thousands)

Note 8 (continued)

A reconciliation of income tax expense at the statutory federal income tax rate to the actual income tax expense is as follows:

	2002	2001
Income tax at statutory rate of 35%	$3,523	$4,100
Increases (decreases) resulting from -		
State taxes, net of federal income taxes	558	645
Flow through differences	10	72
Amortization of investment tax credits	(85)	(85)
Other, net	39	(29)
Actual income tax expense	$4,045	$4,703

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

	2002	2001
Deferred tax assets:		
Advances and contributions	$ 4,038	$ 3,927
Deferred investment credits	662	731
Deferred OPEB	121	121
Other - Pension	676	550
Other	1,111	2,164
	6,608	7,493
Deferred tax **liabilities:**		
Utility plant, principally due to depreciation differences	31,571	29,342
Utility plant acquisition adustments	182	145
Income taxes recoverable through rates	1,031	1,013
Deferred security costs	687	120
Deferred financial and customer service costs	222	184
Other	4,148	4,863
	37,841	35,667
Net deferred tax liability	$ 31,233	$ 28,174

No valuation allowances were required on deferred tax assets at December 31,2002 and 2001, as management believes it is more likely than not that these assets will be realized.

KENTUCKY-AMERICAN WATER COMPANY
Notes to Financial Statements
December 31,2002 and 2001
(Dollars in thousands)

Note 9 - Rate Matters

As necessary, the Company applies to the Commission for changes in the rates charged for service. The rate increase request is based on the level of operating expenses and capital costs that are expected to be in effect when the rates become effective. The revenues requested are based on forecasted sales, operating expenses and investments for the test year selected by the Company.

The Company has received approval from the Commission to increase its rates for service as follows:

Effective Dates	Requested Annual Effect on Revenues	Estimated Annual Effect on Revenues Granted	Estimated Revenue Realized in 2001
05/09/01	$4,685	$2,568	$2,368

On April 28,2000, the Company filed a rate application with the Commission, requesting $5.034 million in additional annual revenues that was subsequently revised to $4.685 million or 11.69%.

On December 12,2000, the Commission issued an Order adjusting its original Order dated November 27,2000. The adjusted order corrected errors in the initial ruling and reduced the allowed revenue increase from $2.518 million to $2.171 million to be effective for service rendered on and after November 27,2000.

On May 9,2001, a final decision was issued which addressed appeals from reconsideration made by the Company and the State Attorney General. The final decision adjusted the authorized revenue increase from $2.171 to $2.568 million or 6.42% of total operating revenues.

Note 10 - Employee Benefit Plans

Employees' Stock Ownership Plan

The Company participates in an Employees' Stock Ownership Plan sponsored by American, which provides for beneficial ownership of American common stock by all associates who are not included in a bargaining unit. Each participating associate can elect to contribute an amount that does not exceed 2% of their wages. In addition to the associate's participation, the Company makes a contribution equivalent to ½% of each participant's qualified compensation,

KENTUCKY-AMERICAN WATER COMPANY
Notes to Financial Statements
December 31, 2002 and 2001
(Dollars in thousands)

Note 10 (continued)

and matches 100% of the contribution by each participant. The Company expensed contributions of $59 for 2002 and $62 for 2001 that it made to the plan. See Note 16 regarding the sale of American's common stock.

Savings Plan for Employees

The Company participates in a 401(k) Savings Plan for Employees sponsored by American. All Associates can make contributions that are invested at their direction in one or more funds including a fund consisting entirely of American common stock. The Company matches 50% of the first 4% of each associate's wages contributed to the plan. The Company expensed matching contributions to the plan totaling $93 for 2002 and $85 for 2001. All of the Company's matching contributions are invested in the fund of American common stock. See Note 16 regarding the sale of American's common stock.

Note 11 - Postretirement Benefits

Pension Benefits

The Company participates in a noncontributory defined benefit pension plan sponsored by American covering substantially all associates. Benefits under the plan are based on the associate's years of service and average annual compensation for those 60 consecutive months of employment, which yield the highest average. Pension cost of the Company is based on an allocation from American of the total cost related to the plan. Information regarding accumulated and projected benefit obligations is not prepared at the subsidiary level. The Company's funding policy is to contribute at least the minimum amount required under the Employee Retirement Income Security Act of 1974. The Company made contributions to the plan of $216 in 2002 and no contributions in 2001.

Postretirement Benefits Other Than Pensions

The Company participates in an American plan that provides certain life insurance benefits for retired associates and certain health care benefits for retired associates and their dependents. Substantially all associates may become eligible for these benefits if they reach retirement age while still working for the Company. Retirees and their dependents under age 65 are covered by a point-of-service managed care plan that requires co-payments or an HMO. Associates who elect to retire prior to attaining age 65 are generally required to make contributions towards their medical coverage until attaining age 65. Retirees and their dependents age 65 and over are covered by a Medicare supplement plan. Costs of the Company are based on an allocation from American of the total cost related to the plan.

KENTUCKY-AMERICAN WATER COMPANY
Notes to Financial Statements
December 31,2002 and 2001
(Dollars in thousands)

Note 11 (continued)

Information regarding accumulated and projected benefit obligations is not prepared at the subsidiary level. The Company made contributions to trust funds established for these postretirement benefits of $560 in 2002 and $561 in 2001. The Company's policy is to fund postretirement benefits costs accrued.

Note 12 - Related Party Transactions

American Water Works Service Company, Inc. (AWWS), an affiliate, provides certain management services to the Company (administration, accounting, data processing, engineering, etc.) and other operating water companies in the American Water Works System on an at-cost, not-for-profit basis in accordance with a management and service agreement. Purchases of such services by the Company were accounted for as follows:

	2002	2001
Included in operation and maintenance expense as a charge against income	$2,532	$1,535
Capitalized in various balance sheet accounts	654	765
	$3,186	$2,300

The Company provided workspace and information system support for associates of the Southeast Region of AWWS. Charges for direct costs and indirect overhead costs associated with these associates are billed to AWWS on an at-cost, not for profit basis, which amounted to $15 in 2002 and $43 in 2001. At December 31,2002, there was no outstanding receivable from this affiliate for these services.

Some of the Company's associates have performed services at cost to AWWS relating to the establishment by American of consolidated customer and shared administrative service centers. The total amount of these services was $148 in 2002 and $217 in 2001. At December 31,2002, net amounts receivable from this affiliate for these services were $47.

The Company has three operating agreements with American Water Services, Inc. (AWS), an affiliate, for the lease of granular activated carbon at one of the Company's water treatment plants. The agreements provide for AWS to regenerate the spent material and return it to the water treatment plant where it originated. Under the terms of the agreements, AWS will provide carbon for a period of thirty-six months beginning in each of March 1999,2000, and

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Note 12 (continued)

2001. The carbon is scheduled for replacement at thirty-six month intervals and is warranted to perform to specific standards during that period. The Company paid $87 in 2002 and $82 in 2001 to AWS under these agreements.

The Company maintains a line of credit through AWCC, an affiliate. The company paid AWCC fees of $61 in 2002 and $47 in 2001, preliminary costs of long-term financings of $3 in 2002 and $1 17 in 2001 and interest on borrowings of $252 in 2002 and $486 in 2001.

Note 13 - Fair Values of Financial Instruments

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

Current assets and current liabilities: The carrying amount reported in the balance sheet for current assets and current liabilities approximates their fair value.

Preferred stocks with mandatory redemption requirements and long-term debt: The fair values of the Company's preferred stocks with mandatory redemption requirements and long-term debt are estimated using discounted cash flow analyses based on the Company's current incremental financing rates for similar types of securities.

The canying amounts and fair values of the Company's financial instruments at December 31 are as follows:

	2002		2001	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Preferred stock with mandatory redemption requirements	$ 5,340	$ 5,287	$ 5,380	$ 5,805
Long-term debt, including current maturities	68,500	69,256	57,500	55,961

Note 14 - Operating Leases

The Company has entered into operating leases involving certain facilities and equipment. Rental expenses under operating leases were $176 in 2002 and $134 in 2001. The operating leases for their equipment expire over the next six years.

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Note 14 (continued)

At December 31,2002, the minimum annual future rental commitments under operating leases that have initial or remaining non-cancellable lease terms in excess of one year are $120 in 2004, $81 in 2005, $38 in 2006 and $22 in 2007.

Note 15 - Commitments and Contingencies

The Company's construction program for 2003 is estimated to cost approximately $13,123. Commitments have been made in connection with certain projects included in this program.

In connection with the merger of American with RWE Aktiengesellschaft (RWE, see Note 16), the Company is subject to an order from the Commission that requires that no rate filings will be submitted until March 2004.

The Company is routinely involved in legal actions. In the opinion of management, none of these matters will have a material adverse effect, if any, on the financial position or results of operations of the Company.

Note 16 - Subsequent Event - Merger with RWE Aktiengesellschaft

On September 16, 2001, American entered into an Agreement and Plan of Merger (the Agreement) with RWE and Thames Water Aqua Holdings GmbH (Thames), which is RWE's holding company for its global water business, to merge with a subsidiary of RWE and become a wholly owned indirect subsidiary of RWE. The transaction was approved at a special meeting of the stockholders of American on January 17, 2002. On January 10, 2003, Apollo Acquisition Company, a Delaware corporation, merged (the Merger) with and into American, pursuant to the Agreement, with American surviving the Merger. Pursuant to the Agreement, each issued and outstanding share of common stock, par value $1.25 per share, of American has been canceled and converted into the right to receive $46.00 in cash without interest, plus a stub period dividend of $0.2153333 per share. As a result of the Merger, American became a wholly owned subsidiary of Thames Water Aqua US Holdings, Inc., a wholly owned subsidiary of Thames.