

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 maintenance	15,467	16,262
Depreciation and amortization	5,184	4,817
Taxes on operating income		
General	1,762	1,711
State income	942	1,017
Federal income	3,520	3,819
	<u>26,875</u>	<u>27,626</u>
Utility operating income	11,845	11,478
Other income		
Allowance for other funds used during construction	397	720
Miscellaneous other income	12	62
	<u>12,254</u>	<u>12,260</u>
Other deductions		
Miscellaneous other deductions	1,786	358
Taxes on other income and deductions		
State income	(146)	(24)
Federal income	(568)	(92)
	<u>1,072</u>	<u>242</u>
Income before interest charges	<u>11,182</u>	<u>12,018</u>
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)
	<u>5,523</u>	<u>4,884</u>
Net income	<u>\$ 5,659</u>	<u>\$ 7,134</u>

STATEMENT OF RETAINED EARNINGS

Retained earnings at beginning of year	\$ 21,686	\$ 20,252
Net income	5,659	7,134
	<u>27,345</u>	<u>27,386</u>
Dividends		
Preferred stock	540	543
Common stock	4,075	5,157
	<u>4,615</u>	<u>5,700</u>
Retained earnings at end of year	<u>\$ 22,730</u>	<u>\$ 21,686</u>

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 amortization	5,184	4,817
Amortization, 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 for 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 revenues	(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	<u>11,342</u>	<u>13,046</u>

Cash flows from investing activities

Construction expenditures	(11,829)	(18,386)
Allowance for other funds used during construction	<u>397</u>	<u>720</u>
Cost of removal, net of salvage	<u>313</u>	<u>(158)</u>
Net cash used in investing activities	(11,119)	(17,824)

Cash flows from financing activities

Repayment of long-term debt	(12,000)	-
Net borrowing under line-of-credit agreement	15,114	5,716
Dividends paid	(4,615)	(5,700)
Customer advances and contributions, net of refunds	1,621	3,926
Redemption of preferred stock	(48)	(48)
Net cash provided by financing activities	<u>72</u>	<u>3,894</u>
Net increase in cash and cash equivalents	295	(884)
Cash and cash equivalents at beginning of year	<u>508</u>	<u>1,392</u>
Cash and cash equivalents at end of year	<u>\$ 803</u>	<u>\$ 508</u>
Cash paid during the year for:		
Interest, net of capitalized amount	<u>\$ 5,835</u>	<u>\$ 4,818</u>
Income taxes	<u>\$ 704</u>	<u>\$ 2,996</u>

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

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
		<u>59,320</u>	<u>58,276</u>
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
		<u>1,570</u>	<u>1,570</u>
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
		<u>5,420</u>	<u>5,468</u>
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
		<u>55,000</u>	<u>67,000</u>
Less: Current portion of long-term debt		13,000	4,000
		<u>42,000</u>	<u>63,000</u>
Long-term debt net of current maturities		42,000	63,000
Total capitalization		<u>\$ 108,310</u>	<u>\$ 128,314</u>

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 IN SHARE AMOUNTS)

	COMMON STOCK		Paid-in Capital	COMMON	
	Shares	Par Value		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	<u>1,567,391</u>	<u>36,569</u>	<u>21</u>	<u>21,686</u>	<u>58,276</u>
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	<u>\$1,567,391</u>	<u>\$36,569</u>	<u>\$ 21</u>	<u>\$22,730</u>	<u>\$59,320</u>

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 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, 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
	<u>232,186</u>	<u>222,330</u>
Less - accumulated depreciation	<u>(42,762)</u>	<u>(38,598)</u>
	<u>\$189,424</u>	<u>\$183,732</u>

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
	<u>\$1,762</u>	<u>\$1,711</u>

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	<u>\$ 796</u>	<u>\$ 993</u>
Federal income taxes:		
Current	\$ 216	\$ 2,439
Deferred		
Current	-	4
Non-current	2,821	1,369
Amortization of deferred investment tax credits	<u>(85)</u>	<u>(85)</u>
	<u>2,952</u>	<u>3,727</u>

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	<u>\$3,748</u>	<u>\$4,720</u>

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
	<u>\$14,912</u>	<u>\$14,523</u>
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
	<u>\$42,183</u>	<u>\$38,117</u>
Net deferred tax liabilities	<u>\$27,271</u>	<u>\$23,594</u>

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

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

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 AWWWS, 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 AWWWS in 2000. Charges for direct costs and indirect overhead costs associated with these associates are billed to AWWWS 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 AWWWS 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		1999 CARRYING	
	Amount	Fair Value	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	<u>\$ 184,115</u>	<u>\$ 176,959</u>	<u>\$ 166,219</u>	<u>\$ 160,639</u>	<u>\$ 151,023</u>	<u>\$ 139,225</u>	<u>\$ 107,322</u>
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 at 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	<u>55,000</u>	<u>67,000</u>	<u>67,000</u>	<u>64,000</u>	<u>62,500</u>	<u>62,500</u>	<u>50,160</u>
	<u>\$ 121,310</u>	<u>\$ 132,314</u>	<u>\$ 130,928</u>	<u>\$ 120,350</u>	<u>\$ 115,076</u>	<u>\$ 113,842</u>	<u>\$ 84,743</u>

Customers served (000)

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

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*	<u>1,822</u>	<u>1,998</u>	<u>1,860</u>	<u>1,759</u>	<u>1,772</u>	<u>1,780</u>	<u>1,687</u>
	<u>12,854</u>	<u>13,360</u>	<u>12,975</u>	<u>12,272</u>	<u>12,518</u>	<u>12,220</u>	<u>11,089</u>

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
	<u>\$ 38,720</u>	<u>\$ 39,104</u>	<u>\$ 37,744</u>	<u>\$ 35,249</u>	<u>\$ 32,664</u>	<u>\$ 32,087</u>	<u>\$ 23,370</u>

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 taxes *	2.9	3.2	3.2	3.0	2.7	2.7	2.1
On total interest before income taxes*	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

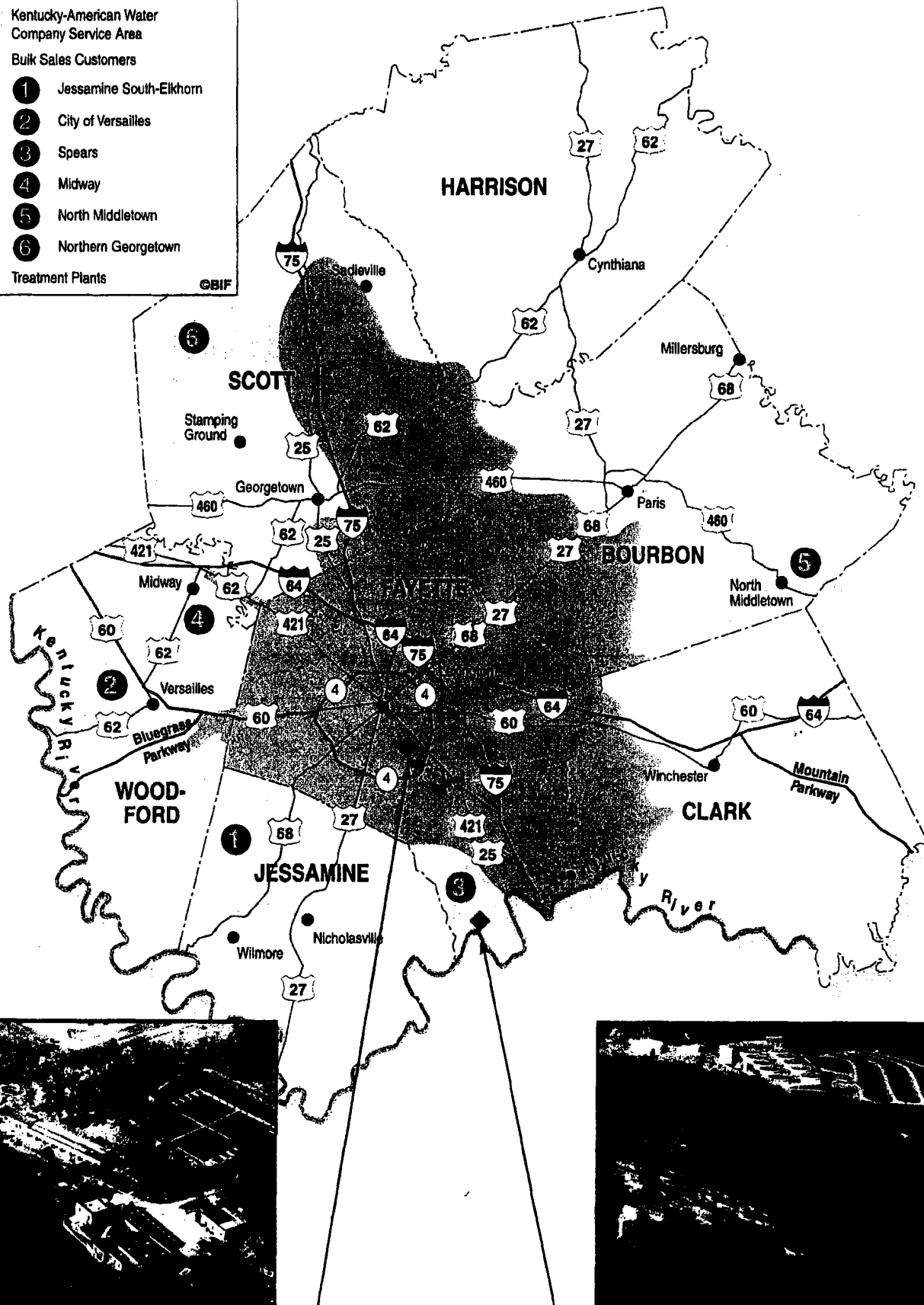
 Kentucky-American Water Company Service Area

Bulk Sales Customers

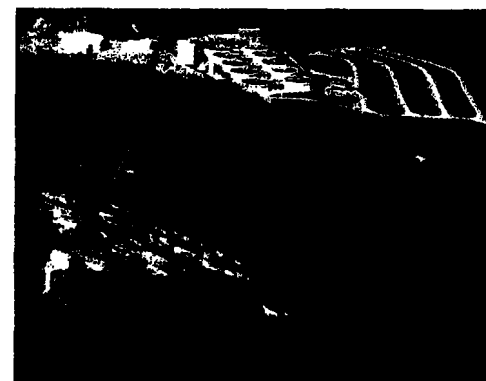
-  Jessamine South-Eikhorn
-  City of Versailles
-  Spears
-  Midway
-  North Middletown
-  Northern Georgetown

 Treatment Plants

©BIF



Richmond Road Treatment Plant



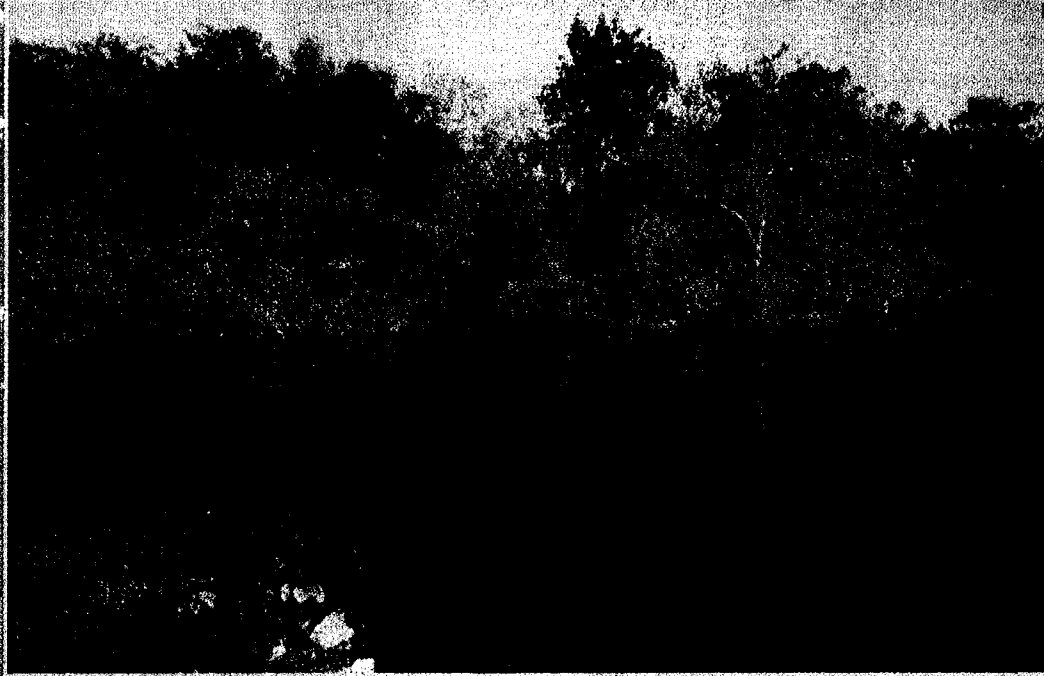
Kentucky River Treatment Plant



Kentucky American Water

www.kawc.com

Water. It's worth using wisely.



Water for Life

 Kentucky-American Water Company

Kentucky-American Water Company – Water For Life

Who is Kentucky-American Water Company?

Kentucky-American Water Company, based in Lexington, provides water service to approximately 280,000 people. Our service area includes most of Fayette County (including Lexington), the eastern half of Scott County (including Sadieville and the Toyota Motor Manufacturing plant), and portions of Bourbon, Clark, Harrison, Jessamine, and Woodford counties. Kentucky-American provides water for drinking, cooking, cleaning, and performing numerous other daily activities. Kentucky-American also provides water for businesses and manufacturers as well as for fire protection. In fact, the company maintains more than 5,700 fire hydrants for the city of Lexington.

Kentucky-American Water Company was incorporated under the laws of the Commonwealth of Kentucky in 1882 as Lexington Hydraulic and Manufacturing Company. The company's name was changed to the Lexington Water Company in 1922, and to Kentucky-American Water Company in 1973.

Kentucky-American Water Company is a wholly-owned subsidiary of American Water Works Company, Inc., the nation's largest and most geographically diversified investor-owned water system. American Water Works Company's 23 utility subsidiaries serve more than seven million people in over 870 communities in 22 states. American Water System stock is traded under the symbol "AWK" on the New York Stock Exchange.



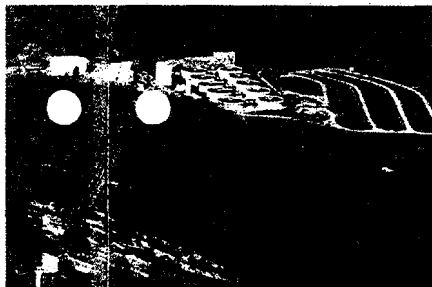
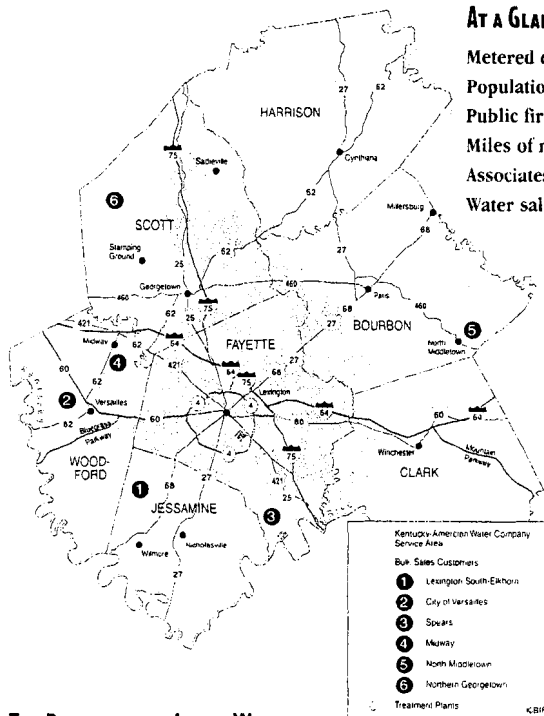
© H. Mark Weidman

The Benefits of a Large Water System

Kentucky-American Water Company and its customers benefit from its affiliation with American Water Works Company, Inc. The American system's purchasing power translates into lower prices for pipes, valves, hydrants, meters, brass goods, treatment chemicals, liability and workers compensation insurance, and group health insurance. Its centralized quality control and research laboratory in Belleville, Illinois, which is totally dedicated to drinking water analysis, provides valuable information for all subsidiaries of the American system. Members of the American Water Works family also benefit from valuable, system-wide educational programs coordinated at the company's corporate center in Voorhees, New Jersey.

At a Glance

Metered customers	.....	89,669
Population served	.....	280,000
Public fire hydrants	.....	5,768
Miles of main	.....	1,365
Associates	.....	152
Water sales (1997)	.....	12.3 billion gallons



Source of Water Supply

Lexington is one of the largest cities in the United States located away from a major source of water. The majority of its water supply, 80% in fact, is withdrawn 12 miles from the city at the Kentucky River. The remaining supply comes from Jacobson Reservoir. Kentucky-American customers use an average of approximately 40 million gallons of water daily. The company treats the water supply at its two treatment plants, one of which is located at the Kentucky River and the other behind the company's headquarters on Richmond Road. These facilities are capable of treating up to 65 million gallons of water per day.

Planning for the Future

Kentucky-American Water Company is working today to make sure that quality water service continues to be available for Central Kentucky's future generations. The city of Lexington and many surrounding communities have experienced significant growth during the past 20 years, and continue to grow. In fact, the U.S. Census Bureau projects that Lexington may be Kentucky's largest city by the year 2000, a distinction that has been held by the city of Louisville for more than 150 years.

To ensure that an ample water supply is available for residential and commercial use as well as for adequate fire protection in the community, Kentucky-American has proposed to augment the community's water supply through the Bluegrass Water Project, a \$48.5 million dollar endeavor that involves constructing a 52.5-mile pipeline. The pipeline will link Kentucky-American customers to an auxiliary treated water source from the Ohio River. The Bluegrass Water Project is the most cost-effective, environmentally safe, and feasible solution to the water supply deficit that the ever-growing Central Kentucky region faces. Pending approval by Kentucky's Public Service Commission, this pipeline could be operational by 2001.



A Quality Product

Kentucky-American Water Company customers can be confident that they receive quality water. The company's in-house team of water quality experts oversees the water treatment process and manages Kentucky-American's water quality research programs. Kentucky-American stays abreast of proposed state and federal drinking water regulations to ensure that the company's water systems comply with current standards. In fact, Kentucky-American goes beyond what is required and routinely tests its water for the presence of regulated as well as non-regulated contaminants.

Kentucky-American Water Company is a voluntary member of the U.S. Environmental Protection Agency's Partnership for Safe Water program, which was formed in 1995 to help water suppliers improve water treatment and water quality. In 1998 the company received two Director's Awards for its distinction as one of the few companies in the United States to complete — for all of its treatment plants — the Phase III Self-Assessment requirements of this program.



Kentucky American Water Company

2300 Richmond Road
606-269-2386

Lexington, Kentucky 40502
www.kawc.com



A GOOD NEIGHBOR

Kentucky American Water Company believes in being an active member of the community it serves. In addition to providing a quality product and service, being a good employer, and paying taxes, the company is committed to enhancing education, providing and fostering leadership, protecting the environment, and encouraging volunteerism.

Kentucky American is especially committed to promoting science education, which is most apparent by the company's extensive involvement in the annual Kentucky American Water Company Science Fair. This event is solely sponsored by the company and coordinated by Fayette County Public Schools.

Kentucky American associates are encouraged to take active roles in their community through participation in numerous projects that focus on

KENTUCKY-AMERICAN'S MISSION

Kentucky American Water Company's mission is to enhance the company's value to customers, associates, shareholders, the communities we serve and the environment which surrounds us by providing the best quality water service at the lowest price to our existing and future customers; providing a corporate environment that maximizes professional development, demanding high expectation and achievement; providing consistent growth in shareholder value by investing in water and wastewater utility companies; providing leadership and corporate citizenship in the communities we serve; and providing education and related initiatives to safeguard the environment.

...

education and environmental awareness, as well as through civic and social memberships.

Kentucky American's civic-mindedness is also demonstrated in other ways, including the company's significant support of McConnell Springs, the site of Lexington's birthplace and the first source of water for the community; Jacobson Park, which Kentucky American leased to the city of Lexington in 1968, for \$10 a year, through 2018 (the park is named after Kentucky American General Manager Ernest E. Jacobson); and the use of one of Kentucky American's 10 water storage tanks as a unique canvas for an 18,000-square-foot equine mural that welcomes visitors to the "horse capital of the world."

...

KENTUCKY-AMERICAN'S VISION

We envision an environment where every member of our team is dedicated to a common mission, empowered with the necessary authority, responsibility, and resources to be caring and responsive to the needs of our customers and other team members.

This vision statement reflects the consensus of all Kentucky American Water Company associates, each of whom play a role in charting the company's course for the future.

...



● KENTUCKY-AMERICAN WATER COMPANY
A Constant Presence

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.

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 investment.

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 MISSION

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

OUR VALUES

We believe in, and will not compromise

Our integrity

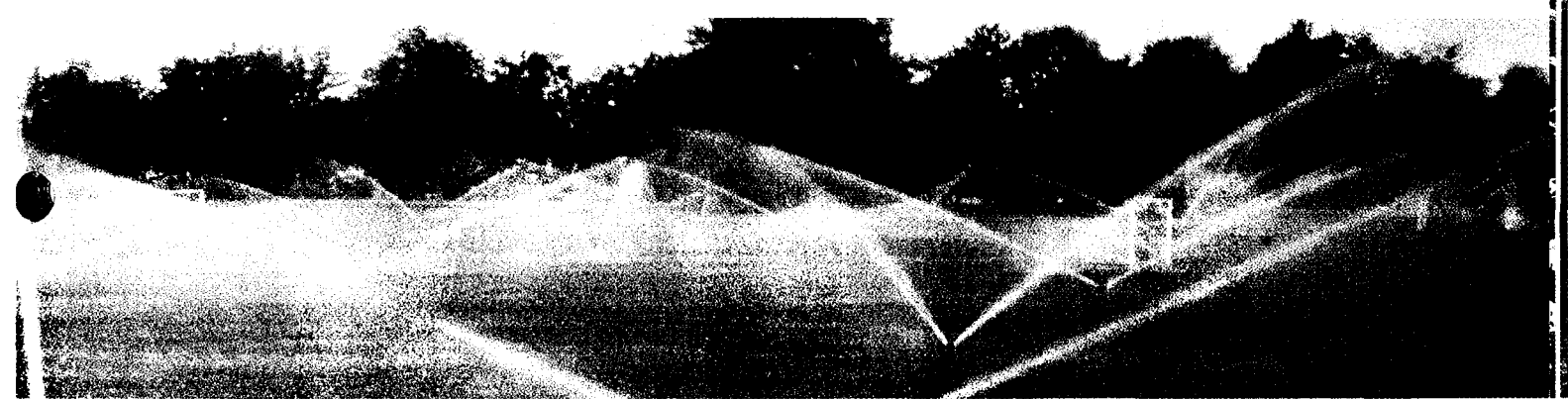
Our respect for our customers, associates and investors

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

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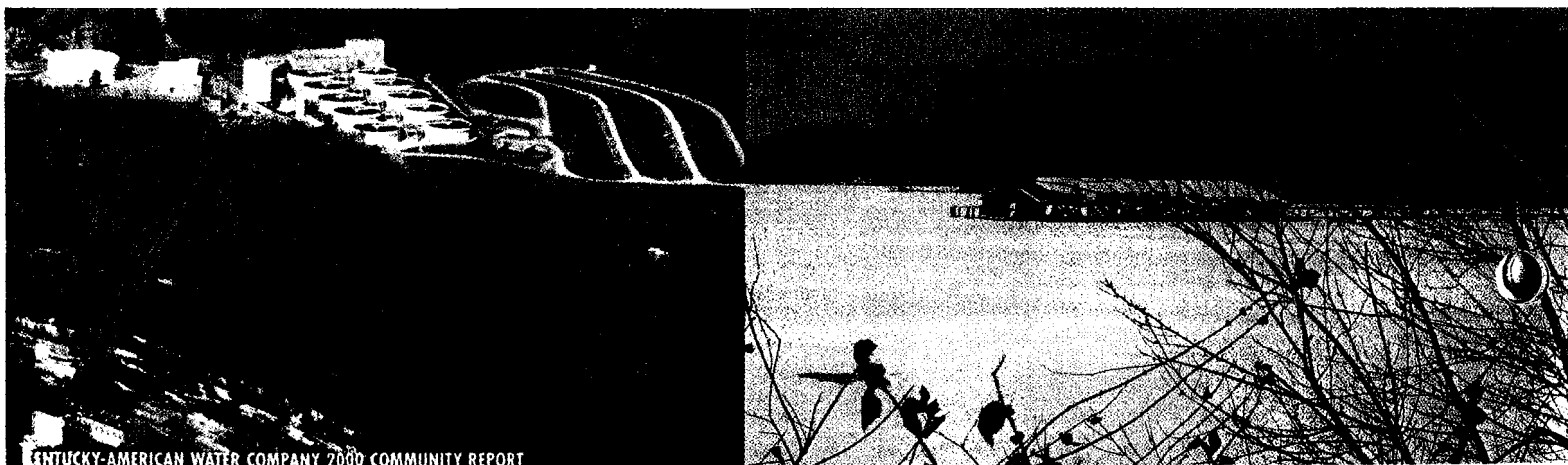
KENTUCKY-AMERICAN WATER COMPANY PROFILE

Kentucky-American Water Company holds a unique position as a major subsidiary of American Water Works Company, Inc., a growth utility serving as the water resource manager of choice for approximately 10 million people in 23 states. American Water Works Company, Inc. is the largest and most geographically diverse investor-owned water utility enterprise in the United States. Kentucky-American Water Company is the largest private water utility in Kentucky, and the second largest water supplier in the Commonwealth of Kentucky – serving approximately 290,000 people in the Lexington-Fayette Urban County area and parts of Scott, Bourbon, Jessamine, Woodford, Clark, and Harrison counties.

As a participant in the prestigious National Partnership For Safe Water, Kentucky-American Water Company continues to deliver some of the highest quality water to the customers it serves. Since the company's initial involvement in the Partnership For Safe Water Program in 1996, Kentucky-American has remained in the forefront of water quality testing and research. Since the launch of this national initiative to help achieve operational excellence in water treatment, Kentucky-American has taken an active role to ensure high performance in water service for its customers.

Kentucky-American Water Company has the flexibility of two treatment plants with a rated capacity of 65-70 million gallons a day. The Richmond Road Station has a rated treatment capacity of 25 million gallons a day, and the Kentucky River Station can deliver up to 40 million gallons a day (45 MGD during the months of June-September). Kentucky-American relies on Jacobson Reservoir, which holds approximately 600 million gallons of water, for a portion of its water supply. Historically, Jacobson Reservoir has supplied up to 30% of the annual supply demand. The company's original reservoir, Lake Ellerslie, serves as a standby supply and holds approximately 74 million gallons of water. Seventy percent of the water treated and distributed is supplied by the Kentucky River. The Kentucky River Station is located on the banks of the Kentucky River, 12 miles from the city of Lexington.

As of year-end 2000, Kentucky-American provided water service to and maintained over 6,074 fire hydrants, and over 1,480 miles of main. Maintaining its standard of excellence, Kentucky-American repeatedly meets and exceeds all water quality regulations on state and federal levels, and performs over 11,000 tests per month, or 132,000 tests per year.



KENTUCKY-AMERICAN WATER COMPANY

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

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

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- Vice President N. O. Rowe
- Vice President & Treasurer C. D. Bush
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- Secretary H. A. Miller, Jr.



TO OUR STAKEHOLDERS



The message on the cover of this year's community report says it all – our water service is a constant in a tumultuous sea of change. As a water utility, we understand the legitimate expectation of our customers to trust that the water flowing from their taps is of high quality and readily available to fulfill the day-to-day needs of our community. For over 116 years this has been true. It is our goal to continue seamless water service to our customers for years to come, and provide an array of services that will fulfill our mission to provide total resource management of all water related needs to our ever-growing customer base.

As our community continues to grow, we remain steadfast in our commitment to meet the needs of those living in our service area, providing not only water for the numerous household tasks conducted on a daily basis, but also enriching the lives of all in our community. We are proud of our role as benefactor to the community, and continue to meet the increasing needs with in-kind contributions, by lending professional expertise to organizations through volunteerism, and providing financial assistance in support of vital projects to enhance the quality of life.

Kentucky-American Water Company is a dynamic participant in the central Kentucky community, repeatedly demonstrating the strength and resilience of the company – weathering the storms of change with unwavering dedication to our customers.

The future of our utility relies on our strength to change. The year 2000 signaled a continued departure from the traditional norm in the way we conduct our core

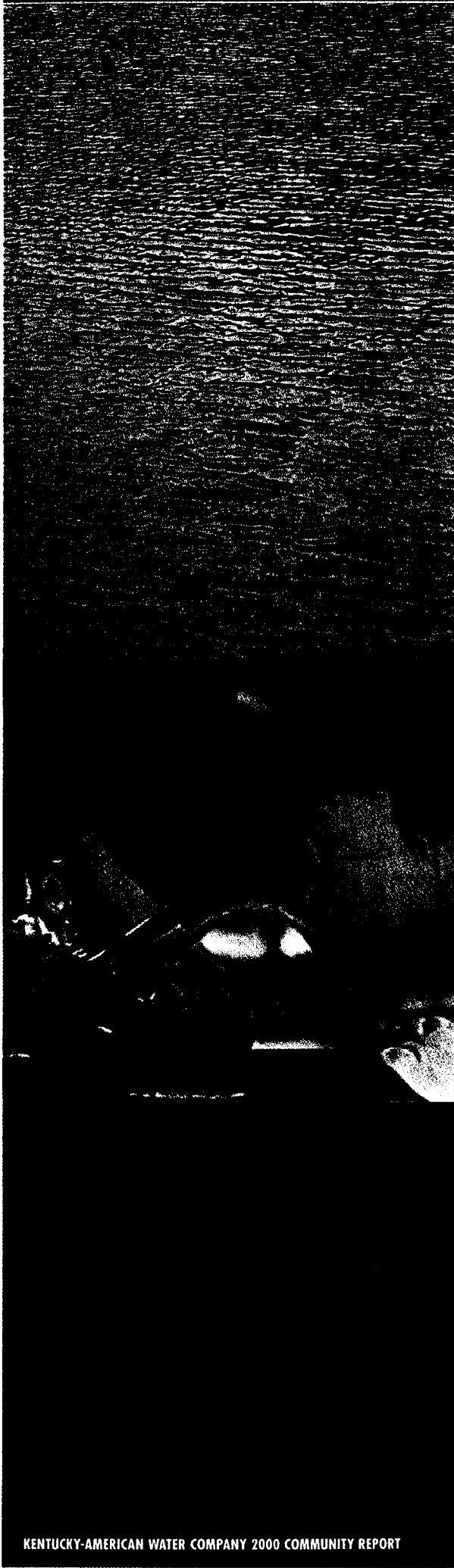


business. Internally, the entire American Water System has concentrated on driving change to better serve the needs of our customers in the ever-changing future. American's objective to be the water resource provider of choice for our nation is being accomplished by drivers from within. The change drivers include implementation of cultural audits to assess the beliefs of our associates, and encourage non-traditional methods of thinking. Increasing efficiency continues to be a driver and has resulted in the initiation of team projects to explore the benefits of shared services within administrative areas. Customer service and accounting are the departments currently under review with plans to implement a universal customer call center to better meet the needs of our growing customer base. Financial services is progressing toward a streamlined operation, with accounting functions performed from a central location in the near future. A prime example of consolidation and centralization in 2000 was the formation of a new wholly-owned subsidiary, American Water Capital Corporation, a special purpose corporation that serves as the primary funding vehicle for American Water Works Company and its utility subsidiaries. This move replaces bilateral lines of credit and consolidates the financing function, creating cash management efficiencies and a lower cost of capital for the utility.

Thinking out of the box has become the standard rather than the exception for American and its subsidiaries. To remain viable in the new economy, our company has taken the core foundation of water delivery, and forged into new territory to remain competitive in an increasingly volatile business environment. Offering new services will be the key to staying in step with the global economy, an area that American is embarking upon with American Water Resources, and American Water Services, Inc. Solutions through community partnerships and achieving cost savings through increasing efficiencies are the wave of the future, and Kentucky-American Water Company joins American Water Services in partnering with municipal systems to meet their needs. Residential customers will experience changes as well, as American Water Resources offers new options for the consumer such as a water line protection program designed to protect customers from unanticipated expenses resulting from leaks in the pipes that carry water from the company's line into the customer's home. This program is currently being offered in a limited service area, with plans to expand to other markets in the near future.

During 2000, a total of 2,741 customers were added to the system. Water main and fire hydrant installation this past year increased by 34 miles of mains and 135 hydrants.

In the area of acquisitions, shareholder value increased as a result of board approval to move



forward with the acquisitions of Tri-Village Water District, Elk Lake Water Company, and South Shores Water Works, Inc. Pending Public Service Commission approval, the addition of these water systems within Kentucky will add 4,335 customers to our expanded service area. As we strive to become the water resource manager of choice for the Commonwealth of Kentucky, we continue to generate interest in communities by offering flexibility of service options, such as contract operations management, wastewater services, billing services, and more.

Resolving the water supply deficit that exists in our community continues to be a challenge. Kentucky-American is committed to working with the community, and remains responsive to community opinions regarding the best solution to our water problems. The water supply issue will greatly impact all members of our community — whatever the ultimate solution. We are encouraged that attention is being directed to the extreme water concerns in our community, and will continue to proactively work to seek a permanent solution to the water supply issue. During the year 2000, Kentucky-American engaged in dialog with the Lexington Fayette Urban County Council and other entities in the Kentucky River Basin in an effort to move forward with regional solutions to the water supply issues. We are receptive to our elected officials' decision to seek a permanent solution through traditional means on the Kentucky River.

In April 2000, Kentucky-American filed a rate case with the Public Service Commission. In November, the Commission authorized an annual increase of \$2,517,651 for Kentucky-American, effective for service on and after that date. This was followed by an additional order received on December 12, 2000, reducing the rate increase granted in November by \$346,971. As a result of the December, 2000 order, Kentucky-American's rate increase was reduced to \$2,170,680, effective November 27, 2000. In January 2001, Kentucky-American petitioned for a rehearing for reconsideration of key issues originally filed in the rate case. A decision is expected in May 2001.

The year 2000 was a banner year for Kentucky-American in the area of customer service. The results of the system-wide surveys conducted by the Working Data Group, a Pennsylvania based research firm, positively demonstrated the company's track record of service to the community. Our success in this area was evident by the company's ranking among the top ten of all American operating centers in the area of customer satisfaction. The challenge in 2001 will be to achieve greater levels of excellence to satisfy the customer. The targets have been set, and all associates of Kentucky-American are poised to strive toward these goals.

Today's new economy has altered not only how we conduct our core business, but also how we manage our lives. The associates of Kentucky-American are active participants in company-wide efforts that focus on programs to enhance productivity and meet new challenges in the workplace. A highlight in 2000 was the launch of the Wellness Program; a progressive project to encourage evaluation of lifestyles, identify health risks, and provide the tools needed to make improvements.

The sea of change surrounding us has also created an opportunity to explore new ways to manage our companies. The American System is embarking on an aggressive program to introduce initiatives to showcase our cultural diversity. The global marketplace we operate in today has provided greater opportunity for all, and fierce competition to retain the best associates. This fact has led American to develop a diversity council to assist in efforts to retain talented professionals.

With all the changes taking place in our environment, in our workplace, and in our personal lives, it is reassuring that providing high quality water at a good value remains a constant in today's world. Our customers can rest assured that Kentucky-American will continue to deliver a premium product at a reasonable cost to our community for years to come.



STAKEHOLDER PARTNERSHIPS

WATER FOR LIFE

Perhaps the highlight of community reinvestment in the year 2000 was the promotion of the Water for Life program, a partnership to provide financial assistance to low income members of the community with payment of their water bills. The Water for Life water bill assistance fund is coordinated by Kentucky-American through the Community Action Council and further established the company's role as a leader in the community. The program officially kicked-off in September with a news conference to encourage customers to contribute one dollar to the fund through a water bill check mark on a designated section of the water bill. The company matched the customer funds dollar-for-dollar, and contributed to the administration of the program. To date, Kentucky-American has contributed \$7,300 to Water for Life. A total of \$6,906 has been distributed to 69 customers in need.



CORPORATE GIVING

Social responsibility has long been a hallmark of Kentucky-American Water Company's corporate giving policy. Founded on promotion and enhancement of science education, Kentucky-American strives to support areas that enhance youth education, yet contributes heavily to agencies and organizations that promote the arts as well as science. In 2000, the company provided contributions to 157 groups in the community, with a total funding of \$206,053.

- 1 Kentucky-American contributed to the local YMCA's capital campaign by sponsoring the lap pool at the Beaumont Centre YMCA.
- 2 One example of Kentucky-American's support for the arts was the company's sponsorship of "Not So Plain Joe" in the Lexington Arts and Cultural Council's Horse Mania project in 2000.

Ongoing contributions to the community include:

Animal Advocacy:

Lexington Humane Society

Arts:

Clark County Independence Day Festival
Ft. Harrod Drama Production
Lexington Arts and Cultural Council
Living Arts and Science Center
Horse Mania

Athletics:

Bluegrass State Games
Fifth-Third Bank Tennis Championship
Kentucky Thoroughblades
Wildcat Aquatics
Bryan Station High School
Paul Laurence Dunbar High School
Fast Pitch Reflex Softball Team
Henry Clay High School
Kentucky Kickers Soccer Club
Lafayette High School
Shillito Youth Football
Tates Creek High School

Community Development:

Bluegrass Community Foundation
Bourbon County Chamber of Commerce
Downtown Lexington Corporation
Greater Lexington Chamber of Commerce
Harrison County Chamber of Commerce
Kentucky Industrial Development Council
Lexington Strides Ahead
Paris City Club

Education:

Berea College
Bluegrass Technology Center
Economics America
Fraternal Order of Firefighters Fire Prevention Week
Greater Lexington Chamber of Commerce
Literacy Program
Henry Clay High School
Innovative Productivity, Inc.
Johnson Elementary School
Jr. Achievement Groundhog Shadow Day
Kentucky Science Olympiad
Kentucky State University
KET - The Kentucky Network
Lexington Children's Museum
Lexington Community College
MathCounts
Midway College
Picadome Elementary School
Sayre School
Southern Middle School
Transylvania University
University of Kentucky
YMCA Black Achievers

Environmental Preservation/Protection:

Fall Haul
Friends of McConnell Springs
Friends of the Arboretum
Kentucky Works Earth Day
Land and Nature Trust of the Bluegrass
N. Elizabeth Street Neighborhood Association
Tree Replacement Program
National Audubon Society -
Clyde E. Buckley Wildlife Sanctuary
Nature Conservancy
Reforest the Bluegrass

General Needs Assistance:

American Red Cross
Black Church Coalition
Bluegrass Search and Rescue
Center for Women, Children and Families
Community Action Council
Donate a Phone
Goodwill Industries of Kentucky
Go Women, Inc.
United Way of the Bluegrass

Health and Health Research:

Alzheimer's Association
American Cancer Society
American Heart Association
American Lung Association
Arthritis Foundation
Cardinal Hill Foundation
Center on Aging Foundation
Central Kentucky Blood Center
Cystic Fibrosis Foundation
Hospice of the Bluegrass
March of Dimes
Mental Health Association
Muscular Dystrophy Association
National Multiple Sclerosis Society
Susan G. Komen Race for the Cure
UK Children's Hospital
UK Student Dental Association

Historic Preservation:

Ashland - the Henry Clay Estate
Founders Day at McConnell Springs
Historic African Cemetery No. 2
Kentucky Historical Society
Roots and Heritage Festival
Shakertown

Housing Assistance:

Lexington Habitat for Humanity
Resources Education and Assistance for
Community Housing
Realtor Community Housing Foundation

Hunger Relief:

Big Brothers/Big Sisters of the Bluegrass
Thanksgiving Basket Program
God's Pantry

Leadership Development:

African American Leadership Emerge
Georgetown College Peer Exchange Network
Leadership Scott County
Women Mean Business Conference

Youth Programs:

Aviation Museum of Kentucky Summer Camp
Big Brothers/Big Sisters of the Bluegrass
Bluegrass Aspendale Teen Center
Boy Scouts of America
Children's Advocacy Center
Children's Fine Arts Foundation
Fayette County Junior Miss Scholarship
Fayette County Public Schools Literacy Program
Girl Scout Council
Glendover Global Studies School Playground Fund
Jessamine County Future Farmers of America
Junior Achievement
Lexington Kiwanis Foundation -
Harrison Elementary Playground Project
Lexington Montessori Playground Program
Miss Lexington Scholarship Fund
Partners for Youth
Partnerships in Education
Police Activities League
Project Graduation (Fayette and Scott counties)
Scott County 4-H
STEP Teen Employment Program
YMCA of Central Kentucky

Other:

Booneshoro Boat Club
Delta Sigma Theta Sorority
Fraternal Order of Firefighters
Home Builders Association of Lexington
League of Women Voters
Lexington Apartment Association
Lexington Junior League Horse Show
Lexington Senior Citizens Center
National Conference for Community and Justice
Martin Luther King Celebration
USO

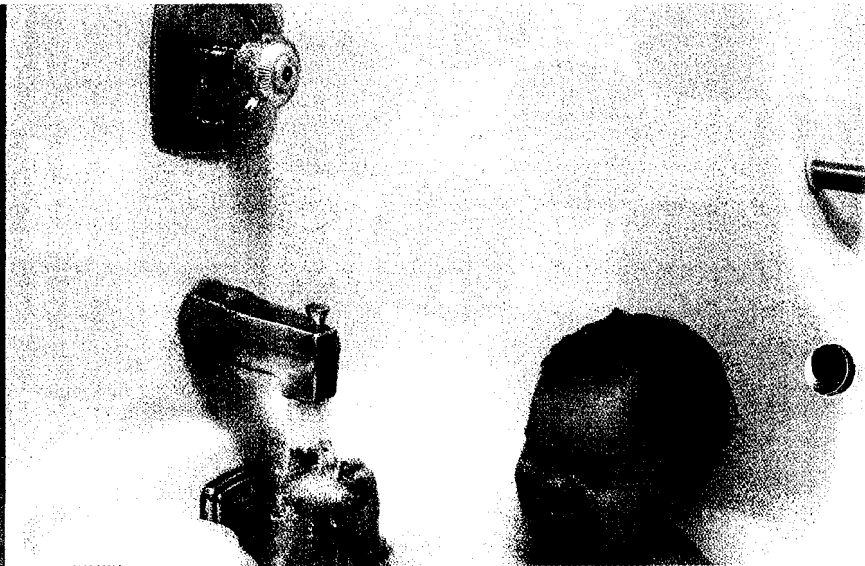


AREAS OF DISTINCTION

With changes abounding in the water industry, it is reassuring to report that one area of constancy is water quality. Truly the main focus of our core business, water quality remains an area of excellence for Kentucky-American Water Company. In the year 2000, over 11,000 tests per month, or 132,000 tests per year were conducted. These tests are in addition to the continuous monitoring that takes place using online instrumentation such as particle counters, turbidimeters, pH, chlorine, fluoride, and phosphate analyzers.

As a recipient of the prestigious Director's Award and a member in good standing of the National Partnership for Safe Water, Kentucky-American continued to demonstrate its commitment to performance excellence by providing filtered water to customers at 0.1 nephelometric turbidity unit (ntu) or better 99.95% of the time. This is much better than the current regulation requirement of .5 ntu.

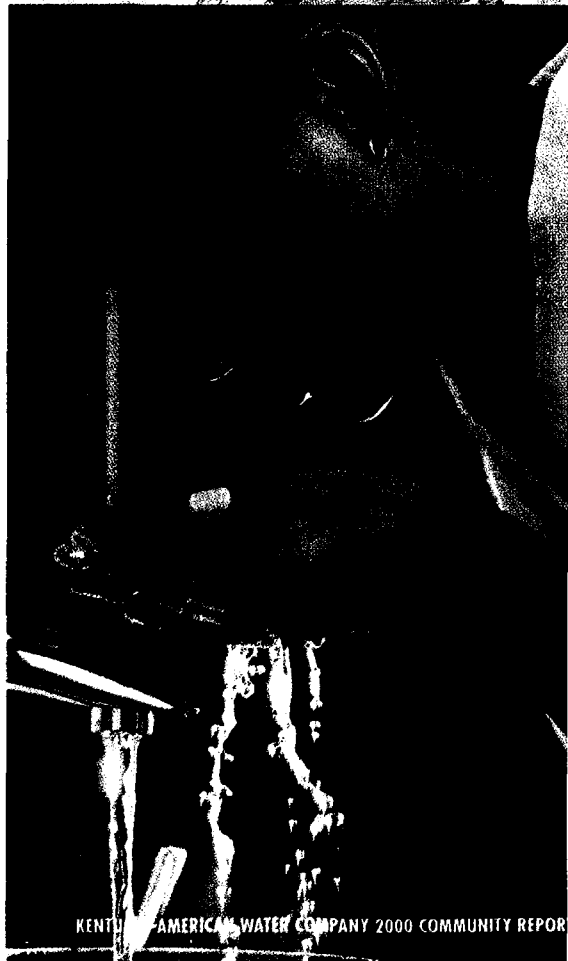
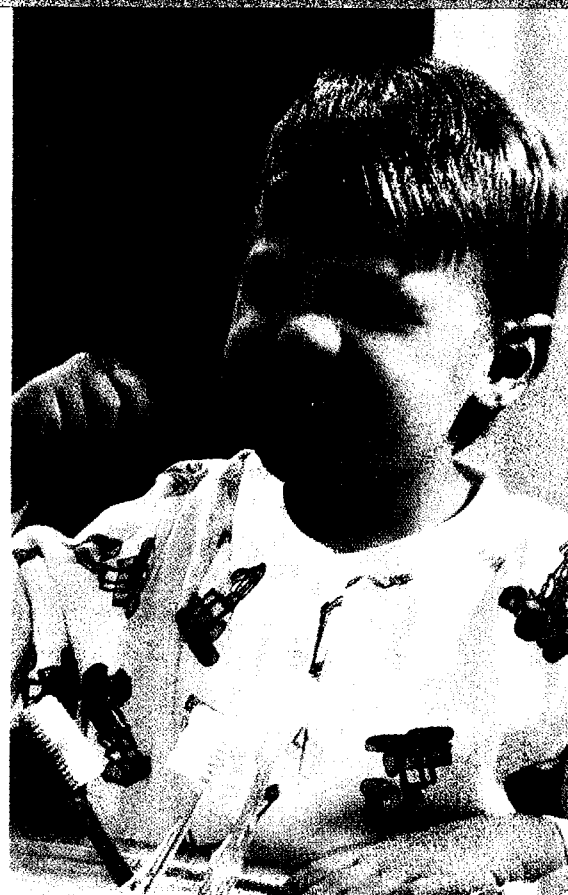
Increased regulation necessitates constant vigilance in the area of water quality. Water quality professionals stay well ahead of the requirements to ensure that Kentucky-American, as well as the entire American Water System, promotes excellence in water quality by continually meeting both state and federal standards, even as they become more stringent. In 2000, Kentucky-American added continuous monitoring particle counters on all filters at the Richmond Road and Kentucky River treatment plants. The benefits of the computerized particle counting system are many, including improved optimization of clarification and filtration. The monitored finished water provided to our customers was maintained throughout the year at standards superior to all safe drinking water requirements. Water distributed throughout the distribution system was maintained at a similar high level. Chlorine disinfectant residuals were maintained, and coliform bacteria were absent in all



compliance samples. Corrosion control was maintained as shown by excellent lead and copper and related water quality parameter monitoring. Kentucky-American's treatment processes and distributed waters met current and pending disinfection byproduct and total organic carbon removal requirements for the year 2000. Kentucky-American maintained state certifications of bacteriological and chemical labs, and added lab testing and treatment optimization capabilities under pending new regulations such as a new total organic carbon analyzer and fine-tuned sampling program.

As one of the largest water suppliers in the state, Kentucky-American often lends a hand to its neighboring water utilities. In 2000, Kentucky-American partnered with other water purveyors in the state to protect and improve water quality. One dramatic example is the coordinated response to a 100,000 gallon oil spill following a coal company's pipeline failure in January and February, which had the potential to threaten the central Kentucky water supply. Another example is Kentucky-American working with the state through the year 2000 to assist two small central Kentucky water utilities in complying with disinfection byproduct limits.

Community involvement through sharing professional expertise is not new to the water quality staff. The director of water quality serves as Vice Chair of the Program Effectiveness Assessment Committee for the National Partnership for Safe Water, and is an active member of the American Water Works Association Water Quality Division Board of Directors, as well as serving as an American Water Works Association Research Foundation Project Advisory Committee member. Other members of the water quality team are involved as well, serving as Chair-Elect of the Ohio River Sanitation Commission Water Users Committee,



and participating in the Kentucky-Tennessee Section of the American Water Works Association. The water quality staff joins in community relations projects and actively participate as plant tour guides, science fair judges, and conduct presentations at local events.

As new regulations come into effect, and the water industry is held to increasingly stringent guidelines, Kentucky-American remains in the forefront, working with local and state regulators and officials to assess and develop new regulatory and related water quality programs. Of special significance is Kentucky-American's participation in national Cryptosporidium research, which has been vital to the water industry. Kentucky-American along with the other subsidiaries of the American Water Works Company, Inc. provide proactive educational information to the severely immunocompromised customer and detailed information through mailings and meetings on issues such as Cryptosporidium.



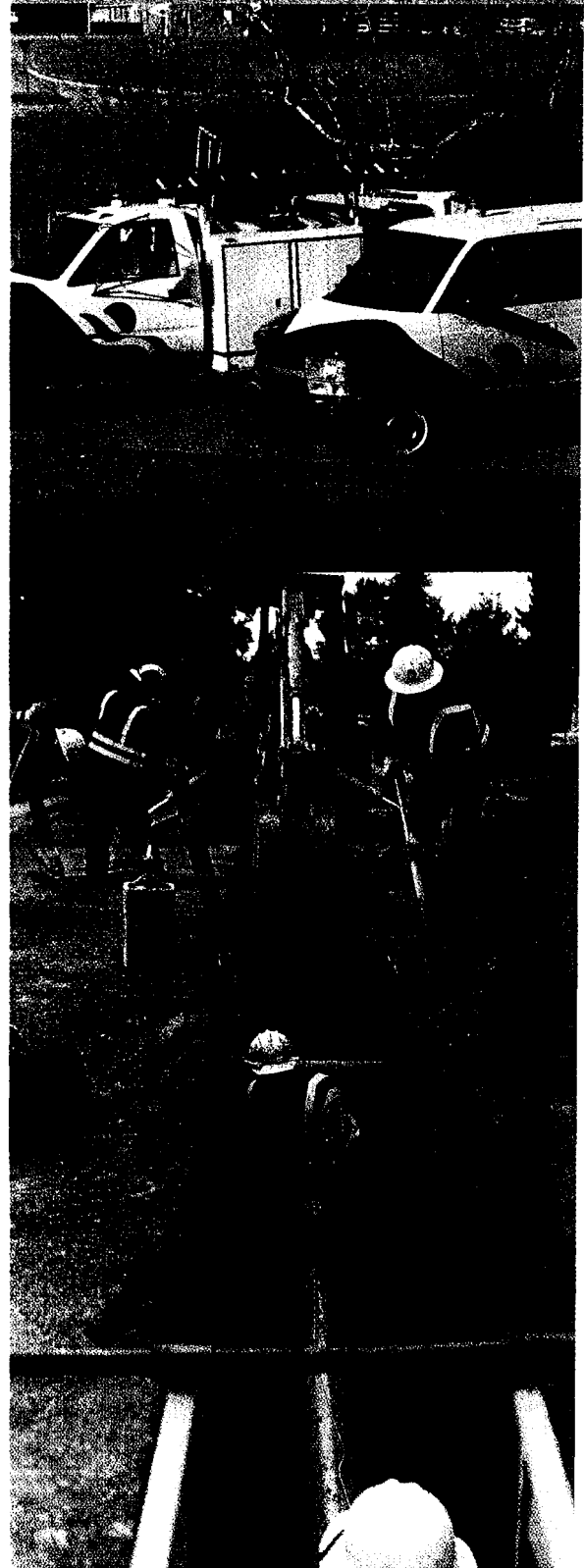
WORKPLACE SAFETY

The leadership of Kentucky-American is committed to the issues of workplace safety. In the water industry, safety on job sites dominates the day-to-day operations of the organization, and at Kentucky-American, the emphasis on safety continues to gain significance.

Safety is a philosophy of the company, embraced at all levels of the organization. More than 70 safety meetings and training sessions were conducted in 2000. The company's Accident Prevention Council conducted monthly inspections of the facilities and made recommendations to improve the safety conditions where necessary.

Approximately 85% of the workforce was eligible to receive a safety recognition award. The award is given to associates who complete the year without a safety code violation or a lost time or chargeable vehicular accident. The number of lost time accidents remained the same as the previous year, however the percentage of lost time days and restricted duty days reduced by 95% and 58% respectively. Although emphasis continues to be placed on defensive driving training, chargeable vehicular accidents increased by 3% in 2000.

Recognizing the global society we operate in today, the company became involved in the Federal Bureau of Investigation's InfraGard Program. This program's objective is to increase security of the United States national infrastructures through ongoing exchanges of information. The program is designed to keep the leadership of organizations abreast of issues that could potentially affect the security of critical infrastructures.





HUMAN RESOURCES







Driving change internally was led by a team that included strong leadership from Human Resources. Expertise in the area of human resource management was critical to the strategic implementation of the programs underway today. Some highlights in 2000 include: conflict resolution classes for all associates, self-directed team training for customer service and financial services, 25 EARN (Educating Associates to Reach New Heights) classes, and four LEAD programs (Leadership Evaluation and Development Program) designed to enhance leadership and professionalism. Kentucky-American's Director of Human Resources has lent expertise in the implementation of the new call center, and provided input in areas of management poised for major change.


- 1 Partnering with area schools through the "Partnership in Education" program has been an enriching experience for Kentucky-American associates.
- 2 Kentucky-American associates celebrated workplace safety achievements at a safety picnic held at the company in the fall.


KENTUCKY-AMERICAN WATER COMPANY SERVICE AREA

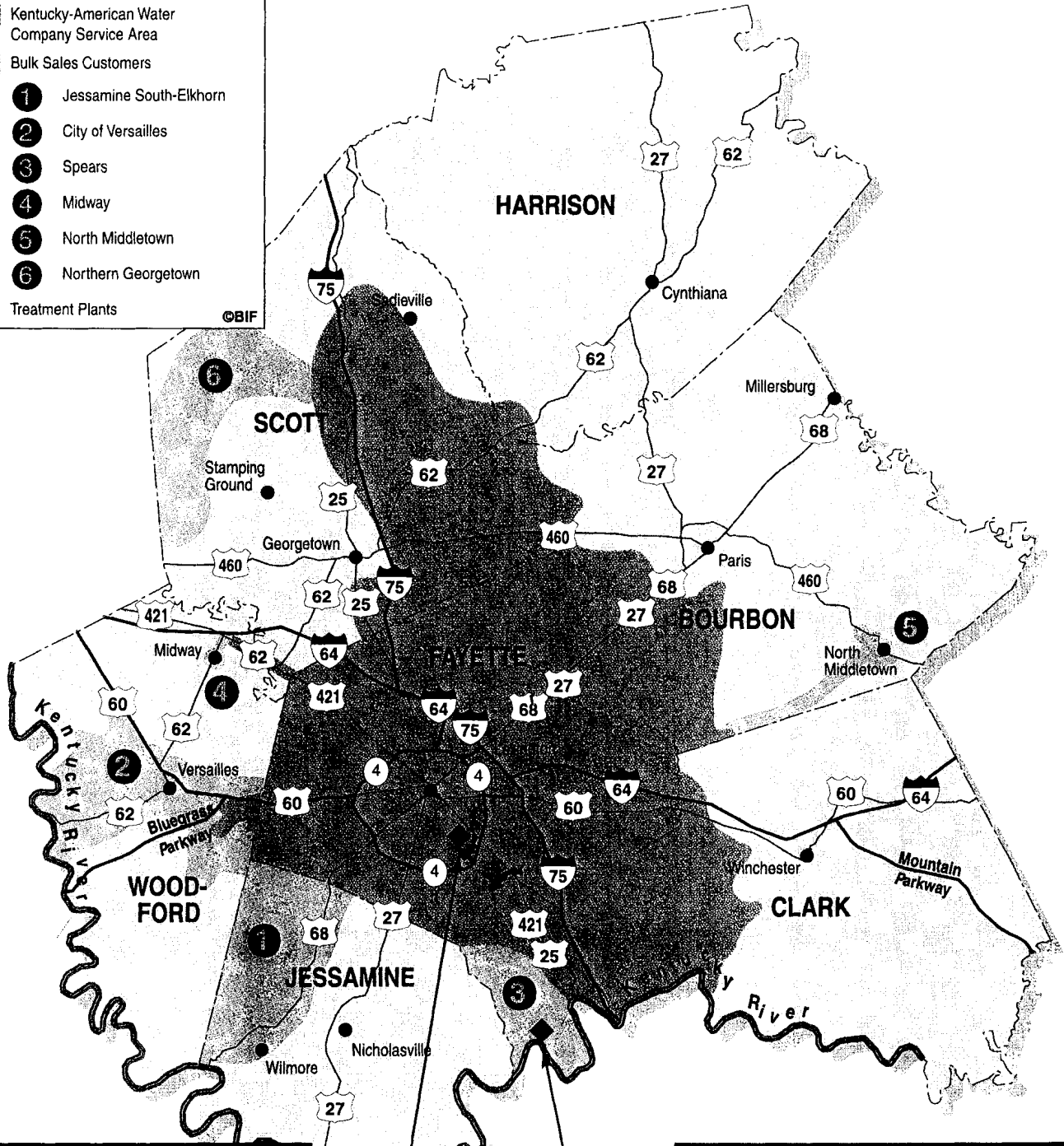
 Kentucky-American Water Company Service Area

 Bulk Sales Customers

-  Jessamine South-Elkhorn
-  City of Versailles
-  Spears
-  Midway
-  North Middletown
-  Northern Georgetown

 Treatment Plants





Dickwood Road Treatment Plant



Kentucky River Treatment Plant



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