

**KENTUCKY-AMERICAN WATER COMPANY**  
**CASE NO. 2007-00143**  
**PUBLIC SERVICE COMMISSION'S FIRST SET OF INFORMATION REQUESTS**  
**ITEMS 1 – 33**

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Witness Responsible:

Michael A. Miller/Linda Bridwell

31. a. Provide a copy of all other service agreements and contracts that Kentucky-American has with any affiliate company.
- b. Describe in detail the pricing policies of Kentucky-American and its affiliates with regard to affiliate company transactions.

Response:

- a. Please see the attached documents.
- b. **American Water Works Service Company**- All billings to KAWC from AWWSC are provided in accordance with the 1989 Service Company Contract. Please see Articles II and III of the Service Company contract provided as an attachment to part (a) above. All services obtained through AWWSC are at cost.

**American Water Capital Corporation** - Costs of AWCC are billed as outlined in the Services Agreement attached to part (a) above between KAWC and AWCC approved by the Commission. As outlined in the Service Agreement, KAWC will pay AWCC a portion of the costs and appropriate overhead incurred by AWCC in providing services as follows. The cost incurred by AWCC in connection with its bank credit lines and short-term public borrowing will be divided amount the Co-Participants in proportion to the maximum principal amount that each Co-Participant requests be made available to it during the course of a year. The costs incurred by AWCC in connection with each long-term borrowing by AWCC will be divided among each Co-Participant in proportion to the principal amount of that borrowing that is loaned to that Co-Participant. AWCC's overhead will be allocated among the Co-Participants in the same proportion as each Co-Participant's long-term and maximum, requested short-term borrowings and investments in a calendar year bear to all the long and maximum short-term borrowings and investments by all Co-Participants during the same year.

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**American Water Resources** – KAWC obtains activated granular carbon from American Water Resources per the GAC Lease Agreement provided in response to part (a) above. The payment and pricing terms of the agreement are contained in Section (B) of the Agreement.

For electronic version, see [KAW\\_R\\_PSCDR1#31\\_052107.pdf](#)

ANNUAL REPORT RELATING TO A  
NONREGULATED ACTIVITY OF AN  
AFFECTED UTILITY OR ITS AFFILIATE

Pursuant to 807 KAR 5:080

YEAR ENDED: DECEMBER 31, 2006

KENTUCKY-AMERICAN WATER COMPANY  
(the "Company")

Section 2. (a) Not applicable.

(b) Not applicable.

(c) Nonregulated affiliates of the Company include those listed in the Public Service Commission Case No. 2002-00018, as amended and reported to the PSC.

Nonregulated affiliates with service agreements with the Company are:

1. American Water Works Service Company dated January 1, 1989, for a variety of services including data processing, finance and accounting, regulatory assistance, human resources, risk management and loss control, water quality testing, communications, auditing, financial management and customer service.

2. American Water Capital Corp. dated June 15, 2000, for a cash management system and both long and short term borrowing pursuant to the PSC approval in Case No. 2000-189.

3. American Water Resources, Inc. (formerly AmericanAnglian Environmental Technologies, L. P.), dba American Carbon Services dated January 21, 2002, for the purpose of services and products for water treatment purposes.

There were no new or amended service agreements in the year ended December 31, 2006.

AGREEMENT

Agreement dated January 1, 1989, between AMERICAN WATER WORKS SERVICE COMPANY, INC., a Delaware corporation (hereinafter "Service Company"), and KENTUCKY-AMERICAN WATER COMPANY, a Kentucky corporation (hereinafter "Water Company").

The background of this Agreement is that:

1. Both Service Company and Water Company are subsidiaries of American Water Works Company, Inc., a Delaware corporation (hereinafter "American").
2. Water Company has been organized for and is presently engaged in the business of providing potable water as a public utility in the State of Kentucky.
3. Service Company maintains an organization whose officers and employees are familiar with all facets of the water utility business, including the development, business and property of Water Company, and are experienced in the efficient management, financing, accounting and operation of water utility properties and the extension and improvement thereof. The officers and employees of Service Company are qualified to aid, assist and advise Water Company in its business operations through the services to be performed under this Agreement.
4. Service Company has provided administrative and operating services to Water Company for many years, the past 17 years pursuant to an agreement dated January 1,

1971. Because Water Company is of the opinion that it cannot obtain the same quality and diversification of services on a comparable economic basis elsewhere, it proposes to enter into a new agreement with Service Company more specifically defining the types of services available to it.

5. Service Company has entered or proposes to enter into agreements similar to this agreement with other affiliated water companies (hereinafter collectively "Water Companies").

6. The services to be rendered under this agreement are to be rendered by Service Company to Water Companies at their cost to Service Company, as hereinafter provided.

NOW, THEREFORE, in consideration of the premises and mutual agreements herein contained, the Water Company and Service Company agree that:

**ARTICLE 1. PERSONNEL AND SERVICES TO BE PROVIDED**

1.1 During the term of this agreement and upon the terms and conditions hereinafter set forth, Service Company shall provide corporate guidance for Water Company. In addition to the guidance provided by the officers and employees of Service Company through the coordination of functional activities for all subsidiaries of American, the officers and employees of Service Company shall furnish and Water Company shall purchase from Service Company, the following services: Accounting, Administration, Communication, Corporate Secretarial, Engineering, Financial, Human Resources,

Information Systems, Operation, Rates and Revenue, Risk Management and Water Quality, together with such other services as Water Company and Service Company may agree; provided, however, that Water Company may perform the service with its own personnel or engage another company or person to provide those services on its behalf. Service Company by mutual consent may engage another Company or person to provide such services on its behalf.

1.2 Service Company shall employ qualified officers and employees and those persons shall be available for election by Water Company to serve as officers of Water Company.

1.3 Without limitation, services to be provided by the Service Company shall be rendered as follows:

A. Accounting: Service Company shall assist in the preparation and implementation of accounting methods and procedures to determine that they conform fully to the requirements, rules and regulations of governmental authorities having jurisdiction and review Water Company's monthly financial reports, annual reports and other reports to stockholders and to any governmental authorities. It shall advise and assist in the establishment and maintenance of current record keeping techniques; review accounting procedures, methods and forms; and evaluate systems of internal control for receipt and disbursement of funds, materials and supplies, and other assets. Service Company shall maintain accounting records as required by Water Company. When appropriate, Service Company shall cooperate and consult with Water Company's independent certified public accountants.

Service Company shall assist in the preparation of operating and construction budgets and monitor the control over such budgets by comparing experienced costs to the projections.

Service Company shall prepare or assist in the preparation of federal, state and local tax returns for and to the extent required by Water Company.

**B. Administration:** Service Company shall make qualified employees available to perform or assist in the performance of Water Company's corporate activities. Those employees shall keep themselves informed on all aspects of Water Company's operations and shall regularly visit Water Company's facilities. They shall make recommendations to Water Company for operating expenditures and for additions to and improvements of property, plant and equipment. They shall keep abreast of economic, regulatory, governmental and operational developments and conditions that may affect Water Company; and advise Water Company of any such developments and conditions to the extent that they may be important to Water Company. Service Company shall provide an internal audit staff for periodic audits of accounts, records, policies and procedures of Water Company and submit reports thereon.

**C. Communications:** Service Company shall recommend procedures to promote satisfactory relations with employees, customers, communities and the general public and assist in the preparation of communication materials, (including press releases, brochures, audio visual presentations and speeches) plant tours, public exhibits and displays and other related services to inform the public.

D. Corporate Secretarial: Service Company shall maintain, in such places and manner as may be required by applicable law, documents of Water Company, such as minute books, charters, by-laws, contracts, deeds and other corporate records, and shall administer an orderly program of records retention. It shall maintain, or arrange for the maintenance of, records of stockholders of Water Company, prepare or arrange for the preparation of stock certificates, perform duties relating to the transfer of stock and perform other corporate secretarial functions as required including preparation of notices of stockholder and director meetings and the minutes thereof.

Service Company shall review and may assist in the preparation of documents and reports required by Water Company such as deeds, easements, contracts, charters, franchises, trust indentures and regulatory reports and filings.

E. Engineering: Service Company shall advise, and provide engineering services to assist Water Company in planning for, operating, maintaining and constructing its facilities.

It shall conduct distribution system surveys and hydraulic analyses and prepare or review maps, charts, operating statistics, reports and other pertinent data.

It shall assist Water Company in the proper maintenance and protection of Water Company properties by periodic inspection of its structures, tanks, reservoirs, dams, wells and electrical and mechanical equipment.

The engineering services provided by Service Company shall also include the conduct of field investigations as necessary to



obtain engineering information and, when required, the preparation of studies, reports, designs, drawings, cost estimates, specifications, and contracts for the construction of additions to or improvements of Water Company's source of supply, treatment plant, pumping stations, distribution system, and such other facilities as Water Company may request. Service Company shall provide a Materials Management Program to arrange for the purchase of equipment, materials, and supplies in volume on a basis advantageous to Water Company and assist in the evaluation of new and existing products and application procedures.

F. Financial: Service Company shall assist in the development and implementation of financing programs for Water Company, including the furnishing of advice from time to time on securities market conditions and the form and timing of financing; advise concerning arrangements for the sale of its securities; and assist in the preparation of necessary papers, documents, registration statements, prospectuses, petitions, applications and declarations. It shall prepare reports to be filed with, and reply to inquiries made by, security holders and bond and mortgage trustees.

Service Company shall assist Water Company in cash management including arrangements for bank credit lines, establishment of collection policies, and development of temporary investment programs.

Service Company shall provide assistance to Water Company in the preparation of all financial reports.

G. Human Resources: Service Company shall assist in obtaining qualified personnel for Water Company; in establishing appropriate rates of pay for those employees; and in negotiating with bargaining units representing Water Company employees. It shall carry out training programs for the development of personnel and advise and assist Water Company regarding personnel. It shall also advise and assist Water Company in regard to group employee insurance, pension and benefit plans and in the drafting or revising of those plans when required. It will keep Water Company apprised of all employment laws and develop procedures and controls to assure compliance.

H. Information Systems: Service Company shall make available to Water Company electronic data processing services. Those services shall include customer billing and accounting, preparation of financial statements and other reports including those required by Federal and State agencies.

I. Operation: Service Company shall develop and assist in the implementation of operating procedures to promote the efficient and economic operation of Water Company. Periodic operational reviews will be performed by Service Company personnel and any deviations from adopted procedures will be reported to Water Company.

J. Rates and Revenue: Service Company personnel shall make recommendations for changes in rates, rules and regulations and shall assist Water Company in the conduct of proceedings before, and in its compliance with the rulings of, regulatory bodies having jurisdiction over its operation. These personnel

shall keep abreast of economic and regulatory developments and conditions that may affect Water Company; and advise Water Company of any such developments and conditions to the extent that they may be important to Water Company. Rates and Revenue personnel shall assist in the preparation of rate filings or applications and the supporting documents and exhibits requested or required by the Water Company and their respective regulatory commissions. Service Company shall also provide qualified personnel to testify on Water Company's behalf as required during any regulatory proceedings.

K. Risk Management: Service Company shall provide a Risk Management Program to review the exposures to accidental loss of the Water Company, recommend efficient methods of protection either through the purchase of insurance, self-insurance or other risk management techniques and arrange for the purchase of insurance coverage. It shall also supervise investigation procedures; review claims; and negotiate and assist in, and evaluate proposals for, settlement at the request of Water Company. It shall assist in the establishment of safety and security programs to avoid or minimize risk and loss.

L. Water Quality: Service Company shall assist Water Company to comply with standards of governmental agencies and establish and attain water quality objectives of the Water Company. It shall assist in providing design criteria for processes, coordinating with public agencies, developing approaches and solutions to water quality problems, and providing

technical assistance and general direction for Water Company personnel.

It shall also provide laboratory services for programmed analyses as required by drinking water regulations, and special analyses as required by Water Company.

#### ARTICLE II. PAYMENT FOR SERVICES

2.1 In consideration for the services to be rendered by Service Company as hereinabove provided, Water Company agrees to pay to Service Company the cost thereof determined as provided in this Article II and in Article III.

2.2 All costs of service rendered by Service Company personnel for Water Company or in common with other Water Companies shall be charged to Water Company based on actual time spent by those personnel as reflected in their daily time sheets or other mutually acceptable means of determination.

2.3 All costs of Service Company incurred in connection with services rendered by Service Company which can be identified and related exclusively to Water Company, shall be charged directly to Water Company.

2.4 All costs incurred in rendering services to Water Company in common with similar services to other Water Companies which cannot be identified and related exclusively to services rendered to a particular Water Company, shall be allocated among all Water Companies so served, or, in the case of costs incurred with respect to services rendered to a particular group of Water

Companies, among the members of such group, based on the number of customers served at the immediately preceding calendar year end.

2.5 Cost for support personnel (secretaries, clerical personnel, clerks, messengers, telephone operators, mail clerks, and other incidental support personnel of the Service Company) as well as the cost of lease payments, depreciation, utilities and other costs associated with leasing office space and equipment by Service Company shall be allocated among the Water Companies on the basis of the proportion of the aggregate cost allocated under Sections 2.3 and 2.4.

#### ARTICLE III. ALLOWANCE FOR OVERHEAD

3.1 In determining the cost to be assessed by Service Company for the rendering of services to Water Company as herein provided, there shall be added to the salaries of all officers and employees for whose services charges are to be made, a percentage sufficient to cover the general overhead of Service Company, as defined below, properly allocable thereto. Such percentage shall be calculated each month and shall be the ratio of the total general overhead of the Service Company for the month to the total salaries of the employees for whose service charges are to be made to the Water Companies. No general overhead of Service Company shall be added to costs incurred for services of non-affiliated consultants employed by Service Company.

3.2 The term "general overhead" shall include:

- (a) pension and insurance premiums paid for the benefit of Service Company employees,

- (b) legal and other fees for services rendered to the Service Company,
- (c) taxes,
- (d) other general office supplies and other similar expenses, and
- (e) interest on working capital.

**ARTICLE IV. BILLING PROCEDURES AND BOOKS AND RECORDS**

4.1 As soon as practicable after the last day of each month, Service Company shall render a bill to Water Company for all amounts due from Water Company for services and expenses for such month plus an amount equal to the estimated cost of such services and expenses for the current month, all computed pursuant to Articles II and III. Such bill shall be in sufficient detail to show separately the charge for each class of service rendered. All amounts so billed shall reflect the credit for payments made on the estimated portion of the prior bill and shall be paid by Water Company within a reasonable time after receipt of the bill therefore.

4.2 Service Company agrees to keep its books and records available at all times for inspection by representatives of Water Company or by regulatory bodies having jurisdiction over Water Company.

4.3 Service Company shall at any time, upon request of Water Company, furnish any and all information required by Water Company with respect to the services rendered by Service Company

hereunder, the costs thereof, and the allocation of such costs among Water Companies.

**ARTICLE V. OTHER AGREEMENTS**

5.1 It is understood by Water Company that Service Company has entered or may enter into similar agreements with other Water Companies that are affiliated with American to which similar services are to be furnished. Service Company will not enter into agreements to perform similar services for other companies on terms more favorable than those provided herein.

5.2 It is understood by Water Company that Service Company has entered or may enter into an agreement or agreements with American and certain other companies not engaged in the water or sewer service business to which limited services are to be furnished; Water Company consents to such additional agreements, provided, however, that no part of the cost of furnishing such services will be charged to Water Company.

**ARTICLE VI. TERM OF AGREEMENT**

This agreement shall become effective as of the later of (a) the date first mentioned above or (b) the date the parties receive the last of any necessary approvals of governmental regulatory agencies having jurisdiction in the premises. Upon becoming effective, this agreement shall be the sole agreement between the parties concerning the subject matter hereof and shall supersede all prior agreements, written or oral, including the agreement dated January 1, 1971, which shall terminate on the date this

agreement becomes effective. This agreement shall continue in full force and effect until terminated by either of the parties hereto giving the other party hereto ninety day's notice in writing; provided, however, that this agreement shall terminate as of the date Water Company or Service Company ceases to be an affiliate of American.

IN WITNESS WHEREOF, Service Company and Water Company have caused this agreement to be signed in their respective corporate names by their respective Presidents or Vice Presidents, and impressed with their respective corporate seals attested by their respective Secretaries or Assistant Secretaries, all as of the day and year first above written.

ATTEST:



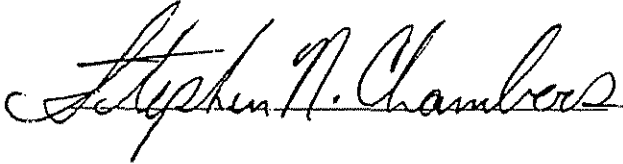
AMERICAN WATER WORKS SERVICE  
COMPANY, INC.

By



President

ATTEST:



KENTUCKY-AMERICAN WATER COMPANY

By



President



FINANCIAL SERVICES AGREEMENT

THIS AGREEMENT, dated as of June 15, 2000, by and between Kentucky-American Water Company (the "Company") and American Water Capital Corp. ("AWCC").

BACKGROUND

The Company currently performs its own financial services.

However, the Company has determined that it can obtain these services more efficiently through the consolidation of certain necessary management and staff functions with those performed for other entities that may enter into agreement with AWCC substantially similar to this one ("Co-Participants").

AWCC is dedicated to performing such consolidated functions.

Accordingly, the parties have determined to enter into this Agreement for the provision of financial services by AWCC to the Company and for the proper determination and allocation of the costs of providing such services.

Therefore, the parties agree as follows:

AGREEMENT

1. Services. AWCC will provide, either directly or through arrangements with third parties for the benefit of the Company, such financial services as the Company and AWCC may from time to time agree, including but not limited to those more fully described in Appendix I attached to this Agreement.

2. Costs. In consideration of the provision of the services contemplated by paragraph 1, the Company agrees to pay AWCC a portion of the costs and appropriate overhead incurred by AWCC in providing those services, as follows. The costs incurred by AWCC in connection with its bank credit lines and short-term public borrowings will be divided among the Co-Participants in proportion to the maximum principal amount that each Co-Participant requests be made available to it during the course of a year. The costs incurred by AWCC in connection with each long-term borrowing by AWCC will be divided among each Co-Participant in proportion to the principal amount of that borrowing that is loaned to that Co-Participant. AWCC's overhead will be allocated among the Co-Participants in the same proportion as each Co-Participant's long-term and maximum, requested short-term borrowings and investments in a calendar year bear to all of the long and maximum short-term borrowings and investments by all Co-Participants during the same year.

3. Statements. AWCC will prepare and deliver to the Company monthly statements of the services provided by AWCC and amounts payable to AWCC, giving effect to

all the provisions of this Agreement. The Company shall pay the net amount shown on its statement within thirty (30) days after the billing date.

4. Inspection. Upon reasonable notice, AWCC will make available to the Company for its inspection AWCC's books, records, bills, accounts and any other documents which describe or support the costs allocated to the Company under this Agreement.

5. Obligations Not Joint. AWCC and the Company expressly agree: (a) that the obligations of the Company and each Co-Participant to AWCC are several and not joint; (b) that the Company will not be responsible to any Co-Participant, to AWCC or to any assignee or creditor of AWCC for any payment in excess of payments due by the Company to AWCC under this Agreement or a Note in the form attached to this Agreement; and (c) that no Co-Participant will be responsible to the Company, to any other Co-Participant, to AWCC or to any assignee or creditor of AWCC for any payment in excess of payments due by that Co-Participant to AWCC under any agreement substantially similar to this Agreement or under any Note attached to that other agreement. AWCC covenants and agrees that it will require, as a condition to its entering into any such other agreement with a Co-Participant, that such other agreement contains the same provision as that contained in the immediately preceding sentence.

6. Notes. The Company's borrowings under this Agreement will be evidenced by one or more promissory notes in the form of Exhibit A or Exhibit B attached to this Agreement.

7. Non-Exclusivity. Nothing in this Agreement prohibits or restricts the Company from borrowing from third parties, or obtaining services described in this Agreement from third parties, whenever and on whatever terms it deems appropriate.

8. Effectiveness. This Agreement shall be effective as of June 15, 2000, provided that, if prior approval by the regulatory commission of any jurisdiction is required before this Agreement may become effective as to the Company, or before AWCC may provide a particular service hereunder to the Company, this Agreement shall not be effective as to the Company or as to that service, as the case may be, unless and until the required approval has been obtained. Unless and until this Agreement becomes effective as to the Company in whole or in part, the Company shall not be entitled to the benefits of, nor shall it have any rights or duties under, this Agreement. This Agreement may be amended or rescinded only by written instrument signed by the Company and AWCC.

9. Termination. The Company may terminate its participation in this Agreement by giving ten (10) days prior written notice of such termination to AWCC; and (b) AWCC may terminate this Agreement by giving ninety (90) days prior written notice of such termination to the Company. Termination of this Agreement will not affect: (a) the Company's obligations under any Promissory Notes; (b) any party's obligations with respect to any amounts owing under Sections 2 and 3 of this Agreement (including such amounts attributable to obligations of any terminating party under any Promissory Notes that remain outstanding after this Agreement is terminated as to that party); or (c) AWCC's obligations to repay any investments made by a Company pursuant to Appendix I.

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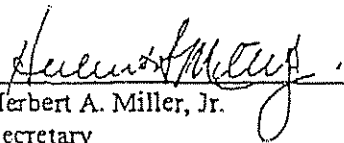
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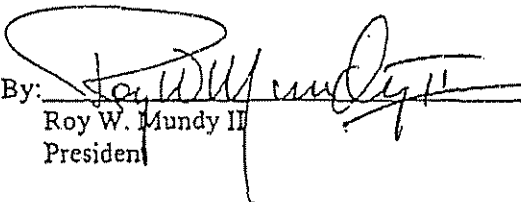
10. Copies. This Agreement may be executed by the parties in one or more copies and each executed copy shall be considered an original.

In witness of the foregoing, each of the Company and AWCC has caused its respective corporate seal to be affixed to this Agreement and has caused this Agreement to be signed on its behalf by its duly authorized officers.

ATTEST:

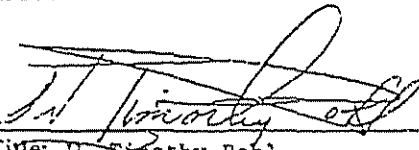
KENTUCKY-AMERICAN WATER COMPANY


By:   
Herbert A. Miller, Jr.  
Secretary

By:   
Roy W. Mundy II  
President

ATTEST:

AMERICAN WATER CAPITAL CORP.

By:   
Title: W. Timothy Pohl  
Vice President and Secretary

By:   
Name and Title: Joseph F. Hartnett, Jr.  
Vice President and Treasurer

APPENDIX I

DESCRIPTION OF FINANCIAL SERVICES

Set forth below is a list of the services which AWCC agrees to provide to the Company upon its request pursuant to the Agreement to which this Appendix is attached.

1. Short-Term Loans. AWCC will provide Short-Term Loans to the Company pursuant to the terms set forth in the promissory notes to be issued by the Company to AWCC, each substantially in the form attached to this Agreement as Exhibit A.

2. Long-Term Borrowings. AWCC will provide loans other than Short-Term Loans to the Company pursuant to the terms set forth in the promissory notes to be issued by the Company to AWCC, each substantially in the form attached hereto as Exhibit B.

3. Cash Management. Cash not required by the Company to pay its daily disbursements or to pay when due the principal of and interest on, the Company's borrowings from AWCC other than Short-Term Loans will be used by AWCC first to reduce the outstanding principal balance of the Company's Short-Term Loans owing to AWCC and any excess will be deemed to be invested with AWCC and will earn a daily rate of interest that is equal to the interest income earned by AWCC on those funds. Upon the request of that Company, AWCC shall execute one or more promissory notes in favor of the Company, in form and substance substantially similar to the Promissory Note attached as Exhibit A to the Agreement as evidence of such investment.

EXHIBIT A  
PROMISSORY NOTE  
FOR SHORT-TERM LOANS

\$ \_\_\_\_\_, 2000

FOR VALUE RECEIVED, [NAME OF COMPANY], a \_\_\_\_\_ corporation (herein "Borrower") hereby promises to pay ON DEMAND to the order of American Water Capital Corp., a Delaware corporation ("Lender"), in same day funds at its offices at Voorhees, New Jersey or such other place as Lender may from time to time designate, the principal sum of \_\_\_\_\_ dollars (\$ \_\_\_\_\_) (the "Maximum Principal Sum"), or such lesser amount as shall equal the aggregate unpaid principal amount of the loans made by Lender to Borrower (other than loans evidenced by a promissory note under which the principal amount is due and payable in one or more scheduled installments more than one year after the date of its issue), together with interest thereon from the date hereof until paid in full. Interest will be charged on the unpaid outstanding principal balance of this Note at a rate per annum equal to Lender's actual cost of funds to make such loan, such rate to change as Lender's actual cost of funds changes. Interest on borrowings shall be due and payable on the first business day of each month, commencing with the first business day of the month after the month in which this Note is executed. In the absence of manifest error, the records maintained by Lender of the amount and term, if any, of borrowings hereunder shall be deemed conclusive.

Borrower may borrow, repay and reborrow hereunder in amounts which do not, in the aggregate outstanding at any time, exceed the Maximum Principal Sum.

The occurrence of one or more of any of the following shall constitute an event of default hereunder:

(a) Borrower shall fail to make any payment of principal and/or interest due hereunder or under any other promissory note between Lender and Borrower within five business days after the same shall become due and payable, whether at maturity or by acceleration or otherwise;

(b) Borrower shall apply for or consent to the appointment of a receiver, trustee or liquidator of itself or any of its property, admit in writing its inability to pay its debts as they mature, make a general assignment for the benefit of creditors, be adjudicated a bankrupt or insolvent or file a voluntary petition in bankruptcy or a petition or an answer seeking reorganization or an arrangement with creditors or to take advantage of any bankruptcy, reorganization, insolvency, readjustment of debt, dissolution or liquidation of law or statute, or an answer admitting the material allegations of a petition filed against it in any proceeding under any such law, or if action shall be taken by Borrower for the purposes of effecting any of the foregoing; or

(c) Any order, judgment or decree shall be entered by any court of competent jurisdiction, approving a petition seeking reorganization of Borrower or all or a substantial part of the assets of Borrower, or appointing a receiver, trustee or liquidator of

Borrower or any of its property, and such order, judgment or decree shall continue unstayed and in effect for any period of sixty (60) days.

Upon the occurrence of any event of default, the entire unpaid principal sum hereunder plus all interest accrued thereon plus all other sums due and payable to Lender hereunder shall, at the option of Lender, become due and payable immediately. In addition to the foregoing, upon the occurrence of any event of default, Lender may forthwith exercise singly, concurrently, successively or otherwise any and all rights and remedies available to Lender by law, equity, statute or otherwise.

Borrower hereby waives presentment, demand, notice of nonpayment, protest, notice of protest or other notice of dishonor in connection with any default in the payment of, or any enforcement of the payment of, all amounts due hereunder. To the extent permitted by law, Borrower waives the right to any stay of execution and the benefit of all exemption laws now or hereafter in effect.

Following the occurrence of any event of default, Borrower will pay upon demand all costs and expenses (including all amounts paid to attorneys, accountants, and other advisors employed by Lender), incurred by Lender in the exercise of any of its rights, remedies or powers hereunder with respect to such event of default, and any amount thereof not paid promptly following demand therefor shall be added to the principal sum hereunder and will bear interest at the contract rate set forth herein from the date of such demand until paid in full. In connection with and as part of the foregoing, in the event that this Note is placed in the hands of an attorney for the collection of any sum payable hereunder, Borrower agrees to pay reasonable attorneys' fees for the collection of the amount being claimed hereunder, as well as all costs, disbursements and allowances provided by law.

If for any reason one or more of the provisions of this Note or their application to any entity or circumstances shall be held to be invalid, illegal or unenforceable in any respect or to any extent, such provisions shall nevertheless remain valid, legal and enforceable in all such other respects and to such extent as may be permissible. In addition, any such invalidity, illegality or unenforceability shall not affect any other provisions of this Note, but this Note shall be construed as if such invalid, illegal or unenforceable provision had never been contained herein.

This Note inures to the benefit of Lender and binds Borrower and Lender's and Borrower's respective successors and assigns, and the words "Lender" and "Borrower" whenever occurring herein shall be deemed and construed to include such respective successors and assigns.

This Promissory Note is one of the promissory notes referred to in the Financial Services Agreement dated as of June 15, 2000 between Borrower and Lender to which reference is made for a statement of additional rights and obligations of the parties hereto.

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IN WITNESS WHEREOF, Borrower has executed this Promissory Note the day  
and year first written above.

[BORROWER]

By: \_\_\_\_\_  
Name and Title:

EXHIBIT B  
PROMISSORY NOTE  
FOR LONG-TERM BORROWINGS

\$ \_\_\_\_\_, 2000

FOR VALUE RECEIVED, [NAME OF COMPANY], a \_\_\_\_\_ corporation (herein "Borrower") hereby promises to pay to the order of American Water Capital Corp., a Delaware corporation ("Lender"), in same day funds at its offices at \_\_\_\_\_ or such other place as Lender may from time to time designate, the principal sum of \_\_\_\_\_ dollars (\$ \_\_\_\_\_), together with interest thereon from the date hereof until paid in full. Interest shall be charged on the unpaid outstanding principal balance hereof at a rate per annum equal to the rate paid and to be paid by Lender with respect to the borrowings it made in order to provide funds to Borrower hereunder. Interest on borrowings shall be due and payable in immediately available funds on the same business day on which the Lender must pay interest on the borrowings it made in order to provide funds to the Borrower hereunder. The principal amount hereof shall be due and payable hereunder at such times and in such amounts and in such installments hereunder as the Lender must pay with respect to the borrowings it made in order to provide funds to the Borrower hereunder. Lender has provided Borrower with a copy of the documentation evidencing the borrowings made by Lender in order to provide funds to Borrower hereunder. In the absence of manifest error, such documentation and the records maintained by Lender of the amount and term, if any, of borrowings hereunder shall be deemed conclusive.

The occurrence of one or more of any of the following shall constitute an event of default hereunder:

(a) Borrower shall fail to make any payment of principal and/or interest due hereunder or under any other promissory note between Lender and Borrower within five business days after the same shall become due and payable, whether at maturity or by acceleration or otherwise;

(b) Borrower shall apply for or consent to the appointment of a receiver, trustee or liquidator of itself or any of its property, admit in writing its inability to pay its debts as they mature, make a general assignment for the benefit of creditors, be adjudicated a bankrupt or insolvent or file a voluntary petition in bankruptcy or a petition or an answer seeking reorganization or an arrangement with creditors or to take advantage of any bankruptcy, reorganization, insolvency, readjustment of debt, dissolution or liquidation of law or statute, or an answer admitting the material allegations of a petition filed against it in any proceeding under any such law, or if action shall be taken by Borrower for the purposes of effecting any of the foregoing; or

(c) Any order, judgment or decree shall be entered by any court of competent jurisdiction, approving a petition seeking reorganization of Borrower or all or a substantial part of the assets of Borrower, or appointing a receiver, trustee or liquidator of Borrower or any of its property, and such order, judgment or decree shall continue unstayed and in effect for any period of sixty (60) days.



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F. 10

Upon the occurrence of any event of default, the entire unpaid principal sum hereunder plus all interest accrued thereon plus all other sums due and payable to Lender hereunder shall, at the option of Lender, become due and payable immediately. In addition to the foregoing, upon the occurrence of any event of default, Lender may forthwith exercise singly, concurrently, successively or otherwise any and all rights and remedies available to Lender by law, equity, statute or otherwise.

Borrower hereby waives presentment, demand, notice of nonpayment, protest, notice of protest or other notice of dishonor in connection with any default in the payment of, or any enforcement of the payment of, all amounts due hereunder. To the extent permitted by law, Borrower waives the right to any stay of execution and the benefit of all exemption laws now or hereafter in effect.

Following the occurrence of any event of default, Borrower will pay upon demand all costs and expenses (including all amounts paid to attorneys, accountants, and other advisors employed by Lender), incurred by Lender in the exercise of any of its rights, remedies or powers hereunder with respect to such event of default, and any amount thereof not paid promptly following demand therefor shall be added to the principal sum hereunder and will bear interest at the contract rate set forth herein from the date of such demand until paid in full. In connection with and as part of the foregoing, in the event that this Note is placed in the hands of an attorney for the collection of any sum payable hereunder, Borrower agrees to pay reasonable attorneys' fees for the collection of the amount being claimed hereunder, as well as all costs, disbursements and allowances provided by law.

If for any reason one or more of the provisions of this Note or their application to any entity or circumstances shall be held to be invalid, illegal or unenforceable in any respect or to any extent, such provisions shall nevertheless remain valid, legal and enforceable in all such other respects and to such extent as may be permissible. In addition, any such invalidity, illegality or unenforceability shall not affect any other provisions of this Note, but this Note shall be construed as if such invalid, illegal or unenforceable provision had never been contained herein.

This Note inures to the benefit of Lender and binds Borrower and Lender's and Borrower's respective successors and assigns, and the words "Lender" and "Borrower" whenever occurring herein shall be deemed and construed to include such respective successors and assigns.

This Promissory Note is one of the promissory notes referred to in the Financial Services Agreement dated as of June 15, 2000 between Borrower and Lender to which reference is made for a statement of additional rights and obligations of Lender and Borrower.

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IN WITNESS WHEREOF, Borrower has executed this Promissory Note the day and year first written above.

[BORROWER]

By: \_\_\_\_\_  
Name and Title:

**GAC LEASE AGREEMENT**

**LEXINGTON, KENTUCKY**

This LEASE AGREEMENT is made this 21 day of January, 2002 between American Water Resources, Inc. (doing business as American Carbon Services) a Virginia corporation, having its principal office at 1025 Laurel Oak Drive, Voorhees, New Jersey 08043 (hereinafter "American Carbon Services") and Kentucky-American, a Kentucky corporation, having its principal office in Lexington, Kentucky (hereinafter "Kentucky");

WHEREAS, American Carbon Services is the owner of a carbon reactivation plant in Columbus, Ohio, that has the capability to provide custom reactivated carbon to the potable water industry; and

WHEREAS, Kentucky has a need for Granular Activated Carbon ("GAC"), for the purpose of Taste and Odor ("T&O) control in its Lexington, Kentucky water plant; and

WHEREAS, American Carbon Services is willing to provide GAC to Kentucky on a lease basis.

THEREFORE, Kentucky desires to enter into this Agreement with American Carbon Services to provide all GAC that Kentucky will procure during 2002, and in consideration of the mutual promises contained in this Agreement the parties agree as follows:

A. Services

1. American Carbon Services will pick up spent carbon requiring reactivation from the six (6) filters, Filters #11, #12, #13, #14, #15 and #16 at the Lexington, Kentucky water plant and transport the spent carbon to its carbon reactivation plant located in Columbus, Ohio during the initial term of this Agreement on a schedule agreed to by the parties. American Carbon Services will provide all labor and equipment for the removal and replacement of all carbon at the Lexington, Kentucky water plant.

2. American Carbon Services will reactivate all spent bituminous carbon and will return all reactivated carbon meeting the Quality Control specifications, set forth in Exhibit I, attached to and made part of this Agreement. In addition, American Carbon Services will provide all make up carbon necessary to return to Kentucky the required volume fill of 680 cubic feet of GAC for each filter. Kentucky acknowledges that American Carbon Services has title to and is the owner of all GAC supplied by American Carbon

Services under this Agreement. Kentucky may not remove the GAC from the filters or cause the GAC to be removed except for emergency maintenance in accordance with the terms of this Agreement.

3. American Carbon Services will test all carbon supplied under this Agreement every six months from samples supplied by Kentucky. The first test will occur during the month of July 2002 and shall include Iodine Number, Apparent Density, Total Ash, Abrasion Number and Screen Analysis.

4. Upon termination of this Agreement, American Carbon Services will provide for the removal, transportation, reactivation and disposal of any GAC provided under this Agreement, unless Kentucky elects to maintain the carbon in service in accordance with Section B.2., below.

5. Kentucky will provide all necessary water, electricity and suitable drainage to accomplish the transfer of the spent and reactivated carbon into and out of filters.

B. Consideration

1. Kentucky shall pay American Carbon Services for the services provided under clauses 1 through 3 of Section A a monthly fee of \$2,850.00 beginning on the first day of the month following installation of all carbon to be initially provided by American Carbon Services, and continuing for the term of this Agreement.

2. Kentucky shall pay American Carbon Services a monthly fee of \$1,425.00 per month for all months beyond the initial term that the GAC is in service at the Kentucky water plant. The payments shall be due on the first day of each month that the GAC remains in service.

3. In the event that Kentucky elects to terminate this Agreement as provided in paragraph D below, American Carbon Services will provide the services in Section A.4 and Kentucky will pay American Carbon Services a fee of \$0.15/lb for all GAC removed. The payment shall be due thirty (30) days after the invoice date.

C. Warranty

1. American Carbon Services warrants that the GAC supplied under this Agreement will, during the initial term of this Agreement, provide acceptable T&O control as detailed in Exhibit II.

D. Term

1. The initial term of this Agreement shall begin on the date of initial installation of all GAC and conclude thirty-six (36) months thereafter. At the end of the initial term, this Agreement shall be automatically extended on a month-to-month basis unless and until either party provides not less than thirty (30) days prior written notice to the other of termination; provided, however, that any such extension shall not extend the warranty under Section C, above, beyond the expiration of the initial thirty-six (36) month term. Following receipt by American Carbon Services of such notice of termination, American Carbon Services will provide the services in Section A.4 and Kentucky will pay American Carbon Services a fee of \$0.15/lb. of carbon removed from filters. Payment shall be due thirty (30) days after the invoice date.

E. Force Majeure

Either party hereto shall be excused to the extent that its performance is prevented by any circumstance reasonably beyond its control, including, but not limited to, fire, explosion, strike, labor dispute, war, act of God, riot, or action of any governmental authority.

F. Kentucky Law to Govern

This Agreement shall be governed and construed in accordance with the laws of the State of Kentucky without giving effect to conflict of law principles.

G. Notices

All notices required under this Agreement shall be given by Certified Mail, Return Receipt Requested and shall be deemed made when deposited in the U.S. Mails properly addressed, with postage prepaid, as follows:

American Water Resources, Inc.  
1025 Laurel Oak Rd.  
Voorhees, NJ 08043  
Attn: Mr. Stephen Gordon, President

Kentucky-American Water Company  
2300 Richmond Road  
Lexington, KY 40502  
Attn: Nick Rowe, Vice President

H. Taxes

The fees provided for in this Agreement to be paid by Kentucky do not include any taxes or other assessments. Kentucky agrees to pay all taxes or governmental assessments imposed on the services to be provided by American Carbon Services.

I. Miscellaneous

1. This Agreement shall not be assignable by either party without the written consent of the other party, which consent shall not unreasonably be withheld. Any assignee shall assume all the obligations of this Agreement and the assignor shall not be relieved of its obligations under this Agreement by reason of an assignment.

2. This Agreement constitutes the entire agreement between the parties. All previous representations relative hereto, either written or oral, are hereby annulled and superseded. No modifications shall be binding on either party unless it shall be in writing and signed by an authorized officer of both parties.

3. Any waiver by either party of any provision or condition of this Agreement shall not be construed or deemed to be a waiver of any other provision or condition of this Agreement nor a waiver of a subsequent breach of the same provision or condition unless such waiver be so expressed in writing and signed by the party to be bound.

4. If any provision contained herein is held to be unenforceable by a court of law or equity, this Agreement shall be construed as if such provisions did not exist and the unenforceability of such provision shall not be held to render any other provision of this Agreement unenforceable.

5. The reactivation must be conducted in a facility dedicated exclusively to the reactivation of GAC from potable water treatment plants. No reactivation facility which has accepted GAC used for purposes other than potable water treatment is acceptable for use under this Agreement. The GAC shall not be mixed or blended with any

other reactivated GAC or exposed to any other reactivation products. All equipment used for reactivation, transport and installation which will come into contact with Kentucky's GAC, including but not limited to GAC storage and feed equipment, GAC cooling, screening and handling equipment, shall be cleaned and thoroughly purged of any previous client's material. Kentucky's GAC for reactivation must be treated as a discreet and separate batch and shall not contact any other reactivated GAC

6. Only NSF-Approved bituminous virgin GAC may be supplied for makeup purposes. The virgin GAC supplier must have at least 10 water treatment plants of similar source as the Kentucky plant using the virgin GAC in service for at least five (5) years. No other sources of GAC for reactivation purposes will be acceptable.

7. American Carbon Services hereby agrees to indemnify and save harmless Kentucky against any and all liability, loss, damage, costs or expense which Kentucky may incur, suffer or be required to pay by reason of any release of hazardous materials, hazardous wastes or hazardous substances, which release arises out of or occurs in connection with the acts of transportation, handling, treatment, storage, disposal or other activity in connection with the GAC which is the subject hereof.

8. At least two weeks prior to beginning the GAC exchange operation, a responsible American Carbon Services representative shall meet with the applicable Kentucky Operations Superintendent to review the plans for the GAC exchange operation, including daily dates and times work is to begin and to end, to determine if any special circumstances exist, and to determine if any special equipment is required. Any auxiliary equipment, services, or materials required to conduct the GAC exchange operation shall be provided by American Carbon Services at no additional cost to Kentucky.

9. At least one week prior to beginning the GAC exchange operation, American Carbon Services shall provide Kentucky with a written schedule showing dates and times of installation. The Kentucky Operations Superintendent shall approve this schedule. The GAC exchange operation shall commence promptly each day by 8:00 A.M., and sufficient labor shall be provided by American Carbon Services in order to minimize the amount of time each filter is out of service. Any overtime incurred by Kentucky

personnel as a result of deviation of this schedule shall be reimbursed in full to Kentucky by American Carbon Services.

10. All scheduling of deliveries of materials, equipment, services and GAC shall be conducted by the responsible American Carbon Services representative. Any additional costs incurred as a result of scheduling conflicts, errors, or omissions shall be paid solely by American Carbon Services.

11. During the GAC removal process, all GAC is to be removed from the applicable filters with exception of up to a maximum of one inch of GAC. The contractor shall remove the GAC in a manner so as not to disturb sand and gravel layers. Any sand replacement required as result of disturbance during GAC removal shall be replaced and paid for by American Carbon Services. All waste sand, GAC, or other waste materials generated as a result of the exchange operation shall be removed and properly disposed of by American Carbon Services, at no additional cost to Kentucky.

12. The depth of reactivated GAC installed in each filter shall deviate by no more than one inch from the depths listed in Exhibit III at the completion of installation of each filter. No additional filters shall be taken out of service for exchange purposes until the proper depth in each completed filter has been verified by the Kentucky Operations Superintendent.

13. In order to avoid freezing of equipment and installation delay which could jeopardize the operation of the treatment plant, to the extent operationally practicable, the GAC exchange process shall not occur during periods in which air temperatures drop below 15 degrees Fahrenheit. Where possible and practical, the exchange operation shall be temporarily postponed and rescheduled to when temperature conditions are more favorable. The time period shown in Exhibit III may be extended for a period of up to one month should this condition occur.


IN WITNESS WHEREOF, the parties have caused this Agreement to be executed

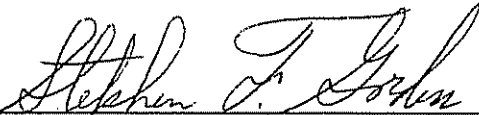


IN WITNESS WHEREOF, the parties have caused this Agreement to be executed  
by their duly authorized representatives.

ACCEPTED AND AGREED:  
KENTUCKY-AMERICAN  
WATER COMPANY

ACCEPTED AND AGREED:  
AMERICAN WATER RESOURCES, INC

By:   
\_\_\_\_\_  
Nick Rowe

By:   
\_\_\_\_\_  
Stephen Gorden

Title: Vice President

Title: President

Date 1-23-02

Date 1-21-02

**EXHIBIT I**

**GRANULAR ACTIVATED CARBON PROPERTIES**

Iodine number	800 minimum
Density	28-30 lb./cubic foot
Effective Size	0.8 - 1.0 mm
Uniformity Coefficient	2.1 maximum
Moisture	2% maximum
Abrasion Number	75 minimum
Typical Mesh Size	8 x 30 mm

## EXHIBIT II

### WARRANTY

American Carbon Services warrants that, when used under normal conditions, as currently exist at the Lexington, Kentucky Plant, the GAC provided under this Agreement will perform the function of adsorption of dissolved organics which contribute to taste and odors during the life of the warranty. For purposes of warranty, effective T&O control is defined as the reduction of adsorbable dissolved odors such that the threshold order number of the carbon filtered water as measured by the procedure defined in "Standard Methods for the Examination of Water and Wastewater", 20<sup>th</sup> Edition, shall not persistently exceed two (2) in the carbon filtered effluent for four (4) consecutive days with the treatment plant in normal operation. The warranty will begin on the date of installation of the GAC and continue for thirty-six (36) months thereafter. The warranty is contingent on the following:

- A. If the concentration of organics in the raw water supply should greatly exceed general background levels, as in the case of an accidental industrial discharge, chemical spill or other adversity, Kentucky will initiate the feed of powered carbon or may elect a complete bypass of contaminated water during the course of abnormal conditions. If emergency measures are not taken immediately to prevent the GAC from being exposed to excessive levels of organic contaminants, the warranty will be voided.
- B. Normal treatment of the water prior to carbon filtration will continue to be practiced. This includes suitable disinfection, coagulation and clarification of the raw water and stabilization of the clarified water before GAC filtration.
- C. Average and maximum filtration rates will not exceed 3.0 and 4.0 gallons per minute per square foot, respectively.
- D. The GAC will be maintained by Kentucky in each filter with the exception of a possible loss of up to one and one-half (1.5) inches of GAC bed depth per year attrition losses. If losses should exceed one and one-half (1.5) inches of bed depth in any filter during any one-(1) year of operation, the excess GAC loss will be replaced. Kentucky shall pay American Carbon Services for any such replacement of GAC at a price of seventy-five cents (\$0.75) per pound or replace the GAC using material that meets that specifications given in Exhibit I.
- E. The water plant filters will be maintained in good operating condition and in accordance with accepted industry practice.

If the GAC fails to perform due to encrustation by inorganic precipitates, this shall not be considered to be a breach of the warranty and Kentucky will bear the cost of cleaning the GAC to restore performance, in accordance with procedures provided by American Carbon Services.

Should the GAC during the warranty period fail to perform in accordance with the warranty, American Carbon Services will, at its sole option, either reactivate or replace all or part of the GAC to restore its capability to meet the warranty. All cost to bring the GAC back into compliance with the terms of this warranty will be for the account of American Carbon Services.

EXCEPT AS SET FORTH IN THIS EXHIBIT II, AMERICAN CARBON SERVICES MAKES NO WARRANTY EXPRESSED OR IMPLIED, INCLUDING THE WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE, WITH RESPECT TO THE CARBON OR THE SERVICES TO BE PROVIDED UNDER THIS AGREEMENT. AMERICAN CARBON SERVICES SHALL HAVE NO LIABILITY FOR ANY INDIRECT, INCIDENTAL OR CONSEQUENTIAL DAMAGES ARISING OUT OF A BREACH OF THIS WARRANTY. KENTUCKY'S SOLE REMEDY FOR ANY BREACH OF THIS WARRANTY SHALL BE TO REQUIRE AMERICAN CARBON SERVICES TO EITHER REACTIVATE OR REPLACE CARBON AS PROVIDED ABOVE.

EXHIBIT III

KENTUCKY-AMERICAN WATER COMPANY — LEXINGTON WTP

Filter No.	Surface Area (sq. ft.)	Carbon Depth (inches)	Carbon Volume (cubic feet)	Exchange Date
11	340	24	680	Feb./2002
12	340	24	680	Feb./2002
13	340	24	680	Feb./2002
14	340	24	680	Feb./2002
15	340	24	680	Feb./2002
16	340	24	680	Feb/2002