

**KENTUCKY-AMERICAN WATER COMPANY**  
**CASE NO. 2008-00427**  
**PUBLIC SERVICE COMMISSION'S FIRST SET OF INFORMATION REQUESTS**  
**ITEMS 1 – 33**

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Witness Responsible: Michael A. Miller

29. a. State the date on which Kentucky-American implemented Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes."
- b. State the effect(s) on Kentucky-American's financial statements as a result of implementing Statement of Financial Accounting Standards No. 109.
- c. State whether the base period or forecasted period includes any effect of the implementation of Statement of Financial Accounting Standards No. 109.
- d. If Kentucky-American's base period or forecasted period includes any effect of the implementation of Statement of Financial Accounting Standards No. 109, describe each effect in detail.

Response:

- a. SFAS was implemented 1/1/93
- b. See adoption entry below.
- c. The base year and forecast test years are not impacted by the FAS 109 adoption entry which was recorded in 1993 some fifteen years ago.
- d. See response to Item C above.

Kentucky-American Water Company

SFAS 109 Adoption Entry

March 1993

	<u>Debit</u>	<u>Credit</u>
Regulatory Liability-ITC		1,362,555
Regulatory Asset-AFUDC Gross-up	1,665,625	
Preliminary Survey (KRS II) – AFUDC Gross-up	18,396	
Abandonment Loss (KRS II) – AFUDC Gross-up	12,235	
Excess Deferred Tax-AFUDC		365,002
Excess Deferred Tax Reserve South Georgia		3,422,991
Regulatory Asset – Temporary Differences Previously flowed thru	5,023,813	
Gross-up Customer Advances		1,872,348

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Excess Deferred Tax-Customer Advance Gross-up	52,919	
Reverse Existing Current Taxes Deferred under APB11		5,049
Reverse Existing Non-Current Taxes Deferred under APB11	12,148,410	
Record Current Deferred SIT under FAS 109	7,937	
Record Non-Current Deferred Sit under FAS 109	30,011	
Record Current Deferred FIT under FAS 109		1,645,185
Record Non-Current Deferred FIT under FAS 109		<u>10,292,689</u>
Cumulative Effect of FAS 109 Adoption	<u>6,473</u>	
TOTALS	18,965,819	18,965,819

For the electronic version, see KAW\_R\_PSCDR1#29\_111408.pdf.

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Witness Responsible: Michael A. Miller

30. a. State whether Kentucky-American's 1989 service contract with the American Waterworks Service Company ("Service Company") has been modified, amended, or replaced.
- b. If the 1989 service contract has been modified, amended, or replaced, provide a complete copy of the current service contract and identify the areas in that contract that differ from the 1989 service contract.

Response:

- a. The 1989 Service Company Contract has not been modified.
- b. Not applicable.

For the electronic version, please refer to KAW\_R\_PSCDR1#30\_111408.pdf.

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Witness Responsible: Michael A. Miller

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

For electronic version, refer to [KAW\\_R\\_PSCDR1#31\\_111408.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.

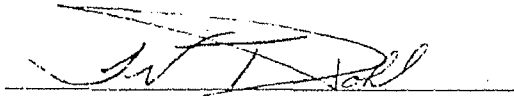
ARTICLE VI. TERM OF AGREEMENT

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.

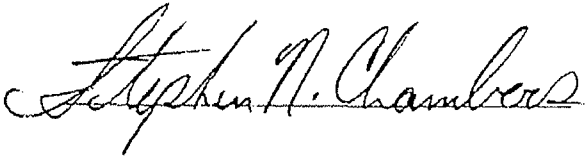
ATTEST:



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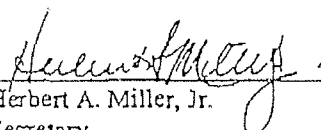
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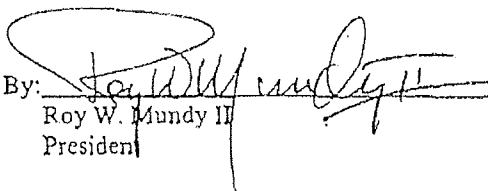
10. Copies. This Agreement may be executed by the parties in one or more copies and each executed copy shall be considered an original.

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:

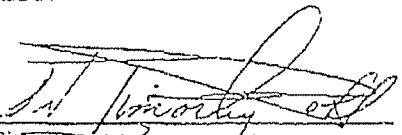
KENTUCKY-AMERICAN WATER COMPANY


By:   
Herbert A. Miller, Jr.  
Secretary

By:   
Roy W. Mundy II  
President

ATTEST:

AMERICAN WATER CAPITAL CORP.

By:   
Title: D. 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.

03-28-02 16:04

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P.08

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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PAGE

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.

03-28-02 16:05

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P. 11

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

[BORROWER]

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

**GAC REACTIVATION AND LEASE AGREEMENT**  
**2008-2011**

**Lease 121**

**THIS AGREEMENT** ("Agreement") is made as of the 1<sup>st</sup> day of April, 2008 ("Effective Date"), by and between AAET, L.P., a Delaware limited partnership, having its principal office at 1025 Laurel Oak Road, Voorhees, New Jersey 08043 (hereinafter, "ACS") and Kentucky-American Water Company, a Kentucky corporation, having its principal office at 2300 Richmond Road, Lexington, Kentucky 40502 (hereinafter, "KAWC").

**RECITALS**

**WHEREAS**, ACS owns and operates a custom Granular Activated Carbon ("GAC") reactivation facility ("Facility") that reactivates GAC to be used, among other things, by treatment plants in the potable water industry; and

**WHEREAS**, KAWC owns and operates a water treatment plant in Lexington, Kentucky ("Plant"), which treats water for the purpose of taste and odor ("T&O") control using, among other things, GAC media; and

**WHEREAS**, KAWC wishes to lease a certain quantity of reactivated GAC media from ACS and ACS wishes to provide reactivation services and lease the specified quantity of reactivated GAC media to KAWC.

**NOW, THEREFORE**, in consideration of the mutual covenants contained herein, the adequacy of which is hereby acknowledged, and intending to be legally bound, the parties hereto agree as follows:

The foregoing Recitals are hereby incorporated into and made part of this Agreement.

A. Services

1. As of the Effective Date of this Agreement, the Plant's filters contain spent GAC media leased to KAWC by ACS pursuant to a prior lease agreement by and between the parties. Beginning as of the Effective Date, ACS will retrieve and reassume ownership of the spent GAC media located in the Plant's filters, which it will do in

accordance with the specifications set forth in Exhibit I, attached hereto, and incorporated herein. ACS will determine the level of the GAC media before the GAC media is removed from each filter by measuring the GAC media depth in place after backwashing ("Noted Level").

2. ACS and will transport the spent GAC media to the Facility for reactivation, which it shall do at its sole cost and expense. ACS will reactivate the spent GAC media at the Facility and sample the reactivated GAC in accordance with the parameters set forth in Exhibit II, attached hereto, and incorporated herein. The test results shall meet the standards set forth in Exhibit II before the reactivated GAC media may be returned to the Plant's filters. ACS will provide KAWC with a copy of the analytical data from the sampling. KAWC reserves the right to conduct initial sampling of the reactivated GAC media to verify contract specifications, which it may do at its sole cost and expense.

3. ACS will return the reactivated GAC media to the Plant for reinstallation following testing and approval. If the volume of GAC media for a filter is below the Noted Level upon replacement of the reactivated GAC media, ACS will provide the quantity of GAC media necessary to return the filter to the Noted Level of fill. ACS will not adjust the cost of the Base Lease Fee or provide additional media at no additional cost in order to fill to a volume of GAC media that is calculated after a filter's initial backwashing.

4. Once installed, the reactivated GAC media will remain in the Plant's filters for the duration of the Agreement Term. During the Term, ACS will test all GAC media supplied under this Agreement every six (6) months from samples supplied by KAWC to determine levels of exhaustion, which ACS will do at its sole cost and expense. The testing shall include the following parameters: Iodine Number, Apparent Density, Total Ash, Abrasion Number, Effective Size, Uniformity Coefficient, and Screen Analysis. ACS will submit copies of the test results to KAWC's local Production Manager, as well as the Service Company Environmental Director.

5. KAWC shall provide all necessary water, electricity, and suitable drainage to accomplish the transfer of the spent and reactivated/virgin GAC media into and out of the filters at the Plant, which it will do at its sole cost and expense.

B. Term

1. The term of the Agreement shall commence as of the Effective Date, and shall include the time during which ACS removes the GAC media and reactivates it, as well as the subsequent thirty-six (36) month lease term (collectively, "Term"). The lease term shall be for a period of thirty-six (36) months, as set forth above, beginning April 1, 2008, and ending March 31, 2011 ("Lease Term"), subject to the Uncontrollable Circumstances and termination provisions set forth hereinbelow. For purposes herein, April 1<sup>st</sup> to March 31<sup>st</sup> of each year will be referred to as a "Term Year". It is understood by and between the parties that ACS will be removing and reactivating the GAC media during the first (1<sup>st</sup>) month of the Term, with the Lease Term to commence immediately upon installation of the reactivated GAC media in the Plant's filters. If the reactivation is delayed due to unforeseen conditions or Uncontrollable Circumstances, as more particularly set forth hereinbelow, the Lease Term and Term Year will be adjusted accordingly.

2. Upon conclusion of the Term of this Agreement, KAWC shall have the right to do the following: (a) request that ACS reactivate the GAC media from some or all of the Plant filters specified in Exhibit I and return the reactivated GAC to the Plant for another lease term, at a cost to be agreed-upon by and between the parties and memorialized in a separate agreement; (b) request that ACS remove the GAC media from some or all of the Plant filters specified in Exhibit I, at a cost to be agreed-upon by and between the parties and memorialized in a separate agreement, at which time ACS will reassume title to the GAC and KAWC will relinquish any leasehold interest therein; or (c) KAWC will maintain the service of the GAC media in the Plant's filters for a period not to exceed one (1) year, extending the Term of this Agreement for that period ("Extension Term"). If KAWC elects to maintain service of the GAC media during the Extension Term, ACS shall not be liable for the failure of the GAC media to control T&O, or for damage that may be caused to the filters or the Plant as a result thereof. KAWC shall notify ACS of its election of one the above options not less than sixty (60) days prior to the conclusion of the Agreement Term. If KAWC wishes to enter into an Extension Term, it shall notify ACS of the desired term, of up to one (1) year, when elected.



C. Consideration

1. KAWC shall pay ACS a monthly fee of \$ 3,872.29 for the lease of the GAC media and the services provided under clauses 1 through 4 of Section A, above ("Base Lease Fee"). The Base Lease Fee shall not be due and owing until ACS has installed the reactivated GAC media into the Plant's filters. Payment of the Base Lease Fee shall commence on the first (1<sup>st</sup>) day of the month that follows ACS's installation of the reactivated GAC media in the filters, and shall be payable on the first (1<sup>st</sup>) day of each month thereafter for thirty-six (36) consecutive months.

2. If KAWC elects to maintain the service of the GAC media in the Plant filters for the Extension Term, as more particularly set forth in Section B.5(c), above, KAWC shall pay ACS a monthly fee of \$ 1,936.15 per month ("Extension Fee"), which shall be due on the first (1<sup>st</sup>) day of each month that the GAC media remains in service; with the first payment being due and owing on April 1, 2011.

3. ACS will remove the GAC media from the filters under the following circumstances: (a) KAWC elects to terminate the Agreement pursuant to the terms set forth in Section F, below; (b) KAWC does not elect to enter into a renewal agreement upon termination of the Agreement Term; (c) KAWC does not elect to maintain the GAC media during an Extension Term; (d) KAWC otherwise requests to have the GAC media removed from the filters as provided for herein; or (e) this Agreement is otherwise terminated. In such instances, KAWC will pay ACS a fee of \$0.25/lb for all GAC media removed ("Removal Fee"), and the parties will have no further obligation to each other, except as otherwise set forth herein. ACS and KAWC will measure the volume of the GAC media upon removal from the filters in accordance with the standards set forth herein. ACS will invoice KAWC for the removal fee, which payment shall be due thirty (30) days following the invoice date.

4. KAWC shall pay interest on all outstanding amounts due to ACS at a rate of prime (as published in The Wall Street Journal), plus three percent (3%). Such interest shall be calculated and added to any unpaid amounts on a monthly basis, but shall not be compounded or treated as recomputed principal. Interest shall begin to accrue on the fifteenth (15<sup>th</sup>) day following the due date of the invoice.

5. ACS will invoice KAWC for the Base Lease Fee after all GAC media is installed in the appropriate filters as shown in the timeframes established in Exhibit I, and subsequently, for Extension Fee and Removal Fees, as applicable. ACS will send the invoices to the Shared Services Center of American Water for processing. A copy of the invoices should be sent to the attention of the following KAWC representative, as well, unless and until KAWC designates a different representative:

Dillard Griffin  
Production Superintendent, Lexington  
Kentucky American Water Company  
2300 Richmond Road.  
Lexington, Kentucky 40502  
Office: 859-268-6340  
E-mail: dillard.griffin@amwater.com  
Workbasket: A12SEC05

6. ACS is providing KAWC with invoices for the Base Lease Fee and Extension Fee as a courtesy for bookkeeping purposes. In no instance will a delayed or missing invoice be deemed cause for KAWC to fail to pay the Base Lease Fee or Extension Fee within the timeframe set forth above.

D. Warranty

1. Pursuant to the terms of the Warranty set forth in Exhibit III, attached hereto and incorporated herein, ACS warrants that the reactivated GAC media will provide T&O control for a period of thirty-six (36) months from the date of the reactivated GAC media's installation in the Plant's filters. In no instance will ACS's warranty of the GAC media be extended beyond the thirty-six (36) month warranty period, including, without limitation, during any Extension Term.

E. Uncontrollable Circumstances

1. An "Uncontrollable Circumstance" is any act, event, condition or circumstance that (1) is beyond the reasonable control of the party relying thereon as justification for not performing an obligation of such party under the Agreement, (2) by itself or in combination with other acts, events, conditions or circumstances adversely affects, interferes with or delays the party's ability to perform its obligations under the

Agreement, expands the scope of the party's obligations under the Agreement, or increases the party's cost of performing its obligations under the Agreement, and (3) is not the direct result of the willful or negligent act, intentional misconduct, or breach of the Agreement by the party claiming the occurrence of an Uncontrollable Circumstance.

2. If an Uncontrollable Circumstance occurs, the affected party shall be entitled to (1) relief from its performance obligations under the Agreement to the extent the occurrence of the Uncontrollable Circumstance prevents its performance of such obligations, (2) an extension of schedule to perform its obligations under the Agreement to the extent the occurrence of the Uncontrollable Circumstance prevents its ability to perform such obligations in the time specified in the Agreement, and (3) an increase in the fee to be paid under the Agreement to the extent the occurrence of the Uncontrollable Circumstance increases its costs of performance of its obligations under the Agreement. The occurrence of an Uncontrollable Circumstance shall not, however, excuse or delay KAWC's obligation to pay monies previously accrued and owing to ACS under the Agreement, or for ACS to perform any obligation under the Agreement not affected by the occurrence of the Uncontrollable Circumstance.

F. Default/Termination

1. Notwithstanding the terms set forth under Section C., above, relating to non-payment of the Base Lease Fee, Extension Fee and Removal Fees, either party shall be deemed in default under the Agreement for its failure to perform any material term, covenant or condition of the Agreement and such failure continues for more than thirty (30) days following the non-defaulting party ("Non-Defaulting Party") giving notice of such default to the defaulting party ("Defaulting Party"); provided, however, that if and to the extent such default cannot reasonably be cured within the thirty (30) day period, and the Defaulting Party has diligently attempted to cure same and continues to diligently attempt to cure same thereafter, then the cure period provided for herein shall extend up to, but in no case more than, a collective sixty (60) days. In the event of a party's default, the Non-Defaulting party shall provide written notice to the Defaulting Party outlining the basis for the alleged material breach or default of its obligations under this Agreement.

2. The Non-Defaulting Party shall have the right to terminate the Agreement upon notice to the Defaulting Party following conclusion of the cure period(s) set forth in Section F.1., above; provided that, (1) the defaulting party has not cured such default within thirty (30) days of notice being given to it, or (2) such breach is capable of being cured or remedied but cannot be cured or remedied within such thirty (30) day period, and the defaulting party either fails to commence such cure or remedy as soon as reasonably possible following such thirty (30) day period or fails to cure the default within a collective sixty (60) days.

3. The right to terminate for default shall be in addition to any other remedy available at law for material breach or default.

4. KAWC has the right to terminate the Agreement for convenience, to be effective upon completion of the first or second Term Years, which right it shall exercise not later than December 1<sup>st</sup> of the year prior. By way of example, but not limitation, should KAWC elect to terminate the Agreement upon the conclusion of the first Term Year, it shall provide notice of its election to ACS not later than December 1, 2008, with the termination to be effective as of March 31, 2009. In no instance shall KAWC have the right to terminate for convenience before conclusion of any Term Year, or during the first Term Year.

#### G. Dispute Resolution

1. If there is a dispute between the parties arising under this Agreement that does not involve claims made by or asserted against third parties, the parties to this Agreement agree to submit such disputes to non-binding mediation, which shall be considered an express condition precedent to any further resolution process. If the parties are unable to resolve such disputes through mediation, the parties shall be entitled to submit the dispute to a court of competent jurisdiction in the State of Kentucky. If the parties mutually agree to do so, the parties may agree to arbitration in lieu of litigation in the local court system, through a mutually agreed upon dispute resolution agency.

2. If there is a claim or demand made in any proceeding against ACS by any third party, which arises out of or relates to the ACS's duties or obligations under this Agreement, nothing in this Agreement shall be construed to limit, waive or otherwise impair ACS's ability to join KAWC as a party to those proceedings, and to assert claims in the

nature of indemnity or contribution for any damages or losses made against ACS in said proceedings.

3. If there is a claim or demand made in any proceeding against KAWC by any third party, which arises out of or relates to the ACS's work under this Agreement, nothing in this Agreement shall be construed to limit, waive or otherwise impair KAWC's ability to join ACS and to assert claims in the nature of indemnity or contribution for any damages or losses made against KAWC in said proceedings.

H. 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.

I. 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. Mail properly addressed, with postage prepaid, as follows:

To ACS: AAET, L.P.  
C/o Carbon Services Group  
1025 Laurel Oak Road  
Voorhees, New Jersey 08043  
Attn: Adam R. McDonough, Vice President, AAET, Inc.

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

J. Taxes

The fees to be paid by KAWC under this Agreement do not include any taxes or other assessments. KAWC agrees to pay all taxes or governmental assessments imposed on the services and materials provided by ACS pursuant to this Agreement.

K. Miscellaneous

1. This Agreement shall not be assignable by either party without the prior written consent of the other party, which consent shall not be unreasonably 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. The failure of a party to insist on strict performance of any or all of the terms of this Agreement, or to exercise any right to remedy under this Agreement, shall not constitute a waiver or relinquishment of any nature regarding such right or remedy or any other right or remedy. 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. ACS hereby agrees to indemnify, defend and save harmless KAWC against any and all liability, loss, damage, costs or expense that KAWC may incur, suffer or be required to pay as a result of ACS's negligent acts, errors or omissions or failure to perform in accordance with this Agreement, or ACS's violation of any Federal, State or local laws or regulations in its performance of this Agreement, but in either case only to the extent of and in proportion to the degree of fault, failure, or negligence of ACS or any of its officers, directors, employees and agents.

6. KAWC hereby agrees to indemnify, defend and save harmless ACS against any and all liability, loss, damage, costs or expense which ACS may incur, suffer or be required to pay as a result of KAWC's negligent acts, errors or omissions or failure to

perform in accordance with this Agreement, or KAWC's violation of any Federal, State or local laws or regulations in its performance of this Agreement, but in either case only to the extent of and in proportion to the degree of fault, failure, or negligence of KAWC or any of its officers, directors, employees and agents; or the GAC media becoming classified as a hazardous material, hazardous waste or hazardous substance pursuant to applicable environmental laws, while in the care, possession and control of KAWC.

7. ACS shall not be liable or responsible for the transportation, handling, treatment, storage, disposal, or other activity in connection with GAC media that is or becomes a hazardous material, hazardous waste, or hazardous substance.

8. In no event shall the parties be liable to each other, and each party specifically waives as against the other, any and all claims for consequential, incidental, special or punitive damages resulting in any way from performance or non-performance of this Agreement, whether such damages are characterized as arising under breach of contract or warranty, tort (including negligence), fault, strict liability, indemnity or other theory of legal liability.

L. Performance Requirements

1. The reactivation must be conducted in a facility dedicated exclusively to the reactivation of GAC media from potable water treatment plants. No reactivation facility that has accepted GAC media used for purposes other than potable water treatment is acceptable for use under this Agreement. The GAC media shall not be mixed or blended with any other reactivated GAC media or exposed to any other reactivation products. All equipment used for reactivation, transport and installation that will come in contact with KAWC's GAC media, including but not limited to GAC media storage and feed equipment, cooling, screening and handling equipment, shall be cleaned and thoroughly purged of any previous client's material. All of KAWC's GAC media prepared for reactivation must be treated as a discreet and separate batch and shall not contact any other reactivated GAC media.

2. Only NSF-approved bituminous virgin GAC media may be supplied for makeup purposes. The virgin GAC media supplier must have at least ten (10) water treatment plants of similar source as the KAWC plant using the virgin GAC media in

services for at least five (5) years. No other sources of GAC media for reactivation purposes will be acceptable. All reactivated GAC media delivered under this Agreement shall be produced exclusively from the spent GAC media removed from the KAWC Lexington water treatment plant.

3. At least two (2) weeks prior to beginning the GAC media exchange operation, a responsible ACS representative shall meet with the applicable KAWC Production Manager or his/her designated representative to review the plans for the GAC media 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. ACS shall provide any auxiliary equipment, services, or materials required to conduct the GAC media exchange operation, which it shall do at no additional cost to KAWC.

4. At least one (1) week prior to beginning the GAC media exchange operation, ACS shall provide KAWC with a written schedule showing dates and times of installation. The KAWC Production Manager or his/her designated representative shall approve this schedule. The GAC media exchange operation shall commence promptly each day by 8:00 A.M., or other mutually agreed upon time, and ACS shall provide sufficient labor in order to minimize the amount of time each filter is out of service. ACS shall reimburse any overtime incurred by KAWC personnel as a result of deviation from this schedule, except where such deviation is due to KAWC's request, fault, failure or negligence or an uncontrollable circumstance.

5. All scheduling of deliveries of materials, equipment, services, and GAC media shall be conducted by the ACS representative. Any additional costs incurred as a result of scheduling conflicts, errors, or omissions shall be paid solely by ACS, except where such cost overage is due to KAWC's rescheduling, fault, failure or negligence or an uncontrollable circumstance.

6. During the GAC media removal process, all GAC media is to be removed from the applicable filters, with the exception of up to a maximum of one (1) inch of GAC media. The contractor shall remove the GAC media in a manner so as not to disturb sand and gravel layers. Any sand replacement required as result of disturbance during GAC media removal shall be replaced by ACS, at its sole cost. All waste sand, GAC



media, or other waste materials generated as a result of the exchange operation shall be removed and properly disposed of by ACS, at no additional cost to KAWC.

7. Upon completion of installation of the GAC media in each filter, the depth of the reactivated GAC media shall deviate by no more than one (1) inch from the Noted Level. No additional filters shall be taken out of service for exchange purposes until the KAWC - Production Manager or his/her designated agent has verified the proper depth in each completed filter.

8. In order to avoid equipment freezing and installation delays that could jeopardize the operation of the Plant, the GAC media exchange process shall not occur during periods in which air temperatures drop below 15 degrees Fahrenheit, to the extent reasonably and operationally practicable. Where possible and reasonably practical, the exchange operation shall be temporarily postponed and rescheduled to a time when temperature conditions exceed 15 degrees Fahrenheit. The term of the Warranty as set forth in Exhibit III will be extended for a period of time that is proportionate to the delay if the media exchange process is postponed due to inclement weather, as set forth above.

M. Insurance

1. ACS shall return two (2) copies of its current "Certificate of Insurance" ("Certificate") concurrent with the signed Agreement. ACS shall not commence any work under this Agreement until it has provided the Certificate to KAWC.

2. ACS shall carry Workers Compensation Insurance during the life of this Agreement to insure its statutory liability to its employees in the State of Kentucky plus \$100,000 Employers Liability coverage. ACS shall carry the Comprehensive form of General Liability and property damage insurance during the life of this Agreement covering all risks itemized in the form for "Certificate of Insurance" provided in this Agreement. The limits shall not be less than \$1,000,000 for each occurrence of bodily injury and property damage and \$1,000,000 for general aggregate. ACS shall carry the comprehensive form of Automobile Liability and Property damage insurance during the life of this Agreement to cover the risks itemized in the form "Certificate of Insurance" provided for in this Agreement. The limits shall be not less than \$1,000,000 for each occurrence of bodily injury and property damage combined.

3. ACS shall carry Umbrella and/or Excess Liability Insurance during the life of this Agreement covering all risks above the limits shown above. The limit shall not be less than \$1,000,000.

*[signature page to follow]*

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed by their duly authorized representatives as of the date first set forth above.

ACCEPTED AND AGREED:  
Kentucky-American  
Water Company

By: Keith Carter

Title: V.P. Operations

ACCEPTED AND AGREED:  
AAET, L.P.

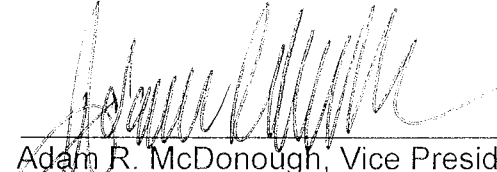
By:   
Adam R. McDonough, Vice President  
of AAET, Inc., its General Partner

EXHIBIT I

Kentucky-American Water Company -- Lexington WTP

GAC Media Exchange Schedule

Filter(s) No.	Surface Area Sq. Ft. Each	GAC Depth Inches	GAC Volume Cu. Ft. Each	Exchange Period	Base Lease Fee Upon Re-Installation
11-16	340	24	680	March 1, 2008 to March 31, 2008	\$ 3,872.29 Per Month

**EXHIBIT II**

**BASELINE 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
Water Soluble Ash	1% maximum
Typical Mesh Size	8 x 30

### EXHIBIT III

#### WARRANTY

ACS warrants that, when used under the conditions that exist at the Lexington water treatment plant as of the Effective Date of this Agreement, which are considered "normal" conditions, the GAC provided under this Agreement will perform the function of adsorption of dissolved organics that contribute to taste and odors for a period of thirty-six (36) months after installation of the GAC media into the respective filters. For purposes of the warranty, effective T&O adsorption, defined as the reduction of absorbable dissolved odors, such that the threshold odor 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 exceed a level two (2) in the carbon filtered effluent for a duration of four (4) consecutive days while the treatment plant is in normal operation. The thirty-six (36) month warranty period for the GAC media installed into the filters will begin once the respective filtering unit is placed in service after backwashing following installation of the GAC media. ACS's obligation under the warranty is contingent, for the duration of the warranty period, on the following conditions within the control of KAWC:

A. If the concentration of organics in the raw water supply should exceed normal operational levels, as in the case of an accidental industrial discharge, chemical spill or other adversity, KAWC will initiate the feed of powdered activated carbon or may elect a complete bypass of contaminated water during the course of abnormal conditions. If KAWC does not immediately take emergency measures to prevent the GAC media from being exposed to excessive levels of organic contaminants, the warranty for such filters shall be null and void.

B. KAWC will continue to practice normal and customary water treatments prior to carbon filtration. These customary treatments include, without limitation, providing suitable disinfection, coagulation, and clarification of the raw water and stabilizing the clarified water to prevent the deposition of calcium carbonate scale on the media.

C. Average and maximum filtration rates will not exceed 3.0 and 4.0 gallons per minute per square foot, respectively.

D. KAWC will maintain the GAC media bed depth in each filter as close to the Noted Level as possible, with the exception of a possible loss of up to two (2) inches of GAC media bed depth per filter, per year, due to attrition losses. If losses should exceed two (2) inches of bed depth in any filter during any one (1) year of operation, KAWC shall immediately advise ACS to replace the excess GAC media loss with GAC media equal to that supplied. KAWC shall pay ACS for any such replacement of GAC media at a price agreed to by both parties. If KAWC does not immediately advise ACS to replace such loss, the warranty for the GAC media in such filter shall be null and void.

E. KAWC will maintain the water plant filters in good operating condition and in accordance with accepted industry practice. Notwithstanding the above, if the GAC media fails to perform due to encrustation by inorganic precipitates, it shall not be considered to be a breach of this warranty, but KAWC will bear the cost of cleaning, and if necessary, replacing the GAC media to restore performance,

in accordance with procedures provided by ACS.

If, during the warranty period, the GAC media fails to perform in accordance with the parameters established in this warranty and in the Agreement, subject to the conditions contained herein, ACS will, at its sole option and cost, either reactivate or replace all or part of the GAC media to restore its capability.

**EXCEPT AS SET FORTH IN THIS EXHIBIT III, ACS 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. ACS SHALL HAVE NO LIABILITY FOR ANY INDIRECT, INCIDENTAL, OR CONSEQUENTIAL DAMAGES ARISING OUT OF A BREACH OF THIS WARRANTY. KAWC'S SOLE REMEDY FOR ANY BREACH OF THIS WARRANTY SHALL BE TO REQUIRE ACS TO EITHER REACTIVATE OR REPLACE CARBON AS PROVIDED ABOVE.**

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Witness Responsible: Michael A. Miller

32. a. List and describe each service that any affiliated company renders to Kentucky-American.
- b. For each service listed above, describe the benefit(s), if any, that Kentucky-American derives from the provision of this service from the affiliate.

Response:

- a. Please refer to Exhibit 35 KAW\_APP\_EX35\_103108.pdf of the Company's filing for a comprehensive list and detailed description of services rendered to Kentucky-American by the AWWSC and ACS. Also see the testimony of Patrick Baryenbruch and Michael Miller concerning services provided by AWWSC and AWCC.
- b. **AWWSC** – As described in the testimony of Mr. Baryenbruch and Mr. Miller, the Company receives these services at or below what it could obtain those in the market. AWWSC provides the Company FTE's and expertise on a shared basis in many areas critical to the provision of water service that would not be possible to replicate in the market place or locally. Through AWWSC KAWC has available one of the premier water quality labs in the nation on an as needed basis, accounting and tax expertise, national purchasing power, water industry engineering expertise, rate expertise, finance and management expertise and many other disciplines required to provide effective water service. KAWC could not cost effectively replace these services and expertise locally. Because KAWC has these services available on a shared basis through AWWSC, it receives the services and expertise in many cases on a partial FTE basis. To duplicate those costs locally KAWC would need to attract employees with cross disciplinary skills. Such an employee would need to be proficient in both water quality and design engineering, or in water quality and finance. In fact, employees with these multiple disciplinary skills are simply not available at the local level. Over the last few years there



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has been some movement towards more sharing of resources from AWWSC versus local employees for the Company. Please see the testimony of Mr. Miller and Exhibit MAM-6, which describes the increase in Service Company charges and the net financial benefit from those transitions.

**ACS** – The carbon leases from ACS were obtained at or below market costs.

**AWCC** – See testimony of Mr. Miller and his answers to questions 13-15, which describe the benefits of utilizing AWCC to obtain the debt capital for KAWC. Also see Exhibit MAM-4 attached to Mr. Miller's testimony for a recap of the financial savings related to debt obtained from AWCC.

For the electronic version, please refer to KAW\_R\_PSCDR1#32\_111408.pdf.

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Witness Responsible: Michael A. Miller

33. Provide a comprehensive list and detailed description of the services that Kentucky-American has provided to any affiliated companies.

Response:

The Company provides work space for a number of employees on the payroll of American Water Works Service Company – Eastern Region. Office space and overheads related to the space utilized by these employees was billed to AWWSC at cost. During the twelve months ending July 2008, KAWC billed AWWSC \$17,256 for utilization of the Kentucky American office space.

For the electronic version, refer to KAW\_R\_PSCDR1#33\_111408.pdf.