

CORPORATE PROFILE

American States Water Company (NYSE:AWR) is a holding company for Southern California Water Company (SCW) and American States Utility Services, Inc. (ASUS). AWR offers long-term, income-oriented investors an attractive total return potential and has paid dividends on its Common Shares every year since 1931.

AWR's philosophy is to continue to implement long-term strategies through its subsidiaries, to increase shareholder value by earning the authorized rate of return for its utility operations, and to increase overall earnings through selective non-regulated activities.

SCW is a public utility company engaged principally in the delivery of water service. SCW operates 39 separate water systems within 75 communities in 10 counties in California and provides water service to over 1 million people, or one out of every 33 Californians. In addition, SCW provides electric service to approximately 21,000 customers. SCW focuses on customers by providing water and electric services at affordable rates approved by the California Public Utilities Commission (CPUC). SCW complies with state environmental regulations and the federal Safe Drinking Water Act. Over one-half of the water the company sells is provided from its own wells.

ASUS engages in non-regulated business activities through long-term leases or operations and maintenance contracts with municipally-owned water and wastewater systems. ASUS meets the needs and challenges facing municipalities throughout the country, by offering cost effective alternatives to higher water rates and diminishing water supplies.



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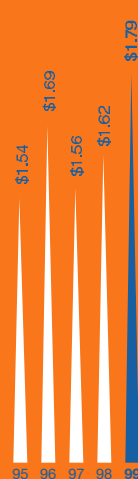
SELECTED FINANCIAL DATA

| (in thousands, except per share amounts) | 1999 | 1998 | Variance | % Change |
|--|------------|------------|-----------|----------|
| INCOME STATEMENT INFORMATION | | | | |
| Total Operating Revenues | \$ 173,421 | \$ 148,060 | \$ 25,361 | 17.13% |
| Total Operating Expenses | 144,907 | 122,999 | 21,908 | 17.81% |
| Operating Income | 28,514 | 25,061 | 3,453 | 13.78% |
| Other Income | 532 | 769 | (237) | (30.82%) |
| Interest Charges | 12,945 | 11,207 | 1,738 | 15.51% |
| Net Income | 16,101 | 14,623 | 1,478 | 10.11% |
| Preferred Dividends | 88 | 90 | (2) | (2.22%) |
| Earnings Available for Common Shareholders | 16,013 | 14,533 | 1,480 | 10.18% |
| Basic Earnings per Common Share | \$ 1.79 | \$ 1.62 | \$ 0.17 | 10.49% |
| Dividends Declared per Common Share | \$ 1.28 | \$ 1.26 | \$ 0.02 | 1.59% |
| BALANCE SHEET INFORMATION | | | | |
| Total Assets | \$ 533,181 | \$ 484,671 | \$ 48,510 | 10.01% |
| Net Utility Plant | 449,595 | 414,753 | 34,842 | 8.40% |
| Common Shareholders' Equity | 158,846 | 154,299 | 4,547 | 2.95% |
| Long-Term Debt (Net) | 167,363 | 120,809 | 46,554 | 38.54% |
| Preferred Shares | 1,600 | 1,600 | — | — |
| Preferred Shares — Subject to Mandatory Redemption | 360 | 400 | (40) | (10.00%) |
| Total Capitalization | \$ 328,169 | \$ 277,108 | \$ 51,061 | 18.43% |
| Book Value per Common Share | \$ 17.73 | \$ 17.23 | \$ 0.50 | 2.90% |
| Average Shares Outstanding | 8,958 | 8,958 | — | — |
| OTHER INFORMATION | | | | |
| Ratio of Earnings to Fixed Charges | 3.27% | 3.21% | 0.06% | 1.87% |
| Ratio of Earnings to Total Fixed Charges | 3.23% | 3.17% | 0.06% | 1.89% |
| Return on Average Common Equity | 10.2% | 9.6% | 0.60% | 6.25% |
| Cash Flow from Operations | \$ 34,913 | \$ 31,404 | \$ 3,509 | 11.17% |
| Earnings Before Interest and Taxes | 42,391 | 35,960 | 6,431 | 17.88% |
| Earnings Before Interest, Taxes, Depreciation and Amortization | \$ 56,041 | \$ 48,498 | \$ 7,543 | 15.55% |

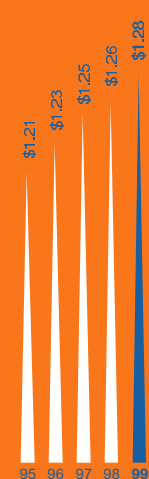
Book Value per Share
(IN DOLLARS)



Earnings per Share
(IN DOLLARS)



Dividends per Share
(IN DOLLARS)



LETTER TO SHAREHOLDERS

As American States Water Company marks the end of the 20th century, and plans for the new century, we are encouraged by the many opportunities for customers and shareholders. The water industry is changing. There is increased emphasis on quality of service and affordability, and your company is positioned to take economic advantage of these growth opportunities.

FINANCIAL RESULTS

We are pleased to report that for the year ended December 31, 1999 total earnings available for common shareholders were \$16.0 million, or \$1.79 per share, as compared to total recorded earnings last year of \$14.5 million, or \$1.62 per share. The 10.5% increase in earnings in 1999 was driven by a return to normal weather patterns and rate increases covering approximately 65% of the company's water customer base. The 1999 rate increases reflected recovery of costs associated with additional investments, designed to provide high quality service levels for customers. The company anticipates continued increases in revenues in future years from additional rate increases to recover capital costs and, to a lesser extent, increased operating expenses.

STRATEGIES FOR THE FUTURE

During 1999, the price per Common Share reached an all-time high of \$39.75. This price reflects both the improved financial performance of the company and current trends in the water utility industry, where consolidation continued at an increasing pace. Although the company's stock price, like most others in the industry, reflects some speculation about the future, your company remains solidly established as a leader within the industry with a sound and responsible business strategy. Customer base expansion, acquisitions, "beyond the meter" services, and continued capital investment for regulated and non-regulated operations drive financial growth. Your company will (i) continue to focus on core regulated operations to earn authorized returns on equity for shareholders, (ii) make acquisitions of regulated assets that complement existing operations



Floyd E. Wicks
President and Chief Executive Officer



Lloyd E. Ross
Chairman of the Board

and promote geographic and regulatory diversity, and (iii) make investments in non-regulated enterprises such as privatized municipal concessions and contract operation and maintenance services. In order to make these long-term, value-enhancing investments, these strategies may be slightly dilutive to current earnings. Management remains committed to making operational improvements to minimize this short-term impact.

WATER QUALITY-RELATED LAWSUITS

In September 1999, the Court of Appeal ordered dismissal of seven of the 11 lawsuits filed against the company. In October 1999, one group of plaintiffs appealed that decision to the California Supreme Court. On December 15, 1999, the California Supreme Court announced that it will review the appeal. Management is confident that there is no factual basis for these lawsuits against the company. However, it is impossible to predict the final decision of the courts in these matters.

YEAR 2000

Like most of the world, the changing of the century was a quiet and successful transition for customers and employees of the company. The capital investments and the hours of effort by employees have, however, better positioned the company in the event of future emergency events.

ABILITY

The word alone is strong, and as a suffix, it creates words defining strong capabilities. Sensibility, durability, affordability and accountability govern your company's ability to provide long-term, income oriented investors with an attractive total return potential and to meet the service needs of its growing customer base into the next century. We invite you to read further about the abilities of your company and thank you for your continued support.



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President and
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STRATEGY AND OPERATING REVIEW

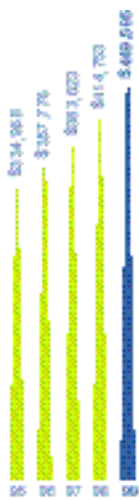
AWR's management team follows a disciplined strategy to protect and increase the value of the company, maintaining high standards on future growth in earnings. AWR is focused on core operations and value-driven acquisitions with the potential to increase shareholder returns and create a strategic match that adds to the value of services provided to current and future customers.

To promote growth, resources are directed to new markets through acquisitions—such as the small “tuck in” acquisition completed last year—and privatization of municipally-owned water, wastewater and electric assets. Although, the latter strategy is developing slowly, AWR has realigned its workforce to focus on these types of opportunities. In addition, the company continues to pursue non-regulated markets that will increase its asset base and water and electric customer base, expand geographic boundaries, and diversify operational factors such as those resulting from varying weather patterns and regulatory oversight.

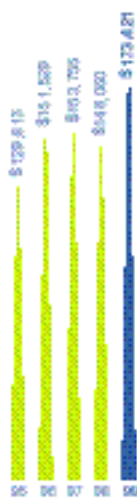
As part of the continued strategy to present AWR as a premier provider of service contracts and acquisition options, American States Utility Services, Inc. (ASUS) will be further developed as an operations and management company. The company has expanded current service contracts and developed opportunities to provide utility services such as billing, 24-hour customer service call handling, meter reading, and other field service options. ASUS is developing concession, operation and maintenance business with municipalities throughout the western United States, and within the next five years, plans to enter into longer term water transfer contracts, which will offer a potential solution to supply challenges.

Sensibility





Net Utility Plant
(IN THOUSANDS)



Total Operating Revenue
(IN THOUSANDS)

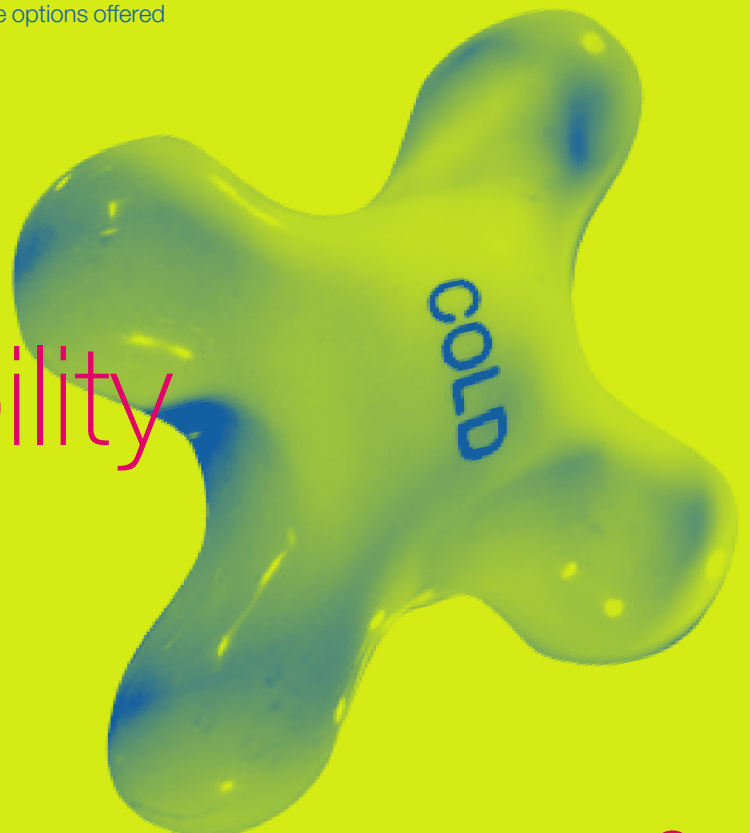
The last year of the 20th century brought significant change in the water industry as the pace of consolidations of public and private utilities throughout California, the United States and the world accelerated. In addition, deregulation of the electric industry in California continued. These changing trends in the delivery of water and electricity, and, indeed the future of the utility industry, will be driven by regulatory and infrastructure demands. These demands force companies to strive for continuous improvement in operations and efficiencies in service. American States Water Company (AWR) continues to embrace and endure change, and to be a key player in the utility industry. The company remains solidly positioned in the top ranks of the United States water utility industry.

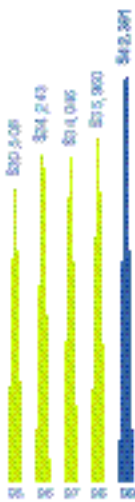
Financial strength, a committed management team, top-rated service and operational standards, and reliable supplies of quality water position AWR as a prime provider of services for water, wastewater and electric utilities faced with current and future business challenges. Beginning in 1929 and continuing through the changes of the last 70 years, AWR has successfully operated a variety of water and electric systems meeting population, supply and infrastructure, and regulatory challenges.

The company's strategy, to focus on core operations and supplement earnings through non-regulated activities in order to increase long-term value, have allowed AWR to weather the current wave of consolidations. Although recent share prices have reflected the effects of consolidations, AWR continues to grow earnings from base operations at an average rate of approximately 5% annually for the past five years. Non-regulated operations will increase this growth rate.

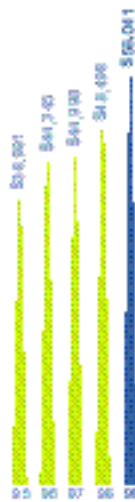
AWR has the professionalism and durability that other utility operators look for when they can no longer efficiently meet the needs of their customers. The future changes in the utility industry present extensive opportunities due to affordable options offered by AWR.

Durability

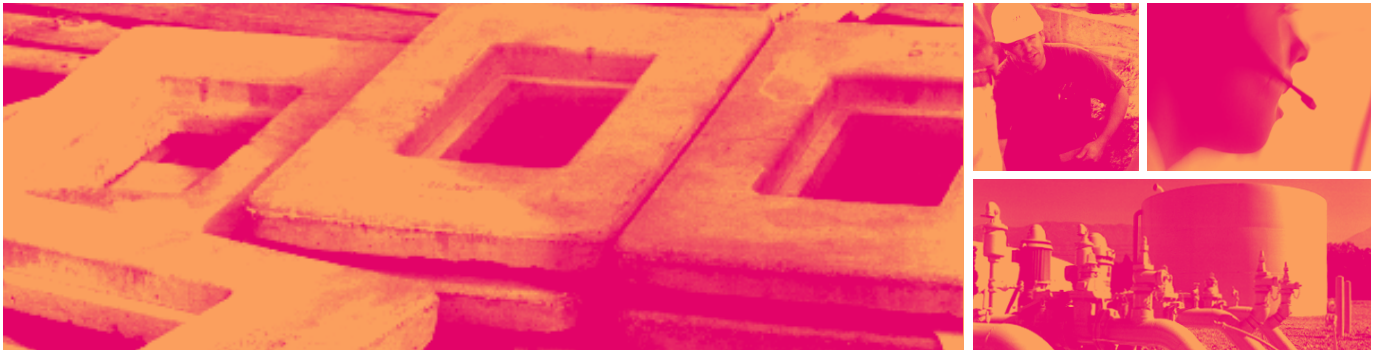




Earnings Before Interest and Taxes
(IN THOUSANDS)



Earnings Before Interest, Taxes, Depreciation and Amortization
(IN THOUSANDS)

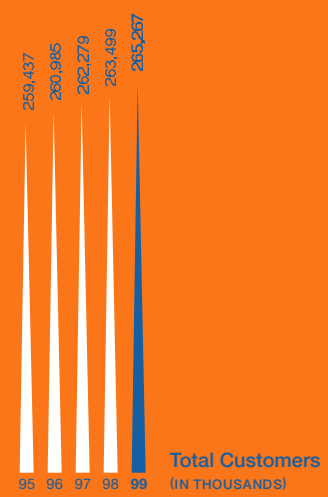


AWR's cost to serve the average residential customer for a day is approximately \$1.50, a monthly cost less than the average tank of gas for a large sport utility vehicle. This efficient cost-of-service figure is due to cost control measures currently in place, and additional improvements are planned for future years. The company's economies of scale—often not available to smaller and municipally-owned water, wastewater and electric utilities—also offers affordable options to these smaller utilities struggling to maintain regulatory compliance and preserve a high level of service to customers. That difficult equation to solve for smaller and municipally-owned utilities is a challenging situation at present, and one that will become increasingly complex in the future. AWR's status as a leader in the industry positions the company to continue to achieve higher earnings from a larger customer base while minimizing the impact on those customers.

Contributing to economies of scale and operational efficiencies, is the company's rate structure. The company's largest operating region, serving portions of the metropolitan Los Angeles area, functions under a single rate enabling the company to offer the same high quality service at a uniform price. By reducing the number of, and costs associated with, general rate case filings, the savings are passed to the customer base.

The company filed an application with the California Public Utilities Commission (CPUC) to combine tariff schedules into regional rates for the company's second largest operating region serving portions of Imperial, Orange, Riverside and Los Angeles counties. The draft decision supports the company's application. A final decision from the CPUC is anticipated in the second quarter of 2000.

In the recent general rate case submitted to the CPUC, the company is requesting regional rates for the third operation region serving customers in Northern and Central California.



Affordability



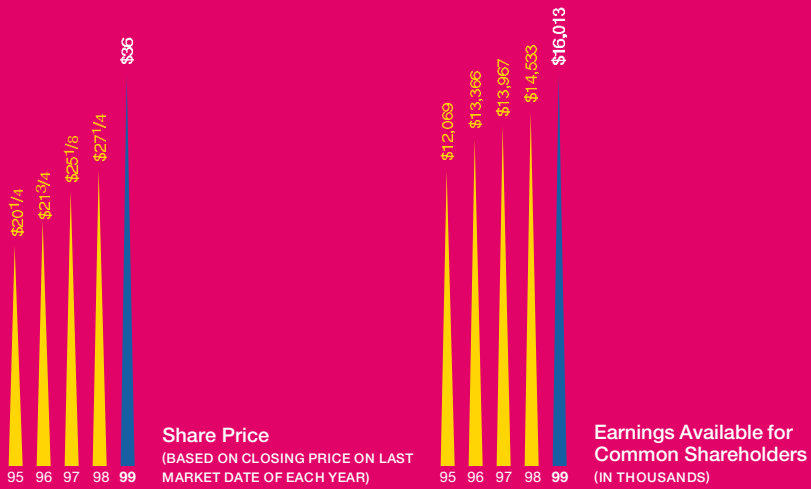
In 1999, the company continued to increase total shareholder return. In fact, \$10,000 invested in December 1994, assuming reinvestment of all dividends, would be worth \$26,917¹ at the end of 1999.

However, management will not rest on past accomplishments. As discussed earlier, consolidation in the water industry has driven up share prices considerably. Future shareholder value depends upon continued growth in earnings and dividends. Maintaining financial growth and value to shareholders is, at a minimum, achieved by earning the CPUC-authorized rate of return on equity in recently filed rate cases and generation of additional revenues through non-regulated opportunities. This balance was met in 1999, and the company's disciplined strategy is structured to maintain this balance in future years.

Drivers of AWR's future financial growth include customer base expansion, investment in capital improvements and replacements, and the pursuit of acquisitions and non-regulated activities. The company has extensive experience and proven success in all of these areas and will aggressively pursue value-driven opportunities.

Strong heritage and endurance, combined with the disciplined strategy to offer investors value and to meet the service needs of a growing customer base, demonstrate that AWR is the company reflecting the needs of a new age.

¹Past performance is no guarantee of future results. Share values and returns fluctuate and gain or loss may occur when shares are sold.



Accountability

MANAGEMENT'S DISCUSSION AND ANALYSIS

American States Water Company (AWR) is the parent company of Southern California Water Company (SCW) and American States Utility Services, Inc. (ASUS). SCW is a public utility engaged principally in the purchase, distribution and sale of water as well as in the distribution of electricity in several mountain communities. SCW is regulated by the California Public Utilities Commission (CPUC) as to its water and electric business including properties, rates, services, facilities and other matters. ASUS performs water and energy related services and operations. AWR and ASUS are not regulated by the CPUC. Unless specifically noted, the following discussion and analysis provides information on the company's consolidated operations and assets.

FORWARD-LOOKING INFORMATION

Certain matters discussed in this report (including the documents incorporated herein by reference) are forward-looking statements intended to qualify for the "safe harbor" from liability established by the Private Securities Litigation Reform Act of 1995. These forward-looking statements can generally be identified as such because the context of the statement will include words such as the company "believes," "anticipates," "expects" or words of similar import. Similarly, statements that describe the company's future plans, objectives, estimates or goals are also forward-looking statements. Such statements address future events and conditions concerning capital expenditures, earnings, litigation, rates, water quality and other regulatory matters, adequacy of water supplies, liquidity and capital resources, opportunities related to operations of municipally-owned water systems and accounting matters. Actual results in each case could differ materially from those currently anticipated in such statements, by reason of factors such as utility restructuring, including ongoing local, state and federal activities; future economic conditions, including changes in customer demand; future climatic conditions; legislative, regulatory and other circumstances affecting anticipated revenues and costs.

RESULTS OF OPERATIONS

Years Ended December 31, 1999 and 1998

Basic earnings per Common Share in 1999 increased by 10.5% to \$1.79 per share as compared to \$1.62 per share for the comparable period last year. The increase in the recorded

results primarily reflects higher revenues at the SCW unit during 1999 as is more fully discussed below.

Water operating revenues increased by 18.5% in 1999 to \$159.7 million from the \$134.8 million reported in 1998. Water sales volumes in 1999 were 9.0% higher than last year due primarily to the much drier and warmer weather conditions throughout Southern California in 1999. Additional increases in revenues were due to the general rate increases in six of the company's customer service areas (CSA) effective January 1, 1999, which were applicable to 65% of SCW's water customers.

Electric operating revenues of \$13.3 million were 1.0% higher in 1999 as compared to last year due to a 2.7% increase in kilowatt-hour sales, primarily by industrial power users. The sales increase was partially offset by the lower billing rates of industrial customers relative to residential customers.

Other revenues increased from \$65,000 to \$390,000 in 1999 due to increased management fees resulting from new ASUS service contracts established in the year and increased activities with existing contracts.

Purchased water costs in 1999 increased to \$36.1 million as compared to \$30.8 million in 1998 due to a 12.1% increase in volumes purchased. The increase also reflects reduced reimbursements in 1999 from potentially responsible parties related to groundwater contamination in SCW's Culver City CSA of approximately \$570,000, compared with reimbursements of \$1.7 million in 1998.

Costs of power purchased for pumping increased by 5.5% to \$7.4 million in 1999 chiefly as a result of an increase in pumped groundwater in SCW's water supply mix due to increased sales volumes.

Costs of power purchased for resale in 1999 increased by 42.0% to \$7.1 million from the \$5.0 million recorded in 1998 due primarily to additional energy demand charges from the energy supplier serving SCW's Bear Valley Electric Service unit in 1999. As discussed below, most of this increase has been included in the supply cost balancing account and will have to be recovered in future rate increases.

Groundwater production assessments decreased by 5.3% to \$7.2 million in 1999 from \$7.6 million in 1998 due to reduced quantity rates in SCW's Metropolitan and San Dimas CSAs.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

A positive entry for the provision for supply cost balancing accounts reflects recovery of previously under-collected supply costs. Conversely, a negative entry for the provision for supply cost balancing accounts reflects an under-collection of previously incurred supply costs. In 1999, recovery of previously under-collected supply costs was lower than 1998 due to the previously discussed increase in energy demand charges, the effect of which was partially offset by new rates effective January 1999 authorized to implement new supply costs and to increase collection of previously under-collected costs.

The balancing account mechanism insulates earnings from changes in the unit cost of supply costs which are outside of the immediate control of the company. However, the balancing account is not designed to insulate earnings against changes in the actual supply mix as compared to that mix authorized for recovery in rates. In 1999, SCW's overall supply mix improved favorably over that mix authorized in rates resulting in additional income. There is no assurance that the favorable mix can be sustained in future periods since actual results are affected by availability and quality of water, both purchased and produced from SCW's wells. See the section titled "Water Supply."

Other operating expenses increased by 7.8% from the \$14.5 million recorded in 1998 due to increased costs for water treatment, and a higher uncollectible provisions as a result of increased revenues.

Administrative and general expenses increased by 30.0% to \$28.6 million in 1999 from the \$22.0 million recorded in 1998. The increase is due to costs associated with various acquisition projects, increased employee benefit costs, and additional amounts reserved for certain legal proceedings.

In 1999, maintenance expense increased to the \$9.8 million level compared to the recorded \$7.3 million in 1998 due principally to increased maintenance on the company's water supply sources, and costs incurred on main replacements. The wet weather conditions during the first part of 1998 also hampered planned maintenance activities, thereby reducing maintenance expense last year.

Depreciation expense in 1999 increased by 8.9% to \$13.7 million reflecting the effects of recording approximately \$38.2 million in net plant additions during 1998, depreciation on which began in 1999.

Taxes on income increased by approximately 31.7% to \$13.3 million in 1999 as compared to the \$10.1 million last

year due to a 24.5% increase in pre-tax income and a higher effective tax rate in 1999 resulting from the turn-around of depreciation-related temporary differences, the benefits of which were previously flowed-through for ratemaking purposes.

Property and other taxes increased by 7.2% in 1999 to \$6.6 million due primarily to increased franchise fees resulting from higher revenues, and increased payroll taxes from higher wages and additional personnel.

Other income decreased by 30.8% in 1999 due primarily to the flow-through of tax benefits related to refinancing of long-term debt in December 1998 for which there were no similar benefits in 1999.

Interest expense increased by 15.5% to \$12.9 million primarily due to the issuance of \$40 million in long-term debt in January 1999, partially offset by the retirement of \$10 million of 10.10% Notes in December 1998.

Years Ended December 31, 1998 and 1997

Basic earnings per Common Share in 1998 increased by 3.8% to \$1.62 per share as compared to \$1.56 per share in 1997. Although wet weather significantly impacted revenues in 1998, lower supply costs and modest increases in other operating expenses partially offset the decline in revenues.

Water operating revenues decreased by 4.3% in 1998 to \$134.9 million from the \$141.0 million reported in 1997. Water sales volumes in 1998 were 9.9% lower than 1997 due to extremely wet weather during the first half of the year. The decrease in sales was partially offset by rate increases effective during 1998.

Electric operating revenues of \$13.2 million were 3.4% higher in 1998 as compared to 1997 due to the impact of a general rate increase effective January 1998, as well as a 2.0% increase in kilowatt-hour sales.

Purchased water costs decreased in 1998 to \$30.8 million as compared to \$38.3 million in 1997 due to a 20.8% decrease in volumes purchased and refunds received from the company's wholesale water supplier during 1998 of approximately \$1.4 million. Refunds of \$2.0 million were received in 1997.

Costs of power purchased for pumping decreased by 7.2% to \$7.0 million in 1998 chiefly as a result of reduced energy costs from the company's suppliers.

Costs of power purchased for resale in 1998 decreased by 3.4% to \$5.0 million from the \$5.2 million recorded in 1997

due to reduced costs from the company's energy providers offset by the effects of increased kilowatt-hour sales volumes recorded during the year.

Groundwater production assessments increased by 10.5% to \$7.6 million in 1998 from \$6.8 million in 1997 due to the increased amounts of pumped water in the company's supply mix as well as additional assessments associated with increased pumping in the company's Metropolitan and Orange County CSAs.

A positive entry for the provision for supply cost balancing accounts reflects recovery of previously under-collected supply costs. Conversely, a negative entry for the provision for supply cost balancing accounts reflects an under-collection of previously incurred supply costs. In 1998, recovery of previously under-collected supply costs was lower than 1997 due to the expiration, in January 1998, of a surcharge designed to recover those costs. The new rates, effective January 1999, increased collection of these under-collected costs. The balancing account mechanism insulates earnings from changes in the unit cost of supply costs which are outside of the immediate control of the company. However, the balancing account is not designed to insulate earnings against changes in supply mix, as occurred during the first eight months of 1997.

Other operating expenses increased by 10.6% from the \$13.1 million recorded in 1997 due to employee time charged to this category. Reversals in 1997 of costs associated with recovery of water quality expenditures through the CPUC's memorandum account mechanism also contributed to the increase. There were no such reversals of equal magnitude in 1998.

Administrative and general expenses decreased slightly by 0.7% to \$22.0 million in 1998 from the \$22.1 million recorded in 1997. The decrease is due to stability in costs associated with health insurance, post-retirement medical benefits, pension and 401(k) plan costs and to a reduction of time charged by employees to this category.

In 1998, maintenance expense remained at approximately the \$7.3 million level recorded in 1997 due principally to the wet weather conditions during the first part of 1998 that hampered planned maintenance activity.

Depreciation expense in 1998 increased by 14.5% to \$12.5 million reflecting the effects of recording approximately \$38 million in net plant additions during 1997, depreciation on which began in 1998. In addition, amortization of start-up and

organizational costs associated with the formation of AWR is reflected in 1998 and there were no similar amortization costs in 1997.

Taxes on income increased by approximately 3.1% to \$10.1 million in 1998 as compared to the \$9.8 million in 1997 due to a 5.7% increase in operating income partially offset by a lower effective tax rate.

Property and other taxes decreased by 2.5% in 1998 to \$6.1 million due primarily to reduced franchise tax payments directly attributable to reduced revenues.

Other income increased by 1.5% in 1998 due principally to the flow-through of tax benefits related to refinancing of long-term debt which was partially offset by an increase in reserves against costs associated with the company's non-regulated joint venture.

Interest expense increased by 10.3% to \$11.2 million primarily due to increased short-term bank borrowing and the issuance of \$15 million in long-term debt in March 1998.

LIQUIDITY AND CAPITAL RESOURCES

AWR funds its operating expenses, dividends on its outstanding Common and Preferred Shares, and makes its mandatory sinking fund payments, principally through dividends from SCW. AWR has filed a Registration Statement with the Securities and Exchange Commission (SEC) for issuance, from time to time, of up to \$60 million in Common Shares, Preferred Shares and/or debt securities. The proceeds will be used primarily for investment in its subsidiaries. No securities have been issued under this Registration Statement as of December 31, 1999.

SCW funds the majority of its operating expenses, interest payments on its debt, and dividends on its outstanding Common Shares through internal sources. SCW continues to rely on external sources, including short-term bank borrowing, contributions-in-aid-of-construction, advances for construction and install-and-convey advances, to fund the majority of its construction expenditures.

Because of the seasonal nature of its water and electric operations, SCW utilizes its short-term borrowing capacity to finance current operating expenses. The aggregate short-term borrowing capacity available to SCW under its three bank lines of credit was \$47 million as of December 31, 1999, of which a total of \$21 million was outstanding. SCW routinely employs short-term bank borrowing as an interim financing source prior to funding capital expenditures on a long-term basis.

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

In 1998, SCW filed a Registration Statement with the SEC for issuance, from time to time, of up to \$60 million in long-term debt. In January 1999, SCW issued \$40 million of long-term debt pursuant to this Registration Statement, leaving \$20 million for issuance at a later date. The funds were used primarily to repay short-term bank borrowings, after which capital expenditures were funded.

The company has no derivative financial instruments, financial instruments with significant off-balance sheet risks or financial instruments with concentrations of credit risk.

CONSTRUCTION PROGRAM

SCW's construction program is designed to ensure its customers' high quality service. A program for water pipeline replacement is on-going throughout the 22 CSAs, based on priority of leaks detected, fire protection enhancements and reflection of the underlying replacement schedule. In addition, general upgrades in SCW's water supply facilities are anticipated to be on-going. SCW's board of directors has approved anticipated net capital expenditures of \$55.4 million in 2000. Neither AWR nor ASUS currently have material capital requirements.

REGULATORY MATTERS

SCW is subject to regulation by the CPUC, which has broad powers with respect to service and facilities, rates, classifications of accounts, valuation of properties, the purchase, disposition and mortgaging of properties necessary or useful in rendering public utility service, the issuance of securities, the granting of certificates of convenience and necessity as to the extension of services and facilities and various other matters. AWR and ASUS are not regulated by the CPUC. The CPUC does, however, regulate certain transactions between SCW and its non-regulated affiliates.

The 22 CSAs of SCW are grouped into 16 water districts and one electric district for ratemaking purposes. Water rates vary among the 16 ratemaking districts due to differences in operating conditions and costs. SCW monitors operations on a regional basis in each of these districts so that applications for rate changes may be filed, when warranted. Under the CPUC's practices, rates may be increased by three methods: general rate case increases (GRC), offsets for certain expense increases and advice letter filings related to certain plant additions. GRCs are typically for three-year periods, which include step increases for the second and third year. Rates are

based on a forecast of expenses and capital costs. GRCs have a typical regulatory lag of one year. Offset rate increases typically have a two to four month regulatory lag.

New water rates for six of SCW's customer service areas and recovery of costs associated with SCW's general office functions were implemented in January 1999. Step increases in rates for Arden-Cordova, Bay Point and Los Osos CSAs were also effective in January 1999.

Applications to increase water rates were filed for four water ratemaking districts in SCW's Region III in March 1999. A draft decision has been issued by the Administrative Law Judge assigned to this matter that supports the settlement on all issues reached between SCW and the CPUC staff. SCW has also filed an application with the CPUC to combine tariff schedules into regional rates for the CSAs that make up SCW's Region III. The Administrative Law Judge assigned to this matter has issued a draft decision that supports SCW's application. A final decision from the CPUC on both issues is anticipated in the second quarter of 2000.

The GRC step increase for the Metropolitan CSA and the General Office Allocation step increases for Simi Valley, Arden-Cordova, Santa Maria and Bay Point CSAs were effective beginning January 2000. Attrition increases for Arden-Cordova and Bay Point CSAs were effective beginning January 2000.

In March 1998, the CPUC issued an Order Instituting Investigation (OII) to regulated water utilities in California, including SCW. The purpose of the OII is to determine whether existing standards and policies regarding drinking water quality adequately protect the public health and whether those standards and policies are being uniformly complied with by those water utilities. The OII delineates the constitutional and statutory jurisdiction of the CPUC and the California Department of Health Services (DOHS) in establishing and enforcing adherence to water quality standards. The CPUC's jurisdiction provides for the establishment of rates, which permit water utilities to provide water service meeting the established water quality standards at prices which are both affordable and allow the utility to earn a reasonable return on its investment. SCW has provided its response to a series of questions dealing with the adequacy of current drinking water standards, compliance by water utilities with such standards, appropriate remedies for failure to comply with drinking water standards and whether increased enforcement and additional drinking water standards are necessary. The Administrative

Law Judge assigned to the OII has issued a draft decision finding that water utilities, including SCW, have complied with DOHS regulations and requirements. SCW is unable to predict whether the draft decision will be approved in part or in its entirety. SCW anticipates a final decision by the CPUC on this matter in 2000.

On April 22, 1999, the CPUC issued an order denying SCW's application seeking approval of its recovery through rates of costs associated with its participation in the Coastal Aqueduct Extension of the State Water Project (SWP). SCW's participation in the SWP commits it to a 40-year entitlement with a value of approximately \$9.5 million. SCW's investment in SWP is currently included in Other Property and Investments. The remaining balance of the related liability of approximately \$7 million is recorded as other long-term debt. SCW intends to recover its investment in SWP through contributions from developers on a per-lot or other basis, and, failing that, sale of its 500 acre-foot entitlement in SWP. SCW believes that its full investment and on-going costs associated with its ownership will be fully recovered.

ENVIRONMENTAL MATTERS

The 1996 amendments to the Safe Drinking Water Act (SDWA) revised the 1986 amendments to the SDWA with a new process for selecting and regulating contaminants. The Environmental Protection Agency (EPA) can only regulate contaminants that may have adverse health effects, which are known or are likely to occur at levels of public health concern, and, if regulated, the regulation would provide "a meaningful opportunity for health risk reduction." The EPA has published a list of contaminants for possible regulation and must update that list every five years. In addition, every five years, the EPA must select at least five contaminants on that list and determine whether to regulate them. The new law allows the EPA to bypass the selection process and adopt interim regulations for contaminants in order to address urgent health threats. Current regulations, however, remain in place and are not subject to the new standard-setting provisions. The DOHS, acting on behalf of the EPA, administers the EPA's program in California.

The 1996 SDWA amendments allow the EPA, for the first time, to base primary drinking water regulations on risk assessment and cost/benefit considerations and on minimizing overall risk. The EPA must base regulations on the best available, peer-reviewed science and data from best

available methods. For proposed regulations that involve the setting of maximum contaminant levels (MCLs), the EPA must use, and seek public comment on, an analysis of quantifiable and non-quantifiable risk-reduction benefits and cost for each MCL.

SCW currently tests its wells and water systems according to requirements listed in the SDWA. Water from wells found to contain levels of contaminants above the established MCLs is treated before it is delivered to customers.

Since the SDWA became effective, SCW has experienced increased operating costs for testing to determine the levels, if any, of the constituents in SCW's sources of supply and additional expense to lower the level of any such contaminants in order to meet the MCLs. Such costs and the costs of controlling any other contaminants may cause SCW to experience additional capital costs and increased operating costs. The ratemaking process provides SCW with the opportunity to recover prudently incurred capital and operating costs associated with water quality.

There have been no environmental matters that have materially affected or are currently materially affecting SCW's Bear Valley Electric Service CSA. The construction of a proposed 115kv line to serve the Bear Valley Electric Service CSA is subject to an Environmental Impact Study (EIS). Delays in approval of the EIS could impact service in the area. SCW has, however, taken other measures, including some measures that will be enacted on an emergency basis, to meet load growth and mitigate delay in approval of the EIS.

WATER SUPPLY

During 1999, the company supplied a total of 195,886 acre feet of water. Of this amount, approximately 58.2% came from pumped sources and 40.2% was purchased from others, principally the Metropolitan Water District of Southern California (MWD). The remaining amount was supplied by the Bureau of Reclamation (the Bureau) under a no-cost contract. During 1998, the company supplied 179,927 acre feet of water, 60.7% of which came from pumped sources, 39.0% was purchased and the remainder was supplied by the Bureau.

The MWD is a water district organized under the laws of the State of California for the purpose of delivering imported water to areas within its jurisdiction. The company has 52 connections to the water distribution facilities of MWD and

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

other municipal water agencies. MWD imports water from two principal sources: the Colorado River and the State Water Project (SWP). Available water supplies from the Colorado River and the SWP have historically been sufficient to meet most of MWD's requirements and MWD's supplies from these sources are anticipated to remain adequate through 2000. MWD's import of water from the Colorado River is expected to decrease in future years due to the requirements of the Central Arizona Project. In response, MWD has taken a number of steps to secure additional storage capacity and to increase available water supplies by effecting transfers of water rights from other sources.

The company's water supply and revenues are significantly affected by changes in meteorological conditions. Water sales volumes have been impacted during the last two years by the El Nino/La Nina Southern Oscillation phenomena. El Nino brings substantial rainfall to Southern California and the opposite, La Nina, often means diminished rainfall. During the '80s and '90s, El Nino increased precipitation as much as 250% of normal for some SCW service areas, while La Nina decreased rain levels 30% to 50% of normal.

In 1999, after the 1997-1998 El Nino heavy rain season, La Nina moved rainfall to the north and substantially reduced rainfall in SCW's service areas with some systems experiencing less than 32% of normal rainfall.

In spite of the anticipated La Nina conditions, the 2000 water year supply outlook remains adequate to meet SCW's needs. As of January 2000, California reservoirs stand at 125% of average. This positive outlook is due to the fact that reservoirs are still holding some of the El Nino surplus and groundwater levels are usually not diminished by a single year of below normal precipitation. Although overall groundwater conditions remain at adequate levels, certain of SCW's groundwater supplies have been affected to varying degrees by various forms of contamination which, in some cases, have caused increased reliance on purchased water in its supply mix.

WATER-RELATED OPPORTUNITIES

In late 1998, ASUS was formed to pursue opportunities such as long-term leases, and operation and maintenance contracts of government or municipally-owned water and wastewater systems. Privatization opportunities in California have been few to date and ASUS has focused its efforts on service contracts with municipalities and others in order to build long-term relationships.

YEAR 2000 READINESS

The company has no Y2K incidents, business disruptions, failures or legal proceedings to report. There were no actual or anticipated effects or changes to the company's operating trends or revenue patterns as a result of the transition from December 1999 to January 2000.

SCW formally announced its 100% Y2K Ready status when it filed its compliance report with the CPUC on November 1, 1999. The company's general process for addressing the Y2K issue was (i) to inventory all systems that may have a potential Y2K impact, (ii) to determine the materiality of these non-Y2K ready systems, (iii) to replace and test, correct and test, or prepare for the failure of material items that have been determined to be non-Y2K ready, and (iv) to prepare contingency plans, which included, among other things, increased staffing during critical periods, manual back-up for automated systems and the use of portable generators capable of providing power during a black-out.

Not all Y2K problems were necessarily expected to surface in early 2000. The company does not have, and may never fully have, sufficient information about the Y2K exposure of third parties to adequately predict the risks posed by them to the company. If the third parties later discover any Y2K problems that are not remedied, resulting problems could include loss of utility services and disruption of water supplies.

Costs incurred to address Y2K issues are estimated to be \$7.5 million. The company has incurred \$4.8 million in costs associated with Y2K readiness at January 2000, \$4.0 million of which is in capital investments. The company believes that these capital expenditures as well as the remaining Y2K-related investments will generally be recovered through rates. See Note 13 — Year 2000 Readiness Update for additional information.

ACCOUNTING STANDARDS

In June 1998, the FASB issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," which establishes a new model for accounting for derivative and hedging activities, and supersedes and amends a number of existing standards. Adoption of this statement, with an extended effective date for fiscal years beginning after December 15, 1999, will not have a significant impact on financial position or results of operation.

CONSOLIDATED BALANCE SHEETS

| (in thousands) | December 31, | |
|---|-------------------|-------------------|
| | 1999 | 1998 |
| ASSETS | | |
| UTILITY PLANT, AT COST | | |
| Water | \$ 532,007 | \$ 482,989 |
| Electric | 36,349 | 35,171 |
| | <u>568,356</u> | <u>518,160</u> |
| Less — Accumulated depreciation | (151,733) | (138,423) |
| | <u>416,623</u> | <u>379,737</u> |
| Construction work in progress | 32,972 | 35,016 |
| Net utility plant | <u>449,595</u> | <u>414,753</u> |
| OTHER PROPERTY AND INVESTMENTS | <u>10,583</u> | <u>1,077</u> |
| CURRENT ASSETS | | |
| Cash and cash equivalents | 2,189 | 620 |
| Accounts receivable — Customers, less reserves of \$487 in 1999 ; \$403 in 1998 | 10,135 | 7,626 |
| Other accounts receivable | 4,347 | 5,301 |
| Unbilled revenue | 11,345 | 9,303 |
| Materials and supplies, at average cost | 1,153 | 994 |
| Supply cost balancing accounts | 4,774 | 4,300 |
| Prepayments | 4,851 | 5,988 |
| Accumulated deferred income taxes — net | 5,546 | 5,156 |
| Total current assets | <u>44,340</u> | <u>39,288</u> |
| DEFERRED CHARGES | | |
| Unamortized debt expense and redemption premium | 6,811 | 6,635 |
| Regulatory tax-related assets | 19,941 | 21,506 |
| Other | 1,911 | 1,412 |
| Total deferred charges | <u>28,663</u> | <u>29,553</u> |
| TOTAL ASSETS | <u>\$ 533,181</u> | <u>\$ 484,671</u> |
| CAPITALIZATION AND LIABILITIES | | |
| CAPITALIZATION | | |
| Common Shareholders' equity | \$ 158,846 | \$ 154,299 |
| Preferred Shares | 1,600 | 1,600 |
| Preferred Shares — mandatory redemption | 360 | 400 |
| Long-term debt | 167,363 | 120,809 |
| Total capitalization | <u>328,169</u> | <u>277,108</u> |
| CURRENT LIABILITIES | | |
| Notes payable to banks | 21,000 | 38,000 |
| Long-term debt and Preferred Shares — current | 340 | 260 |
| Accounts payable | 13,777 | 10,218 |
| Taxes payable | 5,432 | 5,900 |
| Accrued interest | 1,584 | 1,405 |
| Other | 12,832 | 7,985 |
| Total current liabilities | <u>54,965</u> | <u>63,768</u> |
| OTHER CREDITS | | |
| Advances for construction | 57,485 | 54,743 |
| Contributions in aid of construction | 38,895 | 36,530 |
| Accumulated deferred income taxes — net | 48,302 | 46,902 |
| Unamortized investment tax credits | 3,064 | 3,155 |
| Regulatory tax-related liability | 1,861 | 1,906 |
| Other | 440 | 559 |
| Total other credits | <u>150,047</u> | <u>143,795</u> |
| TOTAL CAPITALIZATION AND LIABILITIES | <u>\$ 533,181</u> | <u>\$ 484,671</u> |

The accompanying notes are an integral part of these financial statements

CONSOLIDATED STATEMENTS OF CAPITALIZATION

| (in thousands) | December 31, | |
|--|-------------------|-------------------|
| | 1999 | 1998 |
| COMMON SHAREHOLDERS' EQUITY: | | |
| Common Shares, \$2.50 stated value — | | |
| Authorized 30,000,000 shares | | |
| Outstanding 8,957,671 in 1999 and 1998 | \$ 22,394 | \$ 22,394 |
| Additional paid-in capital | 74,937 | 74,937 |
| Earnings reinvested in the business | 61,515 | 56,968 |
| | <u>158,846</u> | <u>154,299</u> |
| PREFERRED SHARES: \$25 PAR VALUE | | |
| Authorized 64,000 shares | | |
| Outstanding 32,000 shares, 4% Series | 800 | 800 |
| Outstanding 32,000 shares, 4 1/4 % Series | 800 | 800 |
| | <u>1,600</u> | <u>1,600</u> |
| PREFERRED SHARES SUBJECT TO MANDATORY REDEMPTION | | |
| Requirements: \$25 par value | | |
| Authorized and outstanding 16,000 shares in 1999 and 17,600 shares in 1998, 5% Series | 400 | 440 |
| Less: Preferred Shares to be redeemed within one year | (40) | (40) |
| | <u>360</u> | <u>400</u> |
| LONG-TERM DEBT | | |
| 5.82% notes due 2003 | 12,500 | 12,500 |
| 6.64% notes due 2013 | 1,100 | 1,100 |
| 6.80% notes due 2013 | 2,000 | 2,000 |
| 8.50% fixed rate obligation due 2013 | 1,798 | 1,882 |
| Variable rate obligation due 2014 | 6,000 | 6,000 |
| Variable rate obligation due 2018 | 650 | 630 |
| 6.87% notes due 2023 | 5,000 | 5,000 |
| 7.00% notes due 2023 | 10,000 | 10,000 |
| 7.55% notes due 2025 | 8,000 | 8,000 |
| 7.65% notes due 2025 | 22,000 | 22,000 |
| 5.50% notes due 2026 | 8,000 | 8,000 |
| 6.81% notes due 2028 | 15,000 | 15,000 |
| 6.59% notes due 2029 | 40,000 | — |
| 9.56% notes due 2031 | 28,000 | 28,000 |
| State Water Project due 2035 | 7,028 | — |
| Other | 587 | 917 |
| | <u>167,663</u> | <u>121,029</u> |
| Less: Current maturities | (300) | (220) |
| | <u>167,363</u> | <u>120,809</u> |
| TOTAL CAPITALIZATION | <u>\$ 328,169</u> | <u>\$ 277,108</u> |

The accompanying notes are an integral part of these financial statements

CONSOLIDATED STATEMENTS OF INCOME

| (in thousands, except per share amounts) | For the years ended December 31, | | |
|---|----------------------------------|------------------|------------------|
| | 1999 | 1998 | 1997 |
| OPERATING REVENUES | | | |
| Water | \$ 159,693 | \$ 134,794 | \$ 140,988 |
| Electric | 13,338 | 13,201 | 12,767 |
| Other | 390 | 65 | — |
| Total operating revenues | <u>173,421</u> | <u>148,060</u> | <u>153,755</u> |
| OPERATING EXPENSES | | | |
| Water purchased | 36,143 | 30,833 | 38,318 |
| Power purchased for resale | 7,119 | 5,013 | 5,188 |
| Power purchased for pumping | 7,394 | 7,009 | 7,554 |
| Groundwater production assessment | 7,170 | 7,567 | 6,847 |
| Supply cost balancing accounts | (473) | 28 | 2,813 |
| Other operating expenses | 15,594 | 14,459 | 13,074 |
| Administrative and general expenses | 28,600 | 21,987 | 22,138 |
| Depreciation and amortization | 13,650 | 12,538 | 10,952 |
| Maintenance | 9,799 | 7,311 | 7,301 |
| Taxes on income | 13,345 | 10,130 | 9,830 |
| Property and other taxes | 6,566 | 6,124 | 6,282 |
| Total operating expenses | <u>144,907</u> | <u>122,999</u> | <u>130,297</u> |
| OPERATING INCOME | <u>28,514</u> | <u>25,061</u> | <u>23,458</u> |
| OTHER INCOME | | | |
| Total other income — net | 532 | 769 | 758 |
| Income before interest charges | <u>29,046</u> | <u>25,830</u> | <u>24,216</u> |
| INTEREST CHARGES | | | |
| Interest on long-term debt | 11,294 | 9,612 | 8,821 |
| Other interest and amortization of debt expense | 1,651 | 1,595 | 1,336 |
| Total interest charges | <u>12,945</u> | <u>11,207</u> | <u>10,157</u> |
| NET INCOME | <u>16,101</u> | <u>14,623</u> | <u>14,059</u> |
| Dividends on Preferred Shares | (88) | (90) | (92) |
| EARNINGS AVAILABLE FOR COMMON SHAREHOLDERS | <u>\$ 16,013</u> | <u>\$ 14,533</u> | <u>\$ 13,967</u> |
| BASIC EARNINGS PER COMMON SHARE | <u>\$ 1.79</u> | <u>\$ 1.62</u> | <u>\$ 1.56</u> |
| WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING | <u>8,958</u> | <u>8,958</u> | <u>8,957</u> |

The accompanying notes are an integral part of these financial statements

CONSOLIDATED STATEMENTS OF CHANGES IN COMMON SHAREHOLDERS' EQUITY

| (in thousands) | Common Shares | | Additional Paid-in Capital | Earnings Reinvested in the Business |
|--|---------------------|------------------|----------------------------------|---|
| | Number of Shares | Amount | | |
| BALANCES AT DECEMBER 31, 1996 | 8,886 | \$ 22,215 | \$ 73,645 | \$ 50,906 |
| Add: | | | | |
| Net Income | | | | 14,059 |
| Issuance of Common Shares for public offering | 72 | 179 | 1,292 | |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 92 |
| Dividends on Common Shares — \$1.245 per share | | | | 11,151 |
| BALANCES AT DECEMBER 31, 1997 | 8,958 | \$ 22,394 | \$ 74,937 | \$ 53,722 |
| Add: | | | | |
| Net Income | | | | 14,623 |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 90 |
| Dividends on Common Shares — \$1.26 per share | | | | 11,287 |
| BALANCES AT DECEMBER 31, 1998 | 8,958 | \$ 22,394 | \$ 74,937 | \$ 56,968 |
| Add: | | | | |
| Net Income | | | | 16,101 |
| Deduct: | | | | |
| Dividends on Preferred Shares | | | | 88 |
| Dividends on Common Shares — \$1.28 per share | | | | 11,466 |
| BALANCES AT DECEMBER 31, 1999 | 8,958 | \$ 22,394 | \$ 74,937 | \$ 61,515 |

The accompanying notes are an integral part of these financial statements

CONSOLIDATED STATEMENTS OF CASH FLOWS

| (in thousands) | For the years ended December 31, | | |
|---|----------------------------------|-----------------|-----------------|
| | 1999 | 1998 | 1997 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | |
| Net income | \$ 16,101 | \$ 14,623 | \$ 14,059 |
| Adjustments for non-cash items: | | | |
| Depreciation and amortization | 14,364 | 15,368 | 11,170 |
| Deferred income taxes and investment tax credits | 2,440 | 5,241 | 826 |
| Other – net | 1,066 | 1,394 | 873 |
| Changes in assets and liabilities: | | | |
| Customer receivables | (1,555) | 918 | (673) |
| Supply cost balancing accounts | (474) | (14) | 1,987 |
| Accounts payable | 3,559 | (1,552) | (1,095) |
| Taxes payable | (468) | (3,215) | 3,338 |
| Other – net | 3,977 | 438 | 341 |
| Net cash provided | <u>39,010</u> | <u>33,201</u> | <u>30,826</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | | |
| Construction expenditures | <u>(57,823)</u> | <u>(43,623)</u> | <u>(36,799)</u> |
| Net cash used | <u>(57,823)</u> | <u>(43,623)</u> | <u>(36,799)</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | | |
| Issuance of Common Shares | — | — | 1,472 |
| Issuance of long-term debt and lease obligations | 47,028 | 15,000 | 8,000 |
| Receipt of advances for and contributions in aid of construction | 5,300 | 3,381 | 1,302 |
| Refunds on advances for construction | (2,957) | (2,651) | (2,957) |
| Retirement or repayments of long-term debt and redemption of Preferred Shares — net | (435) | (9,488) | (198) |
| Net change in notes payable to banks | (17,000) | 12,000 | 10,000 |
| Common and Preferred dividends paid | (11,554) | (11,386) | (11,243) |
| Net cash provided | <u>20,382</u> | <u>6,856</u> | <u>6,376</u> |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | 1,569 | (3,566) | 403 |
| CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR | 620 | 4,186 | 3,783 |
| CASH AND CASH EQUIVALENTS, END OF YEAR | \$ 2,189 | \$ 620 | \$ 4,186 |
| TAXES AND INTEREST PAID: | | | |
| Income taxes paid | \$ 12,137 | \$ 5,430 | \$ 6,338 |
| Interest paid | 11,834 | 11,391 | 9,451 |
| NON-CASH TRANSACTIONS: | | | |
| Property installed by developers and conveyed to company | \$ 4,096 | \$ 1,797 | \$ 2,082 |

The accompanying notes are an integral part of these financial statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

American States Water Company (AWR) is the parent company of Southern California Water Company (SCW) and American States Utility Services, Inc. (ASUS). SCW is a public utility engaged principally in the purchase, production, distribution and sale of water as well as in the distribution of electricity in several mountain communities. SCW is regulated by the California Public Utilities Commission (CPUC) as to its water and electric business including properties, rates, services, facilities and other matters. ASUS performs non-regulated, water related services and operations on a contract basis. The consolidated financial statements include the accounts of AWR, SCW and ASUS. Virtually all of AWR's assets and revenues are those of SCW.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements include the accounts of AWR and its wholly-owned subsidiaries, SCW and ASUS, collectively referred to as the company. Inter-company transactions and balances have been eliminated.

The accounting records for SCW are maintained in accordance with the Uniform System of Accounts prescribed by the CPUC. The preparation of these financial statements required the use of certain estimates by management in determining the company's assets, liabilities, revenues and expenses.

Property and Depreciation: The company capitalizes, as utility plant, the cost of additions and replacements of retirement units. Such cost includes labor, material and certain indirect charges. Depreciation is computed on the straight-line, remaining-life basis. For the years 1999, 1998 and 1997 the aggregate provisions for depreciation approximated 2.91%, 2.79%, and 2.77% of the beginning of the year depreciable plant, respectively.

Interest: Interest is generally not capitalized for financial reporting purposes as such procedure is usually not followed for rate-making purposes.

Revenues: Revenues include amounts billed to customers and an amount of unbilled revenue representing amounts to be billed for usage from the last meter reading date to the end of the accounting period.

Basic Earnings Per Common Share: Basic Earnings per Common Share are based upon the weighted average number of Common Shares outstanding and net income after deducting preferred dividend requirements. There are no dilutive securities. Accordingly, diluted earnings per share is not calculated.

Supply Cost Balancing Accounts: As permitted by the CPUC, the company maintains water and electric supply cost balancing accounts to account for under-collections and over-collections of revenues designed to recover such costs. Recoverability of such costs is recorded in income and charged to balancing accounts when such costs are incurred. The balancing accounts are reversed when such costs are recovered through rate adjustments. The company accrues interest on its supply cost balancing accounts at the rate prevailing for 90-day commercial paper.

Debt Issue Expense and Redemption Premiums: Original debt issue expenses are amortized over the lives of the respective issues. Premiums paid on the early redemption of debt which is reacquired through refunding are deferred and amortized over the life of the debt issued to finance the refunding. The redemption premium on debt reacquired without refunding is amortized over the remaining period the debt would have been outstanding.

Other Credits: Advances for construction represent amounts advanced by developers which are generally refundable at either a rate of 22% of the revenue received from the installations for which funds were advanced or in equal annual installments over a 40-year period. Contributions-in-aid-of-construction are similar to advances, but require no refunding and are amortized over the useful lives of the related property.

Cash and Cash Equivalents: For purposes of the Statements of Cash Flows, cash and cash equivalents include short-term cash investments with an original maturity of three months or less.

Financial Instrument Risk: The company does not carry any financial instruments with off-balance sheet risk nor do its operations result in concentrations of credit risk.

Fair Value of Financial Instruments: The table below estimates the fair value of each represented class of financial instrument. For cash and cash equivalents, accounts receivable and short-term debt, the carrying amount is used. Otherwise, rates available to the company at December 31, 1999 and 1998 for debt with similar terms and remaining maturities were used to estimate fair value for long-term debt. Changes in the assumptions will produce differing results.

| (in thousands) | 1999 | | 1998 | |
|------------------------|-----------------|------------|-----------------|------------|
| | Carrying amount | Fair value | Carrying amount | Fair value |
| Financial assets: | | | | |
| Cash | \$ 2,189 | \$ 2,189 | \$ 620 | \$ 620 |
| Accounts receivable | 25,827 | 25,827 | 22,230 | 22,230 |
| Financial liabilities: | | | | |
| Short-term debt | \$ 21,000 | \$ 21,000 | \$ 38,000 | \$ 38,000 |
| Long-term debt | 167,663 | 161,843 | 120,809 | 135,092 |

NOTE 2: CAPITAL STOCK

All of the series of Preferred Shares outstanding at December 31, 1999 are redeemable at the option of the company. At December 31, 1999, the redemption price per share for each series of \$25 Preferred Shares was \$27.00, \$26.50 and \$25.25 for the 4%, 4 1/4% and 5% Series, respectively. To each of the redemption prices must be added accrued and unpaid dividends to the redemption date.

The \$25 Preferred Shares, 5% Series, are subject to mandatory redemption provisions of 1,600 shares per year. The annual aggregate mandatory redemption requirements for this Series for the five years subsequent to December 31, 1999 is \$40,000 each year.

In 1996, the company issued 1,000,000 Common Shares through a secondary public offering. In January 1997, the company issued 71,500 Common Shares through a secondary public offering. The net proceeds from this sale were used to repay a portion of short-term debt then outstanding.

For the years ended December 31, 1999, December 31, 1998 and December 31, 1997, all shares issued under the company's Common Share Purchase and Dividend Reinvestment Plan (DRP) and the 401(k) Plan were purchased on the open market. There are 500,000 and 571,408 Common Shares reserved for issuance under the DRP and the 401(k) Plan, respectively, at December 31, 1999. Shares

reserved for the 401(k) Plan are in relation to company matching contributions and for investment purposes by participants.

As of December 31, 1999 there were no retained earnings restricted under any of the company's debt instruments, as to the payment of cash dividends on Common Shares.

In 1998, the board of directors adopted a Shareholder Rights Plan (Rights Plan) and authorized a dividend distribution of one right (a Right) to purchase 1/1000th of a Junior Participating Preferred Share for each outstanding Common Share. The Rights Plan became effective in September 1998 and will expire in September 2008. The Rights Plan is designed to provide shareholders' protection and to maximize shareholder value by encouraging a prospective acquirer to negotiate with the board.

Each Right represents a right to purchase 1/1000th of a Junior Participating Preferred Share at the price of \$120, subject to adjustment (the Purchase Price). Each Junior Participating Preferred Share is entitled to receive a dividend equal to 1000 times any dividend paid on each Common Share and 100 votes per share in any shareholder election. The Rights become exercisable upon occurrence of a Distribution Date. A Distribution Date event occurs if (i) any person accumulates 15% of the then outstanding Common Shares, (ii) any person presents a tender offer which caused the person's ownership level to exceed 15% and the board determines the tender offer not to be fair to AWR's shareholders, or (iii) the board determines that a shareholder maintaining a 15% interest in the Common Shares could have an adverse impact on AWR or could attempt to pressure AWR to repurchase the holder's shares at a premium.

Until the occurrence of a Distribution Date, each Right trades with the Common Share and is not separately transferable. When a Distribution Date occurs, AWR would distribute separately Rights Certificates to Common Shareholders and the Rights would subsequently trade separate from the Common Shares and each holder of a Right, other than the acquiring person whose Rights will thereafter be void, will have the right to receive upon exercise at its then current Purchase Price that number of Common Shares having a market value of two times the Purchase Price of the Right. If AWR merges into the acquiring person or enters

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

into any transaction that unfairly favors the acquiring person or disfavors AWR's other shareholders, the Right becomes a right to purchase Common Shares of the acquiring person having market value of two times the Purchase Price.

The board of directors may determine that in certain circumstances a proposal which would cause a Distribution Date is in the best interest of AWR's shareholders. Therefore, the board of directors may, at its option, redeem the Rights at a redemption price of \$0.01 per Right.

NOTE 3: COMPENSATING BALANCES AND BANK DEBT

At December 31, 1999, SCW maintained \$47 million in aggregate borrowing capacity with three commercial banks with no compensating balances required. Of this amount, \$21 million was outstanding at year-end. Loans can be obtained at the option of SCW and bear interest at rates based on floating prime borrowing rates or at money market rates.

Short-term borrowing activities for the last three years were as follows:

| (in thousands, except percent) | December 31, | | |
|--------------------------------|------------------|-----------|-----------|
| | 1999 | 1998 | 1997 |
| Balance outstanding at | | | |
| December 31, | \$ 21,000 | \$ 38,000 | \$ 26,000 |
| Interest rate at December 31, | 7.35% | 5.86% | 6.39% |
| Average amount outstanding | \$ 8,775 | \$ 19,309 | \$ 15,678 |
| Weighted average | | | |
| annual interest rate | 5.11% | 6.78% | 6.27% |
| Maximum amount | | | |
| outstanding | \$ 21,000 | \$ 39,000 | \$ 32,000 |

NOTE 4: LONG-TERM DEBT

In March 1998, SCW sold the remaining \$15 million under its Series B Medium Term Note Program and in December 1998, SCW redeemed all of its outstanding 10.10% Notes. In January 1999, \$40 million of Series C Medium Term Notes were sold. The funds were used initially to repay short-term bank borrowings and, after that, to fund construction expenditures. The company has no mortgage debt, and leases and other similar financial arrangements are not material.

SCW has posted an Irrevocable Letter of Credit, which expires July 31, 2000, in the amount of \$646,631 as security for its self-insured workers' compensation plan. SCW has also provided an Irrevocable Letter of Credit, which expires November 14, 2000, in the amount of \$6,296,000 to a trustee with respect to the variable rate obligation issued by the Three Valleys Municipal Water District.

Annual maturities of all long-term debt, including capitalized leases, amount to \$303,356, \$231,559, \$246,528, \$262,036 and \$278,644 for the five years ending December 31, 2000 through 2004, respectively.

NOTE 5: TAXES ON INCOME

The company provides deferred income taxes for temporary differences under Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" (SFAS No. 109), for certain transactions which are recognized for income tax purposes in a period different from that in which they are reported in the financial statements. The most significant items are the tax effects of accelerated depreciation, the supply cost balancing accounts and advances for and contributions-in-aid-of-construction. SFAS No. 109 also requires that rate-regulated enterprises record deferred income taxes for temporary differences accorded flow-through treatment at the direction of a regulatory commission. The resulting deferred tax assets and liabilities are recorded at the expected cash flow to be reflected in future rates. Since the CPUC has consistently permitted the recovery of previously flowed-through tax effects, SCW has established regulatory liabilities and assets offsetting such deferred tax assets and liabilities.

Deferred investment tax credits are being amortized to other income ratably over the lives of the property giving rise to the credits.

The significant components of deferred tax assets and deferred tax liabilities, as reflected in the balance sheets, and the accumulated net deferred income tax liabilities at December 31, 1999 and 1998 were:

| (in thousands) | December 31, | |
|---|-----------------|-----------------|
| | 1999 | 1998 |
| Deferred tax assets: | | |
| Balancing accounts | \$ (175) | \$ 33 |
| State tax effect | 5,721 | 5,123 |
| | <u>5,546</u> | <u>5,156</u> |
| Deferred tax liabilities | | |
| Depreciation | (44,939) | (43,442) |
| Advances and contributions | 15,862 | 16,694 |
| Other property related | (10,007) | (11,488) |
| Other non-property related | (9,218) | (8,666) |
| | <u>(48,302)</u> | <u>(46,902)</u> |
| Accumulated deferred income taxes — net | \$ (42,756) | \$ (41,746) |

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

| (in thousands) | December 31, | | |
|--|---------------|--------------|---------------|
| | 1999 | 1998 | 1997 |
| Current | | | |
| Federal | \$ 9,360 | \$ 5,219 | \$ 7,205 |
| State | 2,799 | 1,727 | 2,287 |
| Total current tax expense | <u>12,159</u> | <u>6,946</u> | <u>9,492</u> |
| Deferred — Federal and State: | | | |
| Accelerated depreciation | 3,405 | 3,319 | 2,996 |
| Balancing accounts | (207) | 6 | (871) |
| Advances and contributions | — | — | (210) |
| California privilege year franchise tax | (970) | (544) | (617) |
| Other | (664) | (398) | (566) |
| Total deferred tax expense | <u>1,564</u> | <u>2,383</u> | <u>732</u> |
| Total income tax expense | <u>13,723</u> | <u>9,329</u> | <u>10,224</u> |
| Income taxes included in operating expenses | 13,345 | 10,130 | 9,830 |
| Income taxes included in other income and expenses — net | 378 | (801) | 394 |
| Total income tax expense | \$ 13,723 | \$ 9,329 | \$ 10,224 |

Additional information regarding taxes on income is set forth in the following table:

| (in thousands, except percent) | December 31, | | |
|--|--------------|--------------|--------------|
| | 1999 | 1998 | 1997 |
| Federal taxes on pre-tax income at statutory rates | \$ 10,438 | \$ 8,470 | \$ 8,451 |
| Increase (decrease) in taxes resulting from: | | | |
| State income tax expense | 2,605 | 1,654 | 1,864 |
| Depreciation | 1,184 | 944 | 853 |
| Federal benefit of state taxes | (912) | (579) | (652) |
| Adjustments to prior years' provisions | 433 | (97) | (143) |
| Payment of premium on redemption | 66 | (813) | — |
| Other — net | (91) | (250) | (149) |
| Total income tax expense | \$ 13,723 | \$ 9,329 | \$ 10,224 |
| Pre-tax income | \$ 29,824 | \$ 23,952 | \$ 24,145 |
| Effective income tax rate | <u>46.0%</u> | <u>38.9%</u> | <u>42.3%</u> |

NOTE 6: EMPLOYEE BENEFIT PLANS

The company maintains a pension plan (the Plan) which provides eligible employees (those age 21 and older, with one year of service) monthly benefits upon retirement based on average salaries and length of service. The normal retirement benefit is equal to 2% of the five highest consecutive years average earnings multiplied by the number of years of credited service, up to a maximum of 40 years, reduced by a percentage of primary social security benefits. There is also an early retirement option. Annual contributions are made to the Plan which comply with the funding requirements of the Employee Retirement Income Security Act (ERISA). At December 31, 1999, the company had 713 participants in the Plan, 54 of these are employees covered by collective bargaining agreements, the earliest of which expires in 2001.

The company also provides all active employees medical, dental and vision care benefits through a medical insurance plan. Eligible employees who retired prior to age 65, and/or their spouses, were able to retain the benefits under the active plan until reaching age 65. Eligible employees, upon reaching age 65, and those employees retiring at or after age 65, and/or their spouses, receive coverage through a Medicare supplemental insurance policy paid for by the company subject to an annual cap limit.

The CPUC has issued a decision which provides for the recovery in rates of tax-deductible contributions made to a separately trusteed fund. In accordance with that decision,

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

SCW established two separate trusts in 1995, one for those retirees who were subject to a collective bargaining agreement and another for all other retirees. The company's funding policy is to contribute annually an amount at least equal to the revenues authorized to be collected through rates for post-retirement benefit costs. Post-retirement benefit costs for 1993, 1994 and 1995 were estimated at a total of \$1.6 million and have been recorded as a regulatory asset for recovery over a 20 year period. The unamortized balance at December 31, 1999 was approximately \$610,000.

The following table sets forth the Plan's funded status and amounts recognized in the company's balance sheets and the components of net pension cost and accrued post-retirement liability at December 31, 1999 and 1998:

| (in thousands) | Pension Benefits | | Other Benefits | |
|--|------------------|-----------|----------------|------------|
| | 1999 | 1998 | 1999 | 1998 |
| Change in Benefit Obligation: | | | | |
| Benefit obligation at beginning of year | \$ 38,572 | \$ 33,410 | \$ 4,363 | \$ 4,503 |
| Service cost | 1,963 | 1,597 | 125 | 112 |
| Interest cost | 2,538 | 2,278 | 305 | 283 |
| Actuarial loss/(gain) | (6,255) | 2,514 | (171) | (368) |
| Benefits paid | (1,305) | (1,227) | (191) | (167) |
| Benefit obligation at end of year | \$ 35,513 | \$ 38,572 | \$ 4,431 | \$ 4,363 |
| Changes in Plan Assets: | | | | |
| Fair value of plan assets at beginning of year | \$ 39,541 | \$ 33,433 | \$ 1,442 | \$ 1,104 |
| Actual return of plan assets | 8,277 | 6,051 | 25 | 44 |
| Employer contributions | 1,264 | 1,284 | 484 | 461 |
| Benefits paid | (1,306) | (1,227) | (191) | (167) |
| Fair value of plan assets at end of year | \$ 47,776 | \$ 39,541 | \$ 1,760 | \$ 1,442 |
| Reconciliation of Funded Status: | | | | |
| Funded status | \$ 12,263 | \$ 969 | \$ (2,671) | \$ (2,921) |
| Unrecognized transition obligation | 57 | 114 | 6,288 | 6,707 |
| Unrecognized net loss/(gain) | (10,683) | 677 | (1,869) | (1,860) |
| Unrecognized prior service cost | 355 | 400 | (3,228) | (3,427) |
| Prepaid/(accrued) pension cost | \$ 1,992 | \$ 2,160 | \$ (1,480) | \$ (1,501) |
| Weighted-Average Assumptions as of December 31: | | | | |
| Discount rate | 7.75% | 6.50% | 7.75% | 6.50% |
| Long-term rate of return | 8.00% | 8.00% | 8.00% | 8.00% |
| Salary assumption | 4.00% | 4.00% | — | — |

A sliding scale for assumed health care cost increases was used for both periods, starting at 8% in 1999 and then remaining at 6% thereafter.

The components of net periodic post-retirement benefits costs for 1999 and 1998 are as follows:

| (in thousands) | Pension Benefits | | Other Benefits | |
|---|------------------|----------|----------------|--------|
| | 1999 | 1998 | 1999 | 1998 |
| Components of Net Periodic Benefits Cost | | | | |
| Service cost | \$ 1,963 | \$ 1,597 | \$ 125 | \$ 112 |
| Interest cost | 2,538 | 2,278 | 305 | 283 |
| Actual return on plan assets | (8,277) | (6,051) | (25) | (44) |
| Net amortization | 5,207 | 3,476 | 58 | 67 |
| Net periodic pension cost | \$ 1,431 | \$ 1,300 | \$ 463 | \$ 418 |

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects:

| (in thousands) | 1-Percentage-Point Increase | 1-Percentage-Point Decrease |
|---|-----------------------------|-----------------------------|
| Effect on total of service and interest cost components | \$ 13 | \$ (12) |
| Effect on postretirement benefit obligation | \$ 177 | \$ (156) |

The company has a 401(k) Investment Incentive Program under which employees may invest a percentage of their pay, up to a maximum investment prescribed by law, in an investment program managed by an outside investment manager. Company contributions to the 401(k) are based upon a percentage of individual employee contributions and, for 1999, 1998 and 1997, totaled \$920,340, \$874,113, and \$785,687, respectively.

NOTE 7: BUSINESS RISKS AND CONCENTRATION OF SALES

The company's utility operations are engaged in supplying water and electric service to the public. SCW is required to provide service and grant credit to customers within its defined service areas. Although the company has a diversified base of residential, industrial and other customers, revenues derived from commercial and residential water customers accounted for approximately 90% of total water revenues in 1999 and 91%

in 1998. The company faces additional risks associated with weather conditions, adequacy and quality of water supplies, regulatory decisions, pronouncements and laws, water-related litigation, general business conditions and condemnation.

Approximately 40% of the SCW's water supply is purchased from wholesalers of imported water, with the remainder produced from company wells. The long-term availability of imported water supplies is dependent upon, among other things, drought conditions throughout the state, increases in population, water quality standards and legislation that may potentially reduce water supplies. SCW does not anticipate any constraints on its imported water supplies in 2000.

NOTE 8: CONTINGENCIES

In 1998, ASUS was formed to pursue non-regulated opportunities such as long-term leases, and operation and maintenance contracts of governmentally-owned water and wastewater systems. In 1999, the company terminated its Golden State Water Company joint venture. The company expensed approximately \$336,000 against future losses and capital account adjustments in 1998. There was no significant financial impact in 1999 associated with the termination.

On April 22, 1999, the CPUC issued an order denying SCW's application seeking approval of its recovery through rates of costs associated with its participation in the Coastal Aqueduct Extension of the State Water Project (SWP). SCW's participation in the SWP commits it to a 40-year entitlement with a value of approximately \$9.5 million. SCW's investment in SWP is currently included in Other Property and Investments. The remaining balance of the related liability of approximately \$7 million is recorded as other long-term debt. SCW intends to recover its investment in SWP through contributions from developers on a per-lot or other basis, and, failing that, sale of its 500 acre-foot entitlement in SWP. SCW believes that its full investment and on-going costs associated with its ownership will be fully recovered.

SCW has been named as a defendant in 11 lawsuits which allege that SCW delivered contaminated water to its customers. Plaintiffs in these actions seek damages, including general, special, and punitive damages, according to proof of trial, as well as attorney's fees on certain causes of action, costs of suit, and other unspecified relief. Nine of the lawsuits involve CSAs located in Los Angeles county in the southern

portion of California; two of the lawsuits involve a CSA located in Sacramento county in Northern California. On September 1, 1999, the Court of Appeal in San Francisco held that the CPUC had preemptive jurisdiction over regulated public utilities and ordered dismissal of a series of lawsuits pertaining to water quality filed against water utilities, including SCW. Seven out of 11 lawsuits against SCW had been ordered for dismissal by the state Court of Appeal. On October 11, 1999, one group of plaintiffs appealed the decision to the California Supreme Court which has accepted the case. Management is unable to predict the outcome of this proceeding but, in any event, does not anticipate a decision prior to 2001.

In light of the breadth of plaintiff's claims, the lack of factual information regarding plaintiff's claims and injuries, if any, the fact that no discovery has yet been completed, SCW is unable to determine at this time what, if any, potential liability it may have with respect to these claims. SCW intends to vigorously defend itself against these allegations. Management can not predict the outcome of these proceedings and if SCW is found liable, SCW would pursue recovery through its insurance coverage providers.

In response to those lawsuits and similar actions, in March 1998 the CPUC issued an Order Instituting Investigation (OII) directed to all Class A and B water utilities in California, including SCW, into whether existing standards and policies regarding drinking water quality adequately protect the public health and whether those standards and policies are being uniformly complied with by those water utilities. The OII notes the constitutional and statutory jurisdiction of the CPUC and the DOHS to establish and enforce adherence to water quality standards for water delivered by utilities to their customers and, in the case of the CPUC, to establish rates which permit water utilities to furnish water that meets the established water quality standards at prices which are both affordable and that allow the utility to earn a reasonable return on its investment. SCW has made its filing in this proceeding on a series of questions dealing with current drinking water standards, compliance by water utilities with such standards, appropriate remedies for failure to comply with drinking water standards and whether stricter or additional drinking water standards are required. The Water Division of the CPUC has issued its report based on these filings by the utilities. A final decision in the OII is anticipated in 2000. The OII leaves open the possibility of evidentiary hearings and further action by the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

CPUC. The Administrative Law Judge assigned to the OII has issued a draft decision finding that water utilities, including SCW, have complied with DOHS regulations and requirements. SCW is unable to predict whether the draft decision will be approved in part or in its entirety by the CPUC.

Management believes that proper insurance coverage and reserves are in place to insure against anticipated property, general liability and workers' compensation claims.

NOTE 9: CONSTRUCTION PROGRAM

SCW's 2000 construction budget provides for gross expenditures of approximately \$59 million, \$3.6 million of which is anticipated to be obtained from developers and others. AWR and ASUS have no material capital expenditure programs.

NOTE 10: ALLOWANCE FOR DOUBTFUL ACCOUNTS

The table below presents SCW's provision for doubtful accounts charged to expense and accounts written off, net of recoveries for the last three years.

| (in thousands) | December 31, | | |
|--|--------------|--------|--------|
| | 1999 | 1998 | 1997 |
| Balance at beginning of year | \$ 403 | \$ 466 | \$ 387 |
| Provision charged to expense | 852 | 631 | 707 |
| Accounts written off, net of recoveries | (768) | (694) | (628) |
| Balance at end of year | \$ 487 | \$ 403 | \$ 466 |

Neither AWR nor ASUS have established any provision for doubtful accounts.

NOTE 11: BUSINESS SEGMENTS

The company has two principal business units: a water and electric distribution unit through its SCW subsidiary, and a non-regulated activity unit through the ASUS subsidiary. All activities currently are geographically located within California, except for one contract providing customer service and billing services to a utility located in Arizona. SCW is a regulated utility which operates both water and electric systems. AWR has no material operations other than its SCW subsidiary. On a stand alone basis, AWR has no material assets other than its investments in its subsidiaries. The tables below set forth information relating to SCW's operating segments. SCW manages its operations on a regional basis using the five categories below as broad-level measures of profitability. Included in the amounts set forth, certain assets have been allocated. The identifiable assets are net of respective accumulated provisions for depreciation.

| (in thousands) | Year Ended December 31, 1999 | | | |
|---|------------------------------|-----------|------------|-----------|
| | Water | | | |
| | Region I | Region II | Region III | Electric |
| Operating revenues | \$ 27,221 | \$ 70,770 | \$ 61,692 | \$ 13,348 |
| Operating income before income taxes | 6,567 | 15,841 | 16,022 | 3,821 |
| Identifiable assets | 108,675 | 140,175 | 177,457 | 25,725 |
| Depreciation expense | 2,736 | 4,041 | 5,395 | 1,344 |
| Capital additions | \$ 12,966 | \$ 21,926 | \$ 14,513 | \$ 2,173 |

| (in thousands) | Year Ended December 31, 1998 | | | |
|---|------------------------------|-----------|------------|-----------|
| | Water | | | |
| | Region I | Region II | Region III | Electric |
| Operating revenues | \$ 24,927 | \$ 57,273 | \$ 52,582 | \$ 13,211 |
| Operating income before income taxes | 6,799 | 11,732 | 13,143 | 3,847 |
| Identifiable assets | 97,463 | 123,044 | 169,264 | 24,981 |
| Depreciation expense | 2,551 | 3,378 | 4,701 | 1,640 |
| Capital additions | \$ 13,302 | \$ 14,452 | \$ 15,795 | \$ 1,720 |

| (in thousands) | Year Ended December 31, 1997 | | | |
|---|------------------------------|-----------|------------|-----------|
| | Water | | | |
| | Region I | Region II | Region III | Electric |
| Operating revenues | \$ 24,340 | \$ 61,085 | \$ 55,551 | \$ 12,779 |
| Operating income before income taxes | 5,897 | 9,593 | 13,709 | 4,089 |
| Identifiable assets | 87,039 | 112,556 | 158,934 | 25,095 |
| Depreciation expense | 2,306 | 3,042 | 4,604 | 1,001 |
| Capital additions | \$ 10,007 | \$ 15,431 | \$ 11,671 | \$ 2,116 |

NOTE 12: SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

The quarterly financial information presented below is unaudited. The business of the company is of a seasonal nature and it is management's opinion that comparisons of earnings for the quarter periods do not reflect overall trends and changes in the company's operations.

| (in thousands, except per share amounts) | Operating Revenues | | Operating Income | | Net Income | | Earnings per Share | |
|--|--------------------|------------|------------------|-----------|------------|-----------|--------------------|---------|
| | 1999 | 1998 | 1999 | 1998 | 1999 | 1998 | 1999 | 1998 |
| First quarter | \$ 36,132 | \$ 29,955 | \$ 5,854 | \$ 4,382 | \$ 2,977 | \$ 1,843 | \$ 0.33 | \$ 0.20 |
| Second quarter | 42,116 | 35,001 | 7,251 | 5,586 | 4,406 | 2,767 | 0.49 | 0.31 |
| Third quarter | 51,597 | 47,002 | 10,266 | 9,432 | 6,690 | 6,374 | 0.74 | 0.71 |
| Fourth quarter | 43,576 | 36,102 | 5,143 | 5,661 | 2,028 | 3,639 | 0.23 | 0.40 |
| Total year | \$ 173,421 | \$ 148,060 | \$ 28,514 | \$ 25,061 | \$ 16,101 | \$ 14,623 | \$ 1.79 | \$ 1.62 |

NOTE 13: YEAR 2000 READINESS UPDATE

The company has no Y2K incidents, business disruptions, failures or legal proceedings to report. There were no effects or changes to the company's operating trends or revenue patterns as a result of the millennium turnover.

SCW formally announced its 100% Y2K Ready status when it filed its compliance report with the CPUC on November 1, 1999. SCW will be submitting the last CPUC report on this issue by March 1, 2000.

The company's general process for addressing the Y2K issue was (i) to inventory all systems that may have a potential Y2K impact, (ii) to determine the materiality of these non-Y2K ready systems, (iii) to replace and test, correct and test, or prepare for the failure of material items that have been determined to be non-Y2K ready, and (iv) to prepare contingency plans.

The company is significantly dependent on third party suppliers, such as energy and telecommunication companies and wholesale water suppliers. In order to conduct its business, the company initiated due diligence with certain of its major service providers to address their Y2K readiness. In the event that such suppliers might be adversely affected by Y2K, the company prepared its contingency plan which included, among other things, increased staffing during critical periods, manual back-up for automated systems and the use of portable generators capable of providing power during a black-out. Several "dry runs" were exercised in 1999, which simulated Y2K situations that implemented the company's contingency plan. The dry runs proved to be effective exercises that identified areas of strength and weakness, and provided real-life experience from which to make informed decisions about Y2K preparation and contingency planning.

Not all Y2K problems were necessarily expected to surface in early 2000. The company does not have, and may never fully have, sufficient information about the Y2K exposure of these third parties to adequately predict the risks posed by them to the company. If the third parties later discover any Y2K problems that are not remedied, resulting problems could include loss of utility services and disruption of water supplies.

On September 2, 1999, the CPUC issued an order denying regulated water utilities the authority to create memorandum accounts for Y2K expenses. The order, however, provides that after January 1, 2000, regulated water utilities may file for recovery of capital investment, not otherwise included in current rates, associated with Y2K mitigation efforts. Y2K final expenditures have been estimated at approximately \$7.5 million. The company has spent \$4.8 million at January 2000, \$4.0 million of which is in capital investments. The company believes that these capital expenditures as well as the remaining Y2K-related investments will generally be recovered through rates.

REPORT OF MANAGEMENT

The consolidated financial statements contained in this annual report were prepared by the management of American States Water Company, which is responsible for their integrity and objectivity. The consolidated financial statements were prepared in accordance with generally accepted accounting principles and include, where necessary, amounts based upon management's best estimates and judgments. All other financial information in the annual report is consistent with the consolidated financial statements and is also the responsibility of management.

The company maintains systems of internal control which are designed to help safeguard the assets of the company and provide reasonable assurance that accounting and financial records can be relied upon to generate accurate financial statements. These systems include the hiring and training of qualified personnel, appropriate segregation of duties, delegation of authority and an internal audit function which has reporting responsibility to the Audit Committee of the board of directors.

The Audit Committee, composed of three outside directors, exercises oversight of management's discharge of its responsibilities regarding the systems of internal control and financial reporting. The committee periodically meets with management, the internal auditor and the independent accountants to review the work and findings of each. The committee also reviews the qualifications of, and recommends to the board of directors, a firm of independent accountants.

The independent accountants, Arthur Andersen LLP, have performed an audit of the consolidated financial statements in accordance with generally accepted auditing standards. Their audit gave consideration to the company's system of internal accounting control as a basis for establishing the nature, timing and scope of their work. The result of their work is expressed in their Report of Independent Public Accountants.



Floyd E. Wicks
President, Chief Executive Officer



McClellan Harris III
Chief Financial Officer, Vice President — Finance,
Treasurer and Corporate Secretary

February 10, 2000

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Shareholders and the Board of Directors of
American States Water Company:

We have audited the consolidated balance sheets and consolidated statements of capitalization of American States Water Company (a California corporation) as of December 31, 1999 and 1998 and the related consolidated statements of income, changes in common shareholders' equity and cash flows for each of the three years in the period ended December 31, 1999. These consolidated financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of American States Water Company as of December 31, 1999 and 1998, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 1999, in conformity with accounting principles generally accepted in the United States.



Arthur Andersen LLP
Los Angeles, California

February 10, 2000

SHAREHOLDER INFORMATION

ANNUAL MEETING OF SHAREHOLDERS

All shareholders are invited to attend the Annual Meeting of Shareholders which will be held on Tuesday, May 2, 2000, beginning at 9:00 am, at the Industry Hills Sheraton, One Industry Hills Parkway, City of Industry, California 91744. Notice of meeting and proxy materials will be mailed.

STOCK LISTING

Common Shares of American States Water Company are traded on the New York Stock Exchange under the symbol AWR. The high and low NYSE prices and the dividends paid on the Common Shares for the past two years were:

| | | High | Low | Dividends Paid |
|----------------|----|--------------------------------|------------------------------------|----------------|
| 1999 | | | | |
| First quarter | \$ | 30 | \$ 23 ⁹ / ₁₆ | \$ 0.32 |
| Second quarter | | 29 ¹ / ₄ | 22 ³ / ₁₆ | 0.32 |
| Third quarter | | 37 ¹ / ₈ | 28 ³ / ₈ | 0.32 |
| Fourth quarter | | 39 ³ / ₄ | 31 ³ / ₄ | 0.32 |
| | | | | \$ 1.28 |
| 1998 | | | | |
| First quarter | \$ | 26 | \$ 23 ¹ / ₁₆ | \$ 0.315 |
| Second quarter | | 27 ¹ / ₈ | 21 ¹ / ₈ | 0.315 |
| Third quarter | | 27 | 23 ¹ / ₄ | 0.315 |
| Fourth quarter | | 29 ¹ / ₄ | 24 ⁷ / ₈ | 0.315 |
| | | | | \$ 1.260 |

INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Arthur Andersen LLP
633 West Fifth Street
Los Angeles, CA 90071

CORPORATE REPORTS

Shareholders with questions, or who wish to obtain a copy of the company's reports to the Securities and Exchange Commission without charge, should contact:

American States Water Company
Attn: Corporate Secretary
630 East Foothill Boulevard
San Dimas, CA 91773
Phone: (909) 394-3600
Fax: (909) 394-1382

SHAREHOLDER ASSISTANCE

Shareholders with questions about replacement of dividend checks, transferring stock, replacing lost or stolen certificates or other matters related to their ownership of stock, should contact:

ChaseMellon Shareholder Services, L.L.C.
Overpeck Centre
85 Challenger Road
Ridgefield Park, NJ 07660
(888) 816-6998
<http://shrrelations@chasmellon.com>

COMMON SHARE PURCHASE AND DIVIDEND REINVESTMENT PLAN

The company has a Common Shares Purchase and Dividend Reinvestment Plan that is sponsored and administered by The Chase Manhattan Bank. The Plan provides a simple and cost-effective method for current and potential shareholders to build ownership in the company through the direct purchase of Common Shares from the company and the reinvestment of their cash dividends. A Prospectus and enrollment form may be obtained from ChaseMellon Shareholder Services, L.L.C. at (800) 842-7629 or from the company at (877) 463-6297 (INFOAWR).

2000 DIVIDEND SCHEDULE

The following schedule shows the anticipated Common and Preferred Share record and payment dates for 2000:

| Record Dates | Payment Dates |
|--------------|---------------|
| February 7 | March 1 |
| May 5 | June 1 |
| August 8 | September 1 |
| November 7 | December 1 |

INTERNET ADDRESS

<http://www.aswater.com>

STATISTICAL REVIEW

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

| | 1999 | 1998 | 1997 | 1996 | 1995 | 1994 | 1993 | 1992 | 1991 | 1990 |
|--|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|-----------|
| FINANCIAL INFORMATION | | | | | | | | | | |
| Revenues by Classification | | | | | | | | | | |
| Residential and Commercial | \$144,273 | \$123,271 | \$131,007 | \$126,456 | \$106,480 | \$100,796 | \$ 86,918 | \$ 82,112 | \$ 68,063 | \$ 69,161 |
| Industrial | 2,278 | 1,917 | 1,998 | 1,847 | 1,674 | 1,459 | 1,134 | 1,110 | 1,019 | 1,021 |
| Fire Service | 1,374 | 1,329 | 1,319 | 1,269 | 1,211 | 1,181 | 1,149 | 1,067 | 927 | 954 |
| Other — Water | 11,768 | 8,277 | 6,664 | 10,425 | 9,557 | 8,651 | 8,954 | 6,336 | 8,273 | 5,150 |
| Total Water Revenue | 159,693 | 134,794 | 140,988 | 139,997 | 118,922 | 112,087 | 98,155 | 90,625 | 78,282 | 76,286 |
| Electric Revenue | 13,338 | 13,201 | 12,767 | 11,532 | 10,891 | 10,588 | 10,351 | 10,035 | 12,378 | 11,054 |
| Other Revenue | 390 | 65 | — | — | — | — | — | — | — | — |
| Total Operation Revenues | 173,421 | 148,060 | 153,755 | 151,529 | 129,813 | 122,675 | 108,506 | 100,660 | 90,660 | 87,340 |
| Net Income | 16,101 | 14,623 | 14,059 | 13,460 | 12,165 | 11,338 | 12,026 | 12,142 | 15,363 | 8,907 |
| Earnings Available for Common Shareholders | 16,013 | 14,533 | 13,967 | 13,366 | 12,069 | 11,240 | 11,926 | 12,040 | 15,259 | 8,801 |
| Earnings per Common Share | 1.79 | 1.62 | 1.56 | 1.69 | 1.54 | 1.43 | 1.66 | 1.82 | 2.34 | 1.40 |
| Dividends Declared per Common Share | 1.28 | 1.26 | 1.25 | 1.23 | 1.21 | 1.20 | 1.19 | 1.15 | 1.10 | 1.08 |
| Book Value per Common Share | 17.73 | 17.23 | 16.86 | 16.52 | 15.5 | 15.16 | 14.92 | 13.28 | 12.59 | 11.31 |
| Total Assets | 533,181 | 484,671 | 457,074 | 430,922 | 406,255 | 383,627 | 358,533 | 312,491 | 293,444 | 268,028 |
| Net Utility Plant | 449,595 | 414,753 | 383,623 | 357,776 | 334,968 | 317,879 | 294,990 | 277,525 | 258,558 | 235,713 |
| Capital Additions | 51,578 | 45,269 | 39,226 | 34,374 | 28,761 | 30,307 | 28,626 | 26,975 | 32,472 | 27,078 |
| Long-term Debt (Net) | 167,363 | 120,809 | 115,286 | 107,190 | 107,455 | 92,891 | 84,621 | 84,195 | 82,634 | 67,246 |
| Preferred Shares | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 | 1,600 |
| Preferred Shares — Mandatory Redemption | 360 | 400 | 440 | 480 | 520 | 560 | 600 | 640 | 680 | 720 |
| Investment per Customer | \$ 2,267 | \$ 2,099 | \$ 1,900 | \$ 1,808 | \$ 1,688 | \$ 1,578 | \$ 1,480 | \$ 1,388 | \$ 1,297 | \$ 1,213 |
| OPERATION INFORMATION | | | | | | | | | | |
| Water Sold by Classification (mg) | | | | | | | | | | |
| Residential and Commercial | 53,742 | 49,302 | 54,623 | 52,843 | 49,641 | 51,084 | 48,033 | 47,541 | 44,528 | 51,696 |
| Industrial | 853 | 832 | 899 | 828 | 802 | 818 | 679 | 699 | 737 | 937 |
| Fire Service | 411 | 649 | 417 | 831 | 130 | 308 | 33 | 23 | 11 | 50 |
| Other | 4,828 | 4,124 | 5,070 | 4,932 | 4,706 | 4,537 | 4,019 | 3,890 | 3,807 | 4,511 |
| Total Water | 59,834 | 54,907 | 61,009 | 59,434 | 55,279 | 56,747 | 52,764 | 52,153 | 49,083 | 57,194 |
| Total Electric Sales (mwh) | 127,584 | 123,791 | 121,315 | 117,139 | 111,519 | 110,234 | 106,234 | 105,346 | 101,923 | 103,376 |
| Customers by Classification | | | | | | | | | | |
| Residential and Commercial | 238,511 | 237,157 | 236,270 | 235,244 | 233,920 | 232,879 | 231,966 | 230,956 | 230,175 | 221,888 |
| Industrial | 328 | 332 | 331 | 333 | 326 | 323 | 322 | 330 | 347 | 376 |
| Fire Service | 3,140 | 3,112 | 2,964 | 2,925 | 2,909 | 2,896 | 2,877 | 2,846 | 2,779 | 2,610 |
| Other | 2,107 | 2,033 | 2,016 | 2,046 | 1,807 | 1,807 | 1,820 | 1,795 | 1,812 | 1,819 |
| Total Water | 244,086 | 242,634 | 241,581 | 240,548 | 238,962 | 237,905 | 236,985 | 235,927 | 235,113 | 226,693 |
| Electric | 21,181 | 20,865 | 20,698 | 20,437 | 20,475 | 20,331 | 20,131 | 20,039 | 19,780 | 19,559 |
| Total Company | 265,267 | 263,499 | 262,279 | 260,985 | 259,437 | 258,236 | 257,116 | 255,966 | 254,893 | 246,252 |
| Water Production by Source (mg) | | | | | | | | | | |
| Purchased | 25,647 | 22,885 | 28,894 | 27,147 | 24,356 | 25,940 | 25,156 | 24,377 | 23,221 | 31,021 |
| Pumped — Electric | 36,969 | 35,596 | 34,531 | 35,216 | 34,105 | 33,337 | 32,056 | 30,406 | 28,640 | 28,923 |
| Pumped — Gas | 179 | 75 | 316 | 40 | 218 | 198 | 195 | 177 | 245 | 270 |
| Gravity and Surface | 1,035 | 74 | 1,147 | 932 | 979 | 967 | 658 | 1,249 | 1,046 | 1,255 |
| Total Supply | 63,830 | 58,630 | 64,888 | 63,335 | 59,658 | 60,442 | 58,065 | 56,209 | 53,152 | 61,469 |
| Miles of Main in Service | 2,742 | 2,654 | 2,638 | 2,603 | 2,587 | 2,567 | 2,560 | 2,549 | 2,535 | 2,517 |
| Number of Employees | 492 | 470 | 467 | 463 | 448 | 467 | 486 | 445 | 422 | 410 |

mg=Millions of Gallons mwh=Mega-Watt Hours

CUSTOMER SERVICE AREAS SERVED BY SOUTHERN CALIFORNIA WATER COMPANY

NUMBER OF CUSTOMERS

Region I

Northern District

| | |
|---------------|--------|
| Arden-Cordova | 13,835 |
| Bay Point | 4,879 |
| Clearlake | 2,110 |

Coastal District

| | |
|-------------|--------|
| Los Osos | 3,137 |
| Ojai | 2,782 |
| Santa Maria | 12,690 |
| Simi Valley | 12,683 |

Region II

Central District

| | |
|--------------------|--------|
| Central Basin East | 19,681 |
| Central Basin West | 19,359 |
| Culver City | 9,340 |

Southwest District

49,444

Region III

Foothill District

| | |
|--------------------|--------|
| Claremont | 10,458 |
| San Dimas | 15,674 |
| San Gabriel Valley | 11,751 |

Mountain/Desert District

| | |
|----------------|-------|
| Apple Valley | 2,350 |
| Barstow | 8,430 |
| Calipatria | 1,152 |
| Morongo Valley | 837 |
| Wrightwood | 2,540 |

Orange County District

| | |
|--------------|--------|
| Los Alamitos | 26,361 |
| Placentia | 14,593 |

Total Water 244,086

Bear Valley Electric Service 21,181

Total SCW Customers 265,267



CORPORATE INFORMATION

ELECTED OFFICERS

Lloyd E. Ross (58,1) (d)
Chairman of the Board

Floyd E. Wicks (56,12) (d)
President, Chief Executive Officer

McClellan Harris III (48,9) (d)
Chief Financial Officer,
Vice President-Finance,
Treasurer and Corporate Secretary

Joel A. Dickson (47,9) (e)
Vice President-Business Development

Donald K. Saddoris (56,32) (f)
Vice President-Customer Service, Region I

Joseph F. Young (54,22) (f)
Vice President-Customer Service, Region II

James B. Gallagher (45,12) (f)
Vice President-Customer Service, Region III

Denise L. Kruger (35,7) (f)
Vice President-Water Quality

Susan L. Conway (38,11) (f)
Vice President-Regulatory Affairs

BOARD OF DIRECTORS OF AMERICAN STATES WATER COMPANY, SOUTHERN CALIFORNIA WATER COMPANY AND AMERICAN STATES UTILITY SERVICES, INC.

Lloyd E. Ross (58,4)
(Chairman of the Board of Directors)
Managing Partner, Invermex L.P.
Irvine, California

Floyd E. Wicks (56,10) (c)
President and Chief Executive Officer

James L. Anderson (56,3) (a,c)
(Chairman of the company's Compensation
Committee)
Senior Vice President, Americo Life Inc.
Austin, Texas

Jean E. Auer (63,4) (a,c)
(Chairperson of the company's Nominating
and Governance Committee)
Consultant to the San Francisco Estuary
Project and member of the Board of
Directors of the Water Education
Foundation
Council Member of the Town of
Hillsborough, California

N. P. Dodge, Jr. (62,9) (a,b)
President, N.P. Dodge Company
Omaha, Nebraska

Anne M. Holloway (47,2) (a,b)
Vice President, Navigant Consulting Inc.
Atherton, California

Robert F. Kathol (58,4) (a,b)
(Chairman of the company's Audit and
Finance Committee)
Executive Vice President
Kirkpatrick, Pettis, Smith, Polian Inc.
Omaha, Nebraska

(age, years of service)

- (a) Member - Compensation Committee
- (b) Member - Audit and Finance Committee
- (c) Member - Nominating and Governance Committee
- (d) Holds same title in American States Water Company, Southern California Water Company and American States Utility Services, Inc.
- (e) Holds same title in American States Water Company, American States Utility Services, Inc. and holds title of Vice President - Customer and Operations Support in Southern California Water Company
- (f) Officer of Southern California Water Company only



(From left) Floyd E. Wicks, Jean E. Auer, N.P. Dodge, Jr., Anne M. Holloway, James L. Anderson, Robert F. Kathol, Lloyd E. Ross

