American Water Works Company, Inc.
Form S-1/A
October 12, 2007
Table of Contents

As filed with the Securities and Exchange Commission on October 11, 2007.

Registration No. 333-145757

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Amendment No. 1 to

Form S-1

REGISTRATION STATEMENT UNDER

THE SECURITIES ACT OF 1933

AMERICAN WATER WORKS COMPANY, INC.

AMERICAN WATER CAPITAL CORP.

(Exact name of registrant as specified in its charter)

Delaware	**4941**	**51-0063696**
Delaware	**522300**	**22-3732448**
(State or other jurisdiction of incorporation or organization)	**(Primary Standard Industrial Classification Code Number)**	**(I.R.S. Employer Identification Number)**

1025 Laurel Oak Road

Voorhees, NJ 08043

(856) 346-8200

(Address, including zip code, and telephone number, including area code, of registrant s principal executive offices)

Donald L. Correll	**George W. Patrick, Esq.**
President and Chief Executive Officer	**Vice President and Secretary**
American Water Works Company, Inc.	**American Water Works Capital Corp.**
1025 Laurel Oak Road	**1025 Laurel Oak Road**
Voorhees, NJ 08043	**Voorhees, NJ 08043**
(856) 346-8200	**(856) 346-8200**

(Name and address, including zip code, and telephone number, including area code, of agent for service)

Copies to:

William V. Fogg, Esq.	**George W. Patrick, Esq.**	**Robert E. Buckholz, Jr., Esq.**
Cravath, Swaine & Moore LLP	**Senior Vice President and General Counsel**	**Sullivan & Cromwell LLP**
Worldwide Plaza	**American Water Works Company, Inc.**	**125 Broad Street**
825 Eighth Avenue	**1025 Laurel Oak Road**	**New York, NY 10004**
New York, NY 10019	**Voorhees, NJ 08043**	**(212) 558-4000**
(212) 474-1000	**(856) 346-8200**	

Approximate date of commencement of proposed sale to the public: As soon as practicable after the effective date of this Registration Statement.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box. ¨

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration number of the earlier effective registration statement for the same offering. ¨

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Proposed Maximum Aggregate Offering Price(1)(2)	Amount of Registration Fee

Equity units	$500,000,000	$15,350.00 (7)
American Water Capital Corp. Senior Notes (3)		
Common stock, par value $1.00 per share (4)	$500,000,000	$15,350.00 (7)
Purchase Contracts (5)		
Support Agreement (6)		

(1) Includes shares to be sold upon exercise of the underwriters option to purchase additional corporate units. See Underwriting.
(2) Estimated solely for the purposes of calculating the registration fee pursuant to Rule 457(o) of Regulation C under the Securities Act of 1933, as amended.
(3) The American Water Capital Corp. Senior Notes are offered as a component of the equity units for no additional consideration.
(4) Shares of common stock of American Water Works, Inc. to be issued to the holders of equity units upon settlement of the purchase contracts, for a purchase price of $50.00 per unit. The actual number of shares of common stock to be issued will not be determined until the date of settlement of the related equity units.
(5) The Purchase Contracts are offered as a component of the equity units for no additional consideration.
(6) The American Water Works Company, Inc. Support Agreement is offered as a component of the equity security units for no additional consideration.
(7) Previously paid.

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

Table of Contents

The information in this preliminary prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This preliminary prospectus is not an offer to sell these securities, and we are not soliciting an offer to buy these securities, in any state where the offer or sale is not permitted.

Subject to Completion. Dated October 11, 2007.

(Preliminary Prospectus)

Equity Units

(Initially Consisting of Corporate Units)

American Water Works Company, Inc.

Equity Units

This is an offering of equity units of American Water Works Company, Inc., referred to as American Water. Each equity unit will have a stated amount of $50 and will consist of a purchase contract issued by us and, initially, a 1/20, or 5%, undivided beneficial ownership interest in $1,000 principal amount of senior notes due 2012 issued by our subsidiary American Water Capital Corp., referred to as AWCC, which we refer to as a corporate unit.

The purchase contract will obligate you to purchase from American Water, no later than , 2010, for a price of $50 in cash, the following number of shares of American Water s common stock, subject to anti-dilution adjustments:

- if the average closing price of American Water s common stock over the 20-trading day period ending on the third trading day prior to , 2010 equals or exceeds $, shares of American Water s common stock;

- if the average closing price of American Water s common stock over the same period is less than $ but greater than $, a number of shares of American Water s common stock having a value, based on such average closing price, equal to $50; and

- if the average closing price of American Water s common stock over the same period is less than or equal to $, shares of American Water s common stock.

American Water will also pay you quarterly contract adjustment payments at a rate of % per year of the stated amount of $50 per equity unit, or $ per year, subject to American Water s right to defer contract adjustment payments, as described in this prospectus.

The senior notes will initially bear interest at a rate of % per year, payable, initially, quarterly. The senior notes will be remarketed as described in this prospectus. Following a successful remarketing, the interest rate on the senior notes will be reset and interest will become payable semi-annually.

The corporate units will initially be sold by the underwriters in minimum increments of 20 units.

Concurrently with this offering, RWE Aktiengesellschaft, through a subsidiary, is offering by separate prospectus shares of American Water s common stock, plus up to an additional shares of common stock if the underwriters exercise their option to purchase additional shares. This offering of equity units is contingent upon the consummation of the concurrent offering of American Water s common stock, referred to as the concurrent initial public offering.

American Water intends to apply to list the corporate units on the New York Stock Exchange under the symbol . American Water intends to apply to have its common stock listed on the New York Stock Exchange under the symbol AWK.

Investing in our equity units involves risks. See Risk Factors on page 23 to read about factors you should consider before buying equity units.

Neither the Securities and Exchange Commission, any state securities commission or any other regulatory body has approved or disapproved of these securities or passed on the accuracy or adequacy of this prospectus. Any representation to the contrary is a criminal offense.

	Per unit	Total
Public offering price	$	$
Underwriting discounts	$	$
Proceeds, before expenses, to American Water	$	$

The underwriters may also purchase up to an additional corporate units from us at the public offering price, less the underwriting discount, within 30 days of the date of this prospectus.

The underwriters expect to deliver the equity units against payment in New York, New York on .

Goldman, Sachs & Co. Citi Merrill Lynch & Co.

Prospectus dated , 2007.

Table of Contents

Table of Contents

Table of Contents

TABLE OF CONTENTS

Our regulated subsidiaries are subject to economic regulation by state PUCs in Arizona, California, Hawaii, Illinois, Indiana, Iowa, Kentucky, Maryland, Missouri, New Jersey, New Mexico, New York, Ohio, Pennsylvania, Tennessee, Texas, Virginia and West Virginia. Some of these states have enacted laws that require regulatory approval for the acquisition of control of any regulated utility. In those states, obtaining control of the parent or any other company that controls a regulated utility also requires prior regulatory approval. The threshold for a change in control is a fact-specific inquiry that varies by state. For example, in some states, a presumption of control will arise when an acquiring party acquires more than 9.9% of the voting securities of the regulated utility or the controlling entity. In addition to ownership, other states may analyze the degree of influence or control an acquiror may exert over the company. Any person acquiring our common stock in this offering, through the concurrent offering of our common stock or in any other purchase of our common stock in a quantity sufficient to trigger a change in control under state law would need the prior approval of the applicable state PUC.

Dealer Prospectus Delivery Obligation

Through and including , 2007 (the 25th day after the date of this prospectus), all dealers that effect transactions in these securities, whether or not participating in this offering, may be required to deliver a prospectus. This is in addition to the dealers obligation to deliver a prospectus when acting as an underwriter and with respect to unsold allotments or subscriptions.

(i)

Table of Contents

PROSPECTUS SUMMARY

This summary highlights information contained elsewhere in this prospectus. It may not contain all the information that is important to you. You should carefully read this entire prospectus, including the section captioned Risk Factors and the consolidated financial statements and notes to the consolidated financial statements, before making an investment decision. For the definition of certain terms used in this prospectus, please refer to the definitions set forth in the Glossary.

Our Company

Founded in 1886, American Water Works Company, Inc., which we refer to, together with its subsidiaries, as American Water or the Company is the largest investor-owned United States water and wastewater utility company, as measured both by operating revenue and population served. Our nearly 6,900 employees provide approximately 16.2 million people with drinking water, wastewater and other water-related services in 32 states and Ontario, Canada.

Our primary business involves the ownership of regulated water and wastewater utilities that provide water and wastewater services to residential, commercial and industrial customers, treating and delivering over one billion gallons of water per day. Our subsidiaries that provide these services are generally subject to economic regulation by state Public Utility Commissions, which we refer to as state PUCs, in the states in which they operate. In 2006, we generated $2,093.1 million in total operating revenue, representing approximately four times the operating revenue of the next largest investor-owned company in the United States water and wastewater business, $252.5 million in operating income, which includes $221.7 million of impairment charges relating to continuing operations, and a net loss of $162.2 million. Our Regulated Business, operating in 20 states in the United States, generated 88.6% of our total operating revenue in 2006.

We also provide services that are not subject to economic regulation by state PUCs. Our Non-Regulated Businesses include our Contract Operations Group, our Applied Water Management Group and our Homeowner Services Group. In 2006, our Non-Regulated Businesses generated $248.5 million in operating revenue, prior to inter-segment eliminations.

Our Industry

The United States water and wastewater industry has two main segments: (i) utility, which involves supplying water and wastewater services to customers, and (ii) general services, which involves providing water and wastewater-related services, including engineering, consulting and sales of water infrastructure and distribution products, such as pipes, to water and wastewater utilities and other consumers on a fee-for-service contract basis.

The utility segment includes municipal systems, which are owned and operated by local governments, and investor-owned systems. Government-owned systems make up the vast majority of the United States water and wastewater utility segment, accounting for approximately 84% of all United States community water systems and approximately 98% of all United States community wastewater systems.

The utility segment is characterized by high barriers to entry, including high capital spending requirements. Investor-owned water and wastewater utilities also face regulatory approval processes in order to do business, which may involve obtaining relevant operating approvals, including certificates of public convenience and necessity (or similar authorizations), pursuant to which state PUCs grant investor-owned utilities the right to provide service within an authorized service area. The utility segment of the United States water and wastewater industry is highly fragmented, with approximately 53,000 community water systems and approximately 16,000

Table of Contents

community wastewater facilities, according to the United States Environmental Protection Agency, or EPA, and therefore presents opportunities for consolidation. Larger utilities, such as ours, that have greater access to capital are generally more capable of making mandated and other necessary infrastructure upgrades to water and wastewater systems.

Our Strengths

We believe that we are distinguished by the following key competitive strengths:

Market leader with broad national footprint and strong local presence. We are the largest and most geographically diversified investor-owned water and wastewater utility company in the United States. Our scale and geographic scope enable us to capitalize effectively on growth opportunities across our service areas, while helping to insulate us from adverse conditions in any one geographic area.

Regulatory, weather and economic diversity. Our presence in numerous jurisdictions and localities across the United States promotes more stable and predictable financial performance across our overall business.

Economies of scale. Our scale and long-standing history with suppliers provide us with a competitive advantage in procuring goods and services reliably and economically.

Active community involvement supports customer satisfaction. We establish an active presence in the local communities where we operate to better serve our customers. We work closely with these communities to help create detailed water development plans, collaborate on growth initiatives and implement various water infrastructure and conservation projects.

Regulated Businesses provide financial stability. Our core Regulated Businesses, which consist of locally managed utility subsidiaries that generally are economically regulated by the states in which they operate, accounted for approximately 88.6% of our consolidated operating revenue in 2006. Our Regulated Businesses provide a high degree of financial stability because (i) high barriers to entry insulate us from competitive pressures, (ii) economic regulation promotes predictability in financial planning and long-term performance through the rate-setting process and (iii) our largely residential customer base promotes consistent operating results.

Experience in securing appropriate rates of return and promoting constructive regulatory frameworks. We seek appropriate rates of return on our investment and a return of our investment and recovery of prudently incurred operating expenses from state PUCs in the form of rate increases, which we refer to as rate relief. We have a strong track record of providing reliable service at cost-effective rates, which has typically resulted in high customer satisfaction and has generally allowed us to maintain positive relations with local communities and regulators. We have generally been granted rate relief in a timely manner after application, and prior to our acquisition by RWE, we often were successful in securing appropriate rate relief when we filed rate cases. In the period following RWE s acquisition of the Company, as a condition to the approval of the acquisition, we agreed with some state PUCs that we would not file rate cases for specified periods of time, also known as rate stay-outs. As of June 30, 2007, all rate stay-out provisions had expired.

Significant growth opportunities with a low risk business profile. We believe we are well positioned to benefit from favorable industry dynamics in the water and wastewater sectors, which provide significant opportunities for future growth in both our Regulated Businesses and complementary Non-Regulated Businesses.

Replacement of aging infrastructure. We intend to invest capital prudently to enable us to continue to provide essential services to our regulated water and wastewater utility customers and to assist municipalities in meeting the capital challenges of making substantial required infrastructure upgrades.

Table of Contents

Fragmented industry provides consolidation opportunities. The presence of our Regulated Businesses in 20 states, provides a large platform on which to grow both organically and through consolidation from among the numerous community wastewater systems in the United States.

Opportunities for non-regulated growth. Our public/private partnership expertise and national footprint increases our ability to make opportunistic investments in non-regulated businesses that are complementary to our Regulated Businesses.

Experienced senior management team. Our three senior managers have an average of 27 years of experience in the utilities industry. Donald L. Correll, our President and Chief Executive Officer, Ellen C. Wolf, our Senior Vice President and Chief Financial Officer, and John S. Young, our Chief Operating Officer, have all held senior management positions at publicly traded companies. Our 12 state presidents have an average of 24 years of experience in the utilities industry.

Industry leader in water quality, testing and research. We are experts in water quality testing, compliance and treatment and have established and own industry-leading water testing facilities. Our technologically advanced quality control and testing laboratory in Belleville, Illinois is certified in 24 states. Our laboratories and other facilities perform more than one million water quality tests per year.

Our Strategy

Our goal is to consistently provide customers with safe, high quality drinking water and reliable water and wastewater services. Our business strategies include:

- continuing to prudently invest in regulated water and wastewater infrastructure projects;
- earning an appropriate rate of return on our investments from state PUCs;
- growing our Regulated Businesses through acquisitions; and
- continuing to pursue public/private partnerships, including O&M and military contracts and services and other non-regulated businesses that are complementary to our Regulated Businesses.

The Transactions

American Water is currently an indirect wholly owned subsidiary of RWE Aktiengesellschaft, a stock corporation incorporated in the Federal Republic of Germany whose shares are publicly listed on the Frankfurt and Düsseldorf stock exchanges and other German stock exchanges as well as on the Zurich stock exchange which we refer to as RWE. RWE is one of Europe s leading electricity and gas companies and supplies 20 million customers with electricity and 10 million customers with gas in Germany, the United Kingdom and Central and Eastern Europe. On November 4, 2005, RWE announced its intention to exit its water activities in the United States and the United Kingdom to focus on its core European electricity and gas business and has since then completed the divestiture of its water business in the United Kingdom. As a part of this strategy, RWE intends to fully divest its ownership of American Water through the consummation of one or more public offerings of common stock of American Water as soon as reasonably practicable, subject to market conditions, which we refer to as the RWE Divestiture. On September 28, 2007, Thames Water Aqua US Holdings Inc., at the time an indirect wholly owned subsidiary of RWE, which we refer to as Thames US Holdings, was merged with and into American Water with American Water being the surviving entity, which we refer to as the Merger.

Table of Contents

Concurrently with this offering, RWE is offering by separate prospectus shares of American Water s common stock, plus up to an additional shares of common stock if the underwriters exercise their option to purchase additional shares. Prior to this offering we will effect a -for- stock split.

On September 20, 2007, we issued $1,750.0 million of debt to RWE, which we refer to as the RWE redemption notes, which was used to fund the early redemption of $1,750.0 million of preferred stock held by RWE. In addition, prior to the consummation of this offering, we intend to use the proceeds from the issuance of approximately $1,500.0 million aggregate principal amount of senior notes, referred to as the new senior notes, to fund the repayment of $1,270.1 million aggregate principal amount of RWE redemption notes and $222.0 million (including after tax gains of $1.3 million) aggregate principal amount of other debt owed to RWE, which we refer to as the RWE notes. The new senior notes will not be registered under the Securities Act and will be offered in reliance on an exemption from the registration requirements of the Securities Act. We intend to use a portion of the net proceeds from this offering of equity units to fund the repayment of approximately $479.9 million of RWE redemption notes, with the balance of the net cash proceeds of approximately $4.3 million to be used for general corporate purposes. These transactions, together with the non-cash equity contribution to the Company by RWE of $1,194.5 million of debt of our subsidiaries held by RWE on December 15, 2006, the non-cash equity contribution to the Company by RWE of $100.0 million of debt of our subsidiaries held by RWE on March 29, 2007 and the $550.0 million cash equity contribution to the Company by RWE on March 29, 2007, which was used to pay down $232.5 million of short-term debt and the remainder used for general working capital purposes, are collectively which we refer to as the Refinancing. The Refinancing, the Merger and the -for- split of common stock are collectively referred to in this prospectus as the Transactions.

Organizational Structure

The following chart sets forth our current organizational structure:

American Water is currently a direct wholly owned subsidiary of Thames Water Aqua Holdings GmbH, the selling stockholder in the concurrent initial public offering, a limited liability company organized under the laws of the Federal Republic of Germany and a direct wholly owned subsidiary of RWE. The following chart sets forth our organizational structure after giving effect to the consummation of the Transactions:

* Assumes that RWE, through its subsidiary Thames Water Aqua Holdings GmbH, will sell its shares of our common stock in more than one offering.

Table of Contents

Our Executive Offices

We are a corporation incorporated under the laws of Delaware. Our principal executive offices are located at 1025 Laurel Oak Road, Voorhees, NJ 08043. Our telephone number is (856) 346-8200. Our internet address is www.amwater.com. **The information contained on or accessible from our website does not constitute a part of this prospectus and is not incorporated by reference herein.**

American Water and its logos are our trademarks. Other service marks, trademarks and trade names referred to in this prospectus are the property of their respective owners.

Table of Contents

THE OFFERING

Unless the context otherwise requires, for purposes of this section entitled The Offering, the terms American Water, our, us or we refer to American Water Works Company, Inc. and not to any of its subsidiaries.

What are equity units?

Equity units may be either corporate units or treasury units as described below. The equity units offered hereby will initially consist of corporate units, each with a stated amount of $50. You can create treasury units from the corporate units in the manner described below under How Can I Create Treasury Units From Corporate Units?

What are the components of a corporate unit?

Each corporate unit consists of a purchase contract and, initially, a 1/20, or 5%, undivided beneficial ownership interest in $1,000 principal amount of AWCC s senior notes due 2012, which we call the applicable ownership interest in senior notes. The senior notes will be issued in minimum denominations of $1,000 and integral multiples thereof, except in certain limited circumstances. The applicable ownership interest in senior notes underlying a corporate unit is owned by you, but it initially will be pledged to us to secure your obligation under the related purchase contract. If the senior notes are successfully remarketed on or prior to the ninth business day immediately preceding , 2010, or if a tax event redemption occurs prior to , 2010, in each case as described in this prospectus, the senior notes underlying the corporate units will be replaced by the treasury portfolio described below under What is the treasury portfolio? and the applicable ownership interest in the treasury portfolio will then be pledged to American Water through the collateral agent to secure your obligation under the related purchase contract.

What is a purchase contract?

Each purchase contract underlying an equity unit obligates the holder of the purchase contract to purchase, and obligates American Water to sell, on , 2010, which we refer to as the purchase contract settlement date, for $50 in cash, a number of newly issued shares of American Water common stock equal to the settlement rate. The settlement rate will be calculated, subject to adjustment under the circumstances set forth in Description of the Purchase Contracts Anti-Dilution Adjustments, as follows:

- if the applicable market value of American Water common stock is equal to or greater than $, which we refer to as the threshold appreciation price, the settlement rate will be shares of American Water common stock;

- if the applicable market value of American Water s common stock is less than the threshold appreciation price but greater than $, which we refer to as the reference price, the settlement rate will be a number of shares of American Water s common stock equal to $50 divided by the applicable market value; and

- if the applicable market value of American Water common stock is less than or equal to the reference price, the settlement rate will be shares of American Water common stock.

Applicable market value means the average of the closing price per share of American Water common stock on each of the 20 consecutive trading days ending on the third trading day immediately preceding the purchase contract settlement date, subject to anti-dilution adjustments. The reference price represents the initial public offering price of American Water s common stock in the concurrent initial public offering. The threshold appreciation price represents a % appreciation over the reference price.

Can I settle the purchase contract early?

You can settle a purchase contract for cash prior to the purchase contract settlement date, subject to certain exceptions described under Description of the Purchase Contracts Early Settlement. If a purchase contract is settled early, the number of shares of American Water common stock to be issued per purchase contract will be the stated amount of $50 divided by the threshold appreciation price, initially shares. In addition, if American Water is involved in a cash merger, which we define as any acquisition (whether by means of a liquidation, share exchange, tender offer, consolidation, recapitalization, reclassification, merger of us or any subsidiaries or other transfer of the consolidation assets of us and subsidiaries) or a series of related transactions or events in which at least 51% of our common stock is exchanged for, converted into or constitutes solely the right to receive cash, securities or other property, more than 10% of which consists of cash, securities or other property that are not, or upon issuance will not be, common equity interests listed for trading or quotation on the New York Stock Exchange or quoted on the Nasdaq Global Market or Nasdaq Global Select Market, you will have the right to accelerate and settle the purchase contract early at the settlement rate in effect immediately prior to the closing of that merger plus, subject to certain limitations, a make-whole amount. See Description of Purchase Contracts Early Settlement Upon Cash Merger. Your early settlement right is subject to the condition that, if required under the U.S. federal securities laws, we have a registration statement under the Securities Act of 1933 in effect covering the shares of common stock and other securities, if any, deliverable upon settlement of a purchase contract. We have agreed that, if required by U.S. federal securities laws, we will use reasonable efforts to have a registration statement in effect covering those shares of common stock and other securities, if any, to be delivered in respect of the purchase contracts being settled.

What is a treasury unit?

A treasury unit is a unit created from a corporate unit and consists of a purchase contract and a 1/20, or 5%, undivided beneficial interest in a zero-coupon U.S. treasury security with a principal amount of $1,000 that matures on , 2010 (CUSIP No.), which we refer to as a treasury security. The ownership interest in the treasury security that is a component of a treasury unit will be owned by you, but will be pledged to American Water through the collateral agent to secure your obligation under the related purchase contract.

How can I create treasury units from corporate units?

Subject to the last sentence of this paragraph, unless the treasury portfolio has replaced the senior notes underlying the corporate units, each holder of corporate units will have the right, at any time on or prior to the seventh business day immediately preceding the purchase contract settlement date, to substitute for the underlying senior notes held by the collateral agent treasury securities in a total principal amount equal to the aggregate principal amount of the senior notes underlying the corporate units with respect to which substitution is being made. Because treasury securities and senior notes are issued in integral multiples of $1,000, holders of corporate units may make this substitution only in integral multiples of 20 corporate units. The ability of holders of corporate units to create treasury units will be subject to the limitation that holders may not create treasury units during any period commencing on and including the business day preceding any three-day remarketing period as described below under What is remarketing? and ending on and including, in the case of a successful remarketing during that three-day remarketing period, the reset effective date, or, if none of the remarketings during that three-day remarketing period is successful, the business day following the last remarketing date during that three-day remarketing period.

If the treasury portfolio has replaced the senior notes underlying the corporate units as a result of either a successful remarketing of the senior notes or a tax event redemption, holders of corporate units will have the right, at any time on or prior to the second business day immediately preceding the purchase contract settlement date, to substitute treasury securities for the applicable ownership interests in the treasury portfolio underlying

Table of Contents

the corporate units held by the collateral agent, but holders of corporate units can only make this substitution in integral multiples of corporate units (or such other number of corporate units as may be determined by the remarketing agent upon a successful remarketing of senior notes if the reset effective date is not a regular quarterly interest payment date).

Each of these substitutions will create treasury units, and the senior notes underlying the applicable ownership interests in senior notes or applicable ownership interests in the treasury portfolio will be released to the holder and be tradable separately from the treasury units.

How can I recreate corporate units from treasury units?

Subject to the last sentence of this paragraph, unless the treasury portfolio has replaced the senior notes underlying the corporate units, each holder of treasury units will have the right, at any time on or prior to the seventh business day immediately preceding the purchase contract settlement date, to substitute for the related treasury securities held by the collateral agent senior notes having a principal amount equal to the aggregate principal amount at stated maturity of the treasury securities for which substitution is being made. Because treasury securities and senior notes are issued in integral multiples of $1,000, holders of treasury units may make these substitutions only in integral multiples of 20 treasury units. The ability of holders of treasury units to recreate corporate units will be subject to the limitation that holders may not recreate corporate units during any period commencing on and including the business day preceding any three-day remarketing period and ending on and including, in the case of a successful remarketing during that three-day remarketing period, the reset effective date, or, if none of the remarketings during that three-day remarketing period is successful, the business day following the last remarketing date during that three-day remarketing period.

If the treasury portfolio has replaced the senior notes underlying the corporate units as a result of either a successful remarketing of the senior notes or a tax event redemption, holders of treasury units will have the right, at any time on or prior to the second business day immediately preceding the purchase contract settlement date, to substitute the applicable ownership interests in the treasury portfolio for the treasury securities underlying the treasury units, but holders of treasury units can only make this substitution in integral multiples of treasury units (or such other number of treasury units as may be determined by the remarketing agent upon a successful remarketing of senior notes if the reset effective date is not a regular quarterly interest payment date). Each of these substitutions will recreate corporate units and the applicable treasury securities will be released to the holder and be separately tradable from the corporate units.

What payments am I entitled to as a holder of corporate units?

Holders of corporate units will be entitled to receive quarterly cash distributions consisting of their pro rata share of interest payments on the senior notes payable by AWCC, equivalent to the rate of % per year on the applicable ownership interests in senior notes (or distributions on the applicable ownership interests in the treasury portfolio if the senior notes have been replaced by the treasury portfolio), and contract adjustment payments payable by American Water at the rate of % per year on the stated amount of $50 per corporate unit, subject to American Water s right to defer the contract adjustment payments as described below.

If interest on the senior notes is reset on a reset effective date that is not a scheduled interest payment date, the collateral agent will receive on behalf of holders of corporate units a payment from AWCC on such reset effective date of accrued and unpaid interest on the senior notes from the most recent quarterly interest payment date to, but excluding, such reset effective date. On the quarterly payment date next following the reset effective date, corporate unit holders will receive a regular quarterly cash distribution comprised of their pro rata portion of that interest payment, the portion of their applicable ownership interest in the remarketing treasury portfolio that matures prior to that quarterly payment date and the contract adjustment payment payable on that date.

Table of Contents

What payments will I be entitled to if I convert my corporate units to treasury units?

Holders of treasury units will be entitled to receive quarterly contract adjustment payments payable by American Water at the rate of % per year on the stated amount of $50 per treasury unit, subject to our right to defer the contract adjustment payments as described below. There will be no distributions in respect of the treasury securities that are a component of the treasury units but the holders of the treasury units will continue to receive the scheduled quarterly interest payments on the senior notes that were released to them when they created the treasury units as long as they continue to hold the senior notes.

Does American Water have the option to defer current payments?

American Water has the right to defer the payment of contract adjustment payments until no later than the purchase contract settlement date; provided, however, that in an early settlement upon a cash merger or any other early settlement of the purchase contracts, American Water will pay deferred contract adjustment payments through the cash merger settlement date or the most recent quarterly payment date, as applicable. Any deferred contract adjustment payments would accrue additional contract adjustment payments at the rate of % per year until paid, compounded quarterly, to, but excluding, the earlier of the purchase contract settlement date and the date of any earlier settlement of the purchase contract. AWCC is not entitled to defer payments of interest on the senior notes.

In the event that American Water exercises its option to defer the payment of contract adjustment payments, then until the deferred contract adjustment payments have been paid, American Water will not, with certain exceptions, declare or pay dividends on, make distributions with respect to, or redeem, purchase or acquire, or make a liquidation payment with respect to, any of its capital stock.

What are the payment dates for the corporate units?

The payments described above in respect of the corporate units will be payable quarterly in arrears on February 1, May 1, August 1 and November 1, of each year, commencing on , subject to, in the case of that portion of the current payment attributable to contract adjustment payments, the deferral provisions described in this prospectus.

What is remarketing?

We may, at our option and in our sole discretion, elect to remarket the aggregate principal amount of senior notes underlying the aggregate applicable ownership interests in senior notes held by corporate unit holders as part of a corporate unit on any remarketing date occurring during the period for early remarketing beginning on the third business day preceding , 2010 and ending on the ninth business day preceding , 2010, unless the senior notes have been previously redeemed in connection with a tax event redemption or have been previously successfully remarketed. Any remarketing during the period for early remarketing will occur during one or more three-day remarketing periods that consist of three sequential possible remarketing dates selected by us and will include the senior notes underlying the corporate units and other senior notes of holders that have elected to include those senior notes in the remarketing.

On each remarketing date occurring during the period for early remarketing, the remarketing agent will use its reasonable efforts to obtain a price for the senior notes remarketed equal to approximately 100% of the purchase price for the remarketing treasury portfolio plus a fee to be determined between us and the remarketing agent, which we refer to as the remarketing fee. A portion of the proceeds from the remarketing equal to the remarketing treasury portfolio purchase price will be applied to purchase the remarketing treasury portfolio. The remarketing treasury portfolio will be substituted for the senior notes underlying the corporate units and will be pledged to us through the collateral agent to secure the corporate unit holders obligations to purchase American Water s common stock under the purchase contracts. When paid at maturity, an amount of the remarketing

Table of Contents

treasury portfolio equal to the principal amount of the substituted senior notes will automatically be applied to satisfy the corporate unit holders obligations to purchase American Water s common stock under the purchase contracts on , 2010.

In addition, the remarketing agent may deduct the remarketing fee from any amount of the proceeds from the remarketing of the senior notes in excess of the remarketing treasury portfolio purchase price; if such excess is less than the remarketing fee, then we shall be liable for the remainder of that remarketing fee. The remarketing agent will then remit the remaining portion of the proceeds from the remarketing of the senior notes, if any, for the benefit of the holders.

If a remarketing attempt described above is unsuccessful on the first remarketing date of a three-day remarketing period, subsequent remarketings as described above will be attempted on each of the two following remarketing dates in that three-day remarketing period until a successful remarketing occurs. If none of the three remarketings occurring during a three-day remarketing period results in a successful remarketing because the remarketing agent cannot obtain a price for the senior notes on any such date equal to at least 100% of the remarketing treasury portfolio purchase price or a condition precedent to the remarketing has not been satisfied, the interest rate on the senior notes will not be reset, the applicable ownership interests in senior notes will continue to be a component of corporate units and subsequent remarketings may, subject to the next paragraph, be attempted during one or more subsequent three-day remarketing periods as described above.

Unless the senior notes have been successfully remarketed on or prior to the ninth business day immediately preceding , 2010, the senior notes that underlie corporate units whose holders have failed to notify the purchase contract agent on or prior to the seventh business day immediately preceding , 2010 of their intention to pay cash in order to satisfy their obligations under the related purchase contracts, will, unless a tax event redemption has occurred or will occur prior to , 2010, be remarketed during a three-day remarketing period beginning on and including the fifth business day, and ending on and including the third business day, immediately preceding , 2010. This three-day remarketing period is referred to as the final three-day remarketing period and we refer to the third business day immediately preceding , 2010 as the final remarketing date. In this remarketing, the remarketing agent will use its reasonable efforts to obtain a price for the senior notes equal to approximately 100% of the aggregate principal amount of the senior notes being remarketed plus the remarketing fee. A portion of the proceeds from the remarketing equal to the aggregate principal amount of the senior notes being remarketed will automatically be applied to satisfy in full the corporate unit holders obligations to purchase American Water s common stock under the related purchase contracts on the purchase contract settlement date.

If a remarketing during the final three-day remarketing period is successful, the remarketing agent may deduct the remarketing fee from any amount of the proceeds in excess of the aggregate principal amount of the remarketed senior notes; if such excess is less than the remarketing fee, then we shall be liable for the remainder of the remarketing fee. The remarketing agent will then remit any remaining portion of the proceeds for the benefit of the holders. In connection with a successful remarketing, interest on the senior notes will be payable semiannually at the reset rate and the maturity date of the senior notes may be extended. The reset rate on the senior notes and the date, if any, to which the maturity date of the senior notes is extended will be determined on the date that the remarketing agent is able to successfully remarket the senior notes. The reset rate, modified interest payment dates and extension, if any, of the maturity date will become effective, if the remarketing is successful, on the reset effective date. The reset effective date will be, in the case of a successful remarketing during the period for early remarketing, the third business day immediately following the date of the successful remarketing and, in the case of a successful remarketing during the final three-day remarketing period, the purchase contract settlement date.

If a remarketing attempt described above is unsuccessful on the first remarketing date of the final three-day remarketing period, subsequent remarketings will be attempted as described above on each of the two following remarketing dates in the final three-day remarketing period until a successful remarketing occurs.

Table of Contents

What happens if the senior notes are not successfully remarketed?

If the senior notes have not been successfully remarketed on or prior to the final remarketing date, the interest rate on the senior notes will not be reset and holders of all senior notes will have the right to put their senior notes to us on the purchase contract settlement date at a put price equal to $1,000 per senior note ($50 per applicable ownership interest) plus accrued and unpaid interest. A holder of a senior note underlying a corporate unit will be deemed to have automatically exercised this put right unless, prior to 11:00 a.m., New York City time, on the second business day immediately preceding the purchase contract settlement date, such holder provides a written notice of an intention to settle the related purchase contract with separate cash and on or prior to the business day immediately preceding the purchase contract settlement date delivers to the collateral agent the purchase price in cash. Unless a corporate unit holder has settled the related purchase contracts with separate cash on or prior to the purchase contract settlement date, such holder will be deemed to have elected to apply a portion of the proceeds of the put price equal to the principal amount of the senior notes underlying such corporate units against such holder s obligations to American Water under the related purchase contracts, thereby satisfying such obligations in full, and American Water will deliver to such holder its common stock pursuant to the related purchase contracts.

Do I have to participate in the remarketing?

You may elect not to participate in any remarketing and to retain the senior notes underlying the applicable ownership interests in senior notes comprising part of your corporate units by (1) creating treasury units at any time prior to the business day preceding any three-day remarketing period or (2) if there has not been a successful remarketing prior to the final three-day remarketing period, notifying the purchase contract agent of your intention to pay cash to satisfy your obligation under the related purchase contracts on or prior to the seventh business day before the purchase contract settlement date and delivering the cash payment required under the purchase contracts to the collateral agent on or prior to the sixth business day before the purchase contract settlement date. Following a successful remarketing prior to the final three-day remarketing period, holders of treasury units can recreate corporate units at any time prior to the second business day immediately preceding the purchase contract settlement date, as described under How can I recreate corporate units from treasury units?

The interest rate, maturity date and scheduled interest payment dates of senior notes that are held by holders that do not participate in a remarketing will still be reset on the reset effective date in accordance with any reset of the interest rate, extension of the maturity date or modification of the scheduled interest payment dates of the senior notes in connection with a successful remarketing.

What is the treasury portfolio?

If there is a successful remarketing on or prior to the ninth business day preceding the purchase contract settlement date or if a tax event redemption described under Description of the Senior Notes Optional Redemption Tax Event occurs prior to the purchase contract settlement date, the senior notes will be replaced by the treasury portfolio. The treasury portfolio is a portfolio of U.S. treasury securities consisting of:

(1) for a remarketing treasury portfolio,

interest or principal strips of U.S. Treasury securities that mature on or prior to , 2010 in an aggregate amount equal to the principal amount of the senior notes underlying the corporate units; and

interest or principal strips of U.S. Treasury securities that mature on or prior to , 2010 in an aggregate amount equal to the aggregate interest payment that would be due on , 2010, on the principal amount of the senior notes that would have been components of the corporate units assuming no remarketing and no reset of the interest rate on the senior notes and assuming that interest on the senior notes accrued from the later of the reset effective date and , 2010 to, but excluding, , 2010.

Table of Contents

(2) for a tax event treasury portfolio,

- interest or principal strips of U.S. Treasury securities that mature on or prior to , 2010 in an aggregate amount at maturity equal to the applicable principal amount; and

- interest or principal strips of U.S. Treasury securities that mature on or prior to the business day immediately preceding that scheduled interest payment date in an aggregate amount at maturity equal to the aggregate interest payment (assuming no reset of the interest rate) that would be due on the applicable principal amount of the senior notes on that date.

If I am holding a senior note as a separate security from the corporate units, can I still participate in a remarketing of the senior notes and do I also have a put right in the event that there is no successful remarketing on or prior to the final remarketing date?

Holders of senior notes that are not part of the corporate units may elect, in the manner described in this prospectus, to have their senior notes remarketed by the remarketing agent along with the senior notes included in the corporate units. See Description of the Senior Notes Optional Remarketing. Such holders may also participate in any remarketing by recreating corporate units from their treasury units at any time on or prior to the second business day immediately prior to any of the three-day remarketing periods.

Holders of senior notes that are not part of a corporate unit may exercise their put right upon a failed final remarketing by providing written notice at least two business days prior to the purchase contract settlement date. The put price will be paid to such holder on the purchase contract settlement date.

Besides participating in a remarketing, how else can I satisfy my obligation under the purchase contracts?

Holders of corporate units or treasury units may also satisfy their obligations, or their obligations will be terminated, under the purchase contracts as follows:

- through early settlement as described under Can I settle the purchase contract early? above;

- through cash settlement prior to the final three-day remarketing period in the case of holders of corporate units, unless the treasury portfolio has replaced the senior notes underlying the corporate units, by notifying the purchase contract agent on or prior to the seventh business day prior to , 2008 and delivering the cash payment required under the related purchase contracts on or prior to the sixth business day immediately prior to , 2010;

- through the automatic application of the proceeds of the treasury securities in the case of the treasury units or proceeds from the treasury portfolio equal to the principal amount of the senior notes in the case of corporate units if the treasury portfolio has replaced the senior notes as a component of the corporate units;

- through exercise of the put right as described under What happens if the senior notes are not successfully remarketed prior to the final remarketing date? if no successful remarketing has occurred and none of the above events has taken place; or

- without any further action, upon the termination of the purchase contracts as a result of our bankruptcy, insolvency or reorganization.

What interest payments will I receive on the senior notes or on the applicable ownership interests in senior notes?

Interest on the senior notes will be payable initially quarterly in arrears at the annual rate of % per annum of the principal amount of $1,000 to, but excluding, the reset effective date, which will be the third business day following the date on which a remarketing of the senior notes is successfully completed, or in the case of a remarketing during the final three-day remarketing period, the purchase contract settlement date.

Table of Contents

Following a successful remarketing, the senior notes will bear interest from the reset effective date at the reset rate to, but excluding, , 2012 or, if the maturity of the senior notes is extended on the reset effective date, such extended maturity date. If interest on the senior notes is reset on a reset effective date that is not a scheduled interest payment date, holders of senior notes will receive on the reset effective date a payment of accrued and unpaid interest from the most recent interest payment date to, but excluding, such reset effective date (provided that holders of corporate units will receive that payment as described under What payments am I entitled to as a holder of corporate units?). On the interest payment date next following the reset effective date, holders of senior notes will receive a payment of interest accrued from and including the reset effective date, to but excluding such interest payment date. For United States federal income tax purposes, original issue discount will accrue on the senior notes. If there is not a successful remarketing of the senior notes, the interest rate will not be reset and the senior notes will continue to bear interest at the initial interest rate, payable quarterly in arrears.

What are the interest payment dates on the senior notes?

On or prior to the reset effective date, interest payments will be payable quarterly in arrears on each , , and , commencing , and on the reset effective date as described above in What interest payments will I receive on the senior notes? if the reset effective date is not otherwise a quarterly interest payment date. If the interest rate on the senior notes is reset on a reset effective date that is not otherwise a quarterly interest payment date, the collateral agent will receive the interest payment made on senior notes underlying corporate units on that reset effective date, which will be paid to holders of corporate units on the quarterly payment date next following that reset effective date.

From the reset effective date, interest payments on all senior notes will be paid semiannually in arrears on interest payment dates to be selected by us. If no successful remarketing of the senior notes occurs, interest payments on all senior notes will remain payable quarterly in arrears on the original quarterly interest payment dates.

When will the interest rate on the senior notes be reset and what is the reset rate?

Unless a tax event redemption has occurred, the interest rate on the senior notes will be reset on the date of a successful remarketing and the reset rate will become effective three business days thereafter, or in the case of a remarketing during the final three-day remarketing period, the purchase contract settlement date. The reset rate will be the interest rate determined by the remarketing agent as the rate the senior notes should bear in order for the senior notes underlying the corporate units to have an approximate aggregate market value on the remarketing date of 100% of the treasury portfolio purchase price plus the remarketing fee, in the case of a remarketing prior to the final three-day remarketing period, or 100% of the aggregate principal amount of the senior notes being remarketed plus the remarketing fee, in the case of a remarketing during the final three-day remarketing period. The interest rate on the senior notes will not be reset if there is not a successful remarketing. Any reset rate may not exceed the maximum rate, if any, permitted by applicable law.

When is the maturity of the senior notes?

The initial maturity date of the senior notes will be , 2012. Upon a successful remarketing of the senior notes, the maturity of the senior notes may be extended to a date selected by us that is up to ten years from the reset effective date. Such extended maturity date, if any, will be selected on the remarketing date and will become effective on the reset effective date. If the senior notes are not successfully remarketed on or prior to , 2012, the maturity of the senior notes will remain , 2012.

When may the senior notes be redeemed?

The senior notes are redeemable at our option, in whole but not in part, upon the occurrence and continuation of a tax event at any time prior to the earlier of the date of a successful remarketing and the purchase contract settlement date, as described in this prospectus under Description of the Senior Notes Optional Redemption Tax Event. Following any such redemption of the senior notes, which we refer to as a tax event redemption, the redemption price for the senior notes that underlie the corporate units will be paid to the collateral agent who will purchase the tax event treasury portfolio and remit any remaining proceeds to the holders. Thereafter, the applicable ownership interests in the tax event treasury portfolio will replace the applicable ownership interests in senior notes as a component of the corporate units and will be pledged to us through the collateral agent. Holders of senior notes that do not underlie corporate units will receive the redemption price paid in such tax event redemption in full.

What is the ranking of the senior notes?

The senior notes will rank equally with all of AWCC s other unsecured and unsubordinated obligations. The indenture under which the senior notes will be issued will not limit our ability to issue or incur other unsecured debt or issue preferred stock. The senior notes will have the benefit of a support agreement from American Water. American Water s obligation under the support agreement will rank equally with all of American Water s other unsecured and unsubordinated obligations.

The senior notes are not guaranteed by any of our subsidiaries and are the obligations only of AWCC and, by virtue of the support agreement, American Water. Accordingly, the senior notes are structurally subordinated to liabilities of our subsidiaries other than AWCC. We have no material assets or operations other than our equity interests, and AWCC has no material assets or operations other than its limited operations as a financial subsidiary for American Water and its operating subsidiaries for our businesses. We expect that payments of interest and principal that AWCC makes on the senior notes will be made only to the extent that our operating subsidiaries distribute cash and other property to us, and through us, to AWCC.

What are the principal U.S. Federal income tax consequences related to corporate units, treasury units and senior notes?

A beneficial owner of corporate units or senior notes, if separated from corporate units, should be treated as owning an interest in a debt instrument that should be subject to the Treasury regulations that govern contingent payment debt instruments. Under these rules, for all accrual periods beginning before the earlier of the reset effective date and , 2010, a holder will be required to include in gross income an amount in excess of the interest actually received, regardless of the holder s usual method of tax accounting, and a holder will generally recognize ordinary income or loss, rather than capital gain or loss, on the sale, exchange or disposition of senior notes (including upon a successful remarketing) or corporate units, to the extent such income or loss is allocable to the senior notes. A beneficial owner of treasury units will generally be required to include in gross income any original issue discount with respect to the treasury securities as it accrues on a constant yield to maturity basis. If the treasury portfolio has replaced the senior notes underlying the corporate units as a result of a successful remarketing of the senior notes or a tax event redemption, a beneficial owner of corporate units generally will be required to include in gross income its allocable share of original issue discount on the treasury portfolio as it accrues on a constant yield to maturity basis. We intend to report contract adjustment payments as ordinary income to you, but you may wish to consult your tax advisor concerning possible alternative characterizations.

FOR ADDITIONAL INFORMATION, SEE UNITED STATES FEDERAL INCOME TAX CONSEQUENCES.

What are the rights and privileges of the common stock?

The shares of American Water s common stock that you will be obligated to purchase under the purchase contracts have one vote per share. For more information, please see the discussion of American Water s common stock in this prospectus under the heading Risk Factors and under the heading Description of Capital Stock.

Table of Contents

THE OFFERING EXPLANATORY DIAGRAMS

The following diagrams demonstrate some of the key features of the purchase contracts, applicable ownership interests in senior notes, corporate units and treasury units, and the transformation of corporate units into treasury units and senior notes. The following diagrams assume that the senior notes are successfully remarketed and the interest rate on the senior notes is reset on the third business day immediately preceding the purchase contract settlement date.

Purchase Contract

Corporate units and treasury units both include a purchase contract under which the holder agrees to purchase shares of American Water s common stock on the purchase contract settlement date. In addition, these purchase contracts include unsecured contract adjustment payments as shown in the diagrams on the following pages.

Notes:

(1) If the applicable market value of American Water s common stock is less than or equal to the reference price of $, the number of shares of American Water s common stock to be delivered to a holder of an equity unit will be calculated by dividing the stated amount of $50 by the reference price.

(2) If the applicable market value of American Water s common stock is less than the threshold appreciation price of $ but greater than the reference price of $, the number of shares of American Water s common stock to be delivered to a holder of an equity unit will be calculated by dividing the stated amount of $50 by the applicable market value.

(3) If the applicable market value of American Water s common stock is greater than or equal to the threshold appreciation price, the number of shares of American Water s common stock to be delivered to a holder of an equity unit will be calculated by dividing the stated amount of $50 by the threshold appreciation price of $.

(4) The reference price is $, which is the initial public offering price of American Water s common stock in the concurrent initial public offering.

(5) The threshold appreciation price is $, which is % of the reference price.

(6) The applicable market value means the average of the closing price per share of American Water s common stock on each of the 20 consecutive trading days ending on the third trading day immediately preceding the purchase contract settlement date, subject to anti-dilution adjustments.

Corporate Units

A corporate unit consists of two components as described below:

Notes:

The holder of a corporate unit owns the 1/20, or 5%, undivided beneficial ownership interest in, and will be entitled to a corresponding portion of each interest payment payable in respect of, a $1,000 principal amount senior note but will pledge it to us to secure the holder s obligation under the related purchase contract.

The foregoing analysis assumes the senior notes are successfully remarketed during the final three-day remarketing period. If the remarketing were to be successful prior to such period, following the remarketing of the senior notes, the applicable ownership interests in the treasury portfolio will replace the applicable ownership interest in senior notes as a component of the corporate unit and the reset rate would be effective three business days following the successful remarketing.

If the treasury portfolio has replaced the senior notes as a result of a tax event redemption prior to , 2010, the applicable ownership interest in the treasury portfolio will also replace the applicable ownership interest in senior notes as a component of the corporate unit.

Table of Contents

Treasury Units

A treasury unit consists of two components as described below:

The holder owns the 1/20 ownership interest in the treasury security that forms a part of the treasury unit but will pledge it to us through the collateral agent to secure the holder s obligations under the related purchase contract. Unless the purchase contract is terminated as a result of our bankruptcy, insolvency or reorganization or the holder recreates a corporate unit, the treasury security will be used to satisfy the holder s obligation under the related purchase contract.

Treasury units can only be created with integral multiples of 20 corporate units.

Table of Contents

Senior Notes

Senior notes have the terms described below:

Notes:

Because the senior notes and the treasury securities are issued in minimum denominations of $1,000, holders of corporate units may only create treasury units in integral multiples of 20 corporate units.

To create 20 treasury units, a holder separates 20 corporate units into their two components 20 purchase contracts and a senior note and then combines the purchase contracts with a treasury security that has a principal amount at maturity of $1,000 that must be purchased on the open market at the corporate unitholder s expense and that matures on the day immediately preceding the purchase contract settlement date.

The senior note, which is no longer a component of corporate units and has a principal amount of $1,000, is released to the holder and is tradable as a separate security.

A holder owns the treasury security that forms a part of the treasury units but will pledge it to us through the collateral agent to secure its obligation under the related purchase contract.

The treasury security together with the 20 purchase contracts constitute 20 treasury units.

Transforming Corporate Units into Treasury Units and Senior Notes

The following illustration depicts the transformation of 20 corporate units into 20 treasury units and one $1,000 principal amount.

Following the successful remarketing of the senior notes prior to the final three-day remarketing period or a tax event redemption, the applicable ownership interests in the treasury portfolio, rather than the senior note, will be released to the holder upon the transformation of a corporate unit into a treasury unit and will be tradable separately.

The holder can also transform 20 treasury units and a $1,000 principal senior note (or, following a successful remarketing of the senior notes or a tax event redemption, the applicable ownership interest in the treasury portfolio) into 20 corporate units. Following that transformation, the treasury security, which will no longer be a component of the treasury unit, will be released to the holder and will be tradable as a separate security.

If the applicable ownership interest in the treasury portfolio has replaced the senior notes underlying the corporate units, the transformation of corporate units into treasury units and the transformation of treasury units into corporate units can only be made in certain minimum amounts, as more fully described in this prospectus.

Table of Contents

SUMMARY HISTORICAL CONSOLIDATED AND UNAUDITED PRO FORMA FINANCIAL DATA

The following table presents our summary historical consolidated financial data and summary unaudited pro forma consolidated financial data at the dates and for the periods indicated. The historical data as of December 31, 2005 and 2006 and for the years ended December 31, 2004, 2005 and 2006 have been derived from our audited historical consolidated financial statements and the notes to those statements included elsewhere in this prospectus. See footnote 1 to the table below. The historical data as of June 30, 2007 and for the six months ended June 30, 2006 and 2007 have been derived from our unaudited historical consolidated financial statements and the notes to those statements included elsewhere in this prospectus. Operating results for the six months ended June 30, 2006 and 2007 have been prepared on a basis consistent with our audited consolidated financial statements and reflect all adjustments, consisting of normal recurring adjustments, which are, in the opinion of management, necessary for a fair presentation of the financial position and results of operations for the periods presented. The results of any interim period are not necessarily indicative of the results that may be expected for any other interim period or for the entire fiscal year.

The summary unaudited pro forma financial data have been derived from our historical financial statements and adjusted to give effect to the Transactions. The summary unaudited pro forma financial data have been prepared to give effect to the Transactions as if they had occurred on January 1, 2006, in the case of the summary unaudited pro forma statement of operations data, and on June 30, 2007, in the case of the summary unaudited pro forma balance sheet data. The pro forma adjustments are based upon available information and certain assumptions that we believe are reasonable. The summary unaudited pro forma financial data are for informational purposes only and do not purport to represent what our results of operations or financial position actually would have been if the Transactions had occurred at any date, and such data do not purport to project the results of operations for any future period. See Unaudited Pro Forma Condensed Consolidated Financial Information.

Our historical financial data are not necessarily indicative of our future performance or what our financial position and results of operations would have been if we had operated as a separate, stand-alone entity during the periods shown. Because the data in this table is only a summary and does not provide all of the data contained in our financial statements, the information should be read in conjunction with Use of Proceeds, Capitalization, Unaudited Pro Forma Condensed Consolidated Financial Information, Selected Historical Consolidated Financial Data, Management s Discussion and Analysis of Financial Condition and Results of Operations and the financial statements and related notes thereto appearing elsewhere in this prospectus.

Table of Contents

	For the years ended December 31, 2004	2005	2006	For the six months ended June 30, 2006 (unaudited)	2007 (unaudited)	Pro forma for the year ended December 31, 2006 (unaudited)	Pro forma for the six months ended June 30, 2007 (unaudited)
	(dollars in thousands, except for share and per share data)						
Statement of operations data(1):							
Operating revenues	$ 2,017,871	$ 2,136,746	$ 2,093,067	$ 1,007,691	$ 1,027,277	$ 2,093,067	$ 1,027,277
Operating expenses							
Operation and maintenance	1,121,970	1,201,566	1,174,544	562,072	581,999	1,176,244	582,509
Depreciation and amortization	225,260	261,364	259,181	128,728	132,764	259,181	132,764
General taxes	170,165	183,324	185,065	94,756	93,819	185,065	93,819
Loss (gain) on sale of assets(2)	(8,611)	(6,517)	79	(1,795)	(6,113)	79	(6,113)
Impairment charges	78,688	385,434	221,685			221,685	
Total operating expenses, net	1,587,472	2,025,171	1,840,554	783,761	802,469	1,842,254	802,979
Operating income (loss)	430,399	111,575	252,513	223,930	224,808	250,813	224,298
Other income (deductions)							
Interest	(315,944)	(345,257)	(365,970)	(178,968)	(142,970)	(297,067)	(141,759)
Amortization of debt expense	(3,377)	(4,367)	(5,062)	(1,678)	(2,397)	(6,030)	(2,881)
Other, net(3)	14,350	13,898	9,581	4,927	7,351	9,581	7,351
Total other income (deductions)	(304,971)	(335,726)	(361,451)	(175,719)	(138,016)	(293,516)	(137,289)
Income (loss) from continuing operations before income taxes	125,428	(224,151)	(108,938)	48,211	86,792	(42,703)	87,009
Provision for income taxes	66,328	50,979	46,912	20,056	34,378	73,106	34,463
Income (loss) from continuing operations	$ 59,100	$ (275,130)	$ (155,850)	$ 28,155	$ 52,414	$ (115,809)	$ 52,546
Income (loss) from continuing operations per basic common share(4)(5)	$ 59,100	$ (275,130)	$ (155,850)	$ 28,155	$ 52,414		
Income (loss) from continuing operations per diluted common share(4)(5)	$ 59,100	$ (275,130)	$ (155,850)	$ 28,155	$ 52,414		
Basic weighted average common shares	1,000	1,000	1,000	1,000	1,000		
Diluted weighted average common shares	1,000	1,000	1,000	1,000	1,000		
Other data(1):							
Cash flows provided by (used in):							
Operating activities	$ 458,408	$ 525,435	$ 323,748	$ 66,723	$ 136,181		
Investing activities	(545,903)	(530,165)	(691,438)	(241,724)	(279,441)		
Financing activities	95,254	(9,049)	332,367	133,391	164,951		
Construction expenditures	(546,241)	(558,446)	(688,843)	(235,818)	(307,726)		

Table of Contents

	As of December 31, 2005	As of December 31, 2006	As of June 30, 2007 (unaudited)	Pro forma as of June 30, 2007 (unaudited)
	(dollars in thousands)			
Balance sheet data(1):				
Cash and cash equivalents	$ 65,077	$ 29,754	$ 51,445	$ 55,719
Utility plant at original cost, net of accumulated depreciation	8,101,769	8,605,341	8,806,066	8,806,066
Goodwill	3,181,570	2,962,493	2,962,564	2,962,564
Total assets	12,542,029	12,783,059	13,071,585	13,088,159
Redeemable preferred stock at redemption value(6)	1,774,691	1,774,475	1,774,299	24,299
Other long-term debt	3,011,827	3,096,404	3,335,579	5,254,579
Other short-term and current portion of long-term debt(7)	2,018,251	1,007,128	253,242	112,242
Total debt	6,804,769	5,878,007	5,363,120	5,391,120
Common stockholder s equity	2,804,716	3,817,397	4,520,149	4,484,793
Preferred stock without mandatory redemption requirements(6)	4,571	4,568	4,568	4,568

(1) On September 28, 2007, Thames US Holdings was merged with and into American Water, with American Water as the surviving entity. American Water is an indirect wholly owned subsidiary of RWE. The historical consolidated financial statements of American Water represent the consolidated results of the Company, formerly issued under the name Thames Water Aqua US Holdings, Inc. and Subsidiary Companies.

(2) Represents primarily losses (gains) on sales of publicly traded securities and dispositions of assets not needed in utility operations.

(3) Includes allowance for other funds used during construction, allowance for borrowed funds used during construction and preferred dividends of subsidiaries.

(4) The number of common shares used to compute net income per basic share and net income per diluted share for the fiscal years ended December 31, 2004, 2005 and 2006 and the six months ended June 30, 2006 and 2007 is 1,000 (the number of shares outstanding during such period) as no dilutive options or instruments were outstanding during these periods.

(5) The number of common shares used to compute pro forma net income per basic share is , which gives effect to the -for- stock split to be effected prior to the concurrent initial public offering. Net income per diluted share also gives effect to all restricted stock units and stock options to be granted under our 2007 Omnibus Equity Compensation Plan to our executive officers and certain key employees upon the consummation of the concurrent initial public offering as if they were exercised or converted into common stock using the treasury method. Incremental common shares included in diluted earnings per share are .

(6) Includes preferred stock held by RWE and other preferred stock issued by subsidiaries of the Company.

(7) Includes the short-term portion of redeemable preferred stock of $0.6 million.

Table of Contents

RISK FACTORS

Risks Related to Our Industry and Business

Our utility operations are heavily regulated. Decisions by state PUCs and other regulatory agencies and can significantly affect our business and results of operations.

Our Regulated Businesses provide water and wastewater services to our customers through subsidiaries economically regulated by state PUCs. Economic regulation affects the rates we charge our customers and has a significant effect on our business and results of operations. Generally, the state PUCs authorize us to charge rates that they determine are sufficient to recover our prudently incurred operating expenses, to enable us to finance the addition of new, or the replacement of existing, water and wastewater infrastructure and to allow us the opportunity to earn what they determine to be an appropriate rate of return on our invested capital and a return of our invested capital.

Our ability to meet our financial objectives depends upon the rates authorized by the various state PUCs. We periodically file rate increase applications with state PUCs. The ensuing administrative process may be lengthy and costly. We can provide no assurances that our rate increase requests will be granted. Even if approved, there is no guarantee that approval will be given in a timely manner or at a sufficient level to cover our expenses, the recovery of our investment and/or provide us an opportunity to earn an appropriate rate of return on our investment and a return of our investment. If the authorized rates are insufficient to cover operating expenses, to allow for the recovery of our investment and to provide an appropriate return on invested capital, or if the rate increase decisions are delayed, our financial condition, results of operations, cash flow and liquidity may be adversely affected. Even if rates are sufficient, we face the risk that we will not achieve the rates of return on our invested capital and a return of our invested capital that are permitted by the state PUC.

Our operations and the quality of water we supply are subject to extensive environmental laws and regulations. Our operating costs have increased, and are expected to continue to increase, as a result of complying with environmental laws and regulations. We also could incur substantial costs as a result of violations of or liabilities under such laws and regulations.

Our water and wastewater operations are subject to extensive United States federal, state and local and, in the case of our Canadian operations, Canadian laws and regulations, that govern the protection of the environment, health and safety, the quality of the water we deliver to our customers, water allocation rights, and the manner in which we collect, treat and discharge wastewater. These requirements include the United States Clean Water Act of 1972, which we refer to as the Clean Water Act, and the United States Safe Drinking Water Act of 1974, which we refer to as the Safe Drinking Water Act, and similar state and Canadian laws and regulations. We are also required to obtain various environmental permits from regulatory agencies for our operations. State PUCs also set conditions and standards for the water and wastewater services we deliver. If we deliver water or wastewater services to our customers that do not comply with regulatory standards, or otherwise violate environmental laws, regulations or permits, or other health and safety and water quality regulations, we could incur substantial fines, penalties or other sanctions or costs or damage to our reputation. In the most serious cases, regulators could force us to discontinue operations and sell our operating assets to another utility or municipality. Given the nature of our business which, in part, involves supplying water for human consumption, any potential non-compliance with, or violation of, environmental laws or regulations would likely pose a more significant risk to us than to an issuer not similarly involved in the water and wastewater industry.

We incur substantial operating and capital costs on an ongoing basis to comply with environmental laws and regulations and other health and safety and water quality regulations. These laws and regulations, and their enforcement, have tended to become more stringent over time, and new or stricter requirements could increase our costs. Although we may seek to recover ongoing compliance costs in our rates, there can be no guarantee that the various state PUCs or similar regulatory bodies that govern our Regulated Businesses would approve rate increases to recover such costs or that such costs will not adversely and materially affect our financial condition, results of operations, cash flow and liquidity.

Table of Contents

We may also incur liabilities under environmental laws and regulations requiring us to investigate and clean up environmental contamination at our properties or at off-site locations where we have disposed of waste or caused adverse environmental impacts. The discovery of previously unknown conditions, or the imposition of cleanup obligations in the future, could result in significant costs, and could adversely affect our financial condition, results of operations, cash flow and liquidity. Such remediation losses may not be covered by our insurance policies and may make it difficult for us to secure insurance in the future at acceptable rates.

Changes in laws and regulations over which we have no control can significantly affect our business and results of operations.

Any governmental entity that regulates our operations may enact new legislation or adopt new regulations or policies at any time, and new judicial decisions may change the interpretation of existing legislation or regulations at any time. The individuals who serve as regulators are elected or are political appointees. Therefore, elections which result in a change of political administration or new appointments may also result in changes in the individuals who serve as regulators and the policies of the regulatory agencies that they serve. New laws, or regulations, new interpretations of existing laws or regulations, or changes in agency policy, including as a response to shifts in public opinion, or conditions imposed during the regulatory hearing process may affect our business in a number of ways, including the following:

- making it more difficult for us to raise our rates and, as a consequence, to recover our costs or earn our expected rates of return;
- changing the determination of the costs, or the amount of costs, that would be considered recoverable in rate cases;
- changing water quality or delivery service standards or wastewater collection, treatment and discharge standards with which we must comply;
- restricting our ability to terminate our services to customers who owe us money for services previously provided;
- requiring us to provide water services at reduced rates to certain customers;
- restricting our ability to sell assets or issue securities;
- changing regulatory benefits that we expected to receive when we began offering services in a particular area;
- changing or placing additional limitations on change in control requirements relating to any concentration of ownership of our common stock;
- making it easier for governmental entities to convert our assets to public ownership via eminent domain;
- restricting or prohibiting our extraction of water from rivers, streams, reservoirs or aquifers; and
- revoking or altering the terms of the certificates of public convenience and necessity (or similar authorizations) issued to us by state PUCs.

Any of these changes or any other changes in laws, regulations, judicial decisions or agency policies applicable to us may have an adverse effect on our business, financial condition, results of operations, cash flow and liquidity.

Table of Contents

Weather conditions, natural hazards, overuse of water supplies and competing uses may interfere with our sources of water, demand for water services and our ability to supply water to customers.

Our ability to meet the existing and future water demands of our customers depends on an adequate supply of water. As a general rule, sources of public water supply, including rivers, lakes, streams and groundwater aquifers are held in the public trust and are not owned by private interests. As such, we typically do not own the water that we use in our operations, and the availability of our water supply is established through allocation rights and passing-flow requirements set by governmental entities. Passing-flow requirements set minimum volumes of water that must pass through specified water sources, such as rivers and streams, in order to maintain environmental habitats and meet water allocation rights of downstream users. Allocation rights are imposed to ensure sustainability of major water sources and passing flow requirements are most often imposed on source waters from smaller rivers, lakes and streams. These requirements can change from time to time and adversely impact our water supply. Drought, overuse of sources of water, the protection of threatened species or habitats or other factors may limit the availability of ground and surface water.

Governmental restrictions on water use during drought conditions may also result in decreased use of water services, even if our water supplies are sufficient to serve our customers, which may adversely affect our financial condition and results of operations. Seasonal drought conditions that would impact our water services are possible across all of our service areas. However, these conditions are more prevalent in the Northeast and West where supply capacity is limited and per capita water demand is high. If a regional drought were to occur affecting our service areas and adjacent systems, governmental restrictions may be imposed on all systems within a region independent of the supply adequacy of any individual system. Following drought conditions, water demand may not return to pre-drought levels even after restrictions are lifted. Cool and wet weather may also reduce demand for water, thereby adversely affecting our financial condition, results of operations, cash flow and liquidity.

Service interruptions due to severe weather events are possible across all our service areas. These include winter storms and freezing conditions in our colder climate service areas, high wind conditions in our service areas known to experience tornados, earthquakes in our service areas known to experience seismic activity, high water conditions for our facilities located in or near designated flood plains, hurricane protection and response planning for our coastal service areas and severe electrical storms which are possible across all of our service areas. These weather events may affect the condition or operability of our facilities, limiting or preventing us from delivering water or wastewater services to our customers. Any interruption in our ability to supply water or to collect, treat and properly dispose of wastewater, or any costs associated with restoring service, could adversely affect our financial condition and results of operations. Furthermore, losses from business interruptions or damage to our facilities might not be covered by our insurance policies and such losses may make it difficult for us to secure insurance in the future at acceptable rates.

Declining residential per customer water usage may reduce our long-term revenues, financial condition and results of operations.

Increased water conservation, including through the use of more efficient household fixtures and appliances among residential consumers, combined with declining household sizes in the United States, has contributed to a trend of declining residential per customer water usage. Our Regulated Businesses are heavily dependent upon revenue generated from rates we charge to our residential customers for the volume of water they use. The rate we charge for our water is regulated by state PUCs and we may not unilaterally adjust our rates to reflect demand. Declining usage will have a negative impact on our long-term operating revenues if we are unable to secure rate increases or to grow our residential customer base to the extent necessary to offset the residential usage decline.

Risks associated with the collection, treatment and disposal of wastewater may impose significant costs.

The wastewater collection, treatment and disposal operations of our subsidiaries are subject to substantial regulation and involve significant environmental risks. If collection or sewage systems fail, overflow or do not operate properly, untreated wastewater or other contaminants could spill onto nearby properties or into nearby streams and rivers, causing damage to persons or property, injury to aquatic life and economic damages, which may not be recoverable in rates. This risk is most acute during periods of substantial rainfall or flooding, which are the main causes of sewer overflow and system failure. Liabilities resulting from such damage could adversely and materially affect our business, results of operations and financial condition. Moreover, in the event that we are deemed liable for any damage caused by overflow, our losses might not be covered by insurance policies, and such losses may make it difficult for us to secure insurance in the future at acceptable rates.

Our Regulated Businesses require significant capital expenditures to maintain infrastructure and expand our rate base and may suffer if we fail to secure appropriate funding to make investments, or if we suffer delays in completing major capital expenditure projects.

The water and wastewater utility business is capital intensive. In addition to our acquisition strategy, we invest significant amounts of capital to add, replace and maintain property, plant and equipment. In 2006, we invested $688.8 million in capital improvements and we expect to invest approximately $740 to $780 million in capital improvements in 2007. We expect the level of capital expenditures necessary to maintain the integrity of our systems to increase in the future. We fund these projects from cash generated from operations, borrowings under our revolving credit facility and commercial paper programs and the issuance of long-term debt and equity securities. We can provide no assurances that we will be able to access the debt and equity capital markets or do so on favorable terms.

Upon the consummation of the concurrent initial public offering, RWE will have certain registration rights with respect to future issuances of our equity securities and, subject to lock-up provisions described under Shares Eligible for Future Sale Lock-Up Agreements, intends to fully divest its ownership of American Water as soon as reasonably practicable, subject to market conditions. The registration rights agreement to be entered into with RWE will impose certain restrictions on our ability to issue equity securities in amounts beyond specified thresholds without RWE s consent. Future sales of our common stock by RWE, as well as the restrictions in the registration rights agreement, may make it more difficult or costly for us to raise additional equity in the future. Furthermore, if we are unable to raise sufficient equity, we can provide no assurances that we will be able to access the debt capital markets, or do so on favorable terms.

If we are unable to obtain sufficient capital, we may fail to maintain our existing property, plant and equipment, realize our capital investment strategies, meet our growth targets and successfully expand the rate base upon which we are able to earn future returns on our investment and a return of our investment. Even if we have adequate resources to make required capital expenditures, we face the additional risk that we will not complete our major capital expenditures on time, as a result of construction delays or other obstacles. Each of these outcomes could adversely affect our financial condition and results of operations. We also face the risk that after we make substantial capital expenditures, the rate increases granted to us by state PUCs may not be sufficient to recover our prudently incurred operating expenses and to allow us the opportunity to earn an appropriate rate of return on our invested capital and a return of our invested capital.

The failure of, or the requirement to repair, upgrade or dismantle, any of our dams may adversely affect our financial condition and results of operations.

We own a total of 99 dams. A failure of any of those dams could result in injuries and property damage downstream for which we may be liable. The failure of a dam would also adversely affect our ability to supply water in sufficient quantities to our customers and could adversely affect our financial condition and results of operations. Any losses or liabilities incurred due to a failure of one of our dams might not be covered by insurance policies or be recoverable in rates, and such losses may make it difficult for us to secure insurance in the future at acceptable rates.

We also are required from time to time to repair or upgrade the dams that we own. The cost of such repairs can be and has been material. We might not be able to recover such costs through rates. The inability to recover these higher costs or regulatory lag in the recovery of such costs can affect our financial condition, results of operations, cash flow and liquidity.

The federal and state agencies that regulate our operations may adopt rules and regulations requiring us to dismantle our dams. Federal and state agencies are currently considering rules and regulations that could require us to strengthen or dismantle one of our dams on the Carmel River in California due to safety concerns related to seismic activity. Any requirement to strengthen or dismantle this dam could result in substantial costs that may adversely affect our financial condition and results of operations. We are currently engaged in negotiations with federal and state agencies and local stakeholders on a plan to maintain our existing Carmel River dams or to share the costs of dismantling one of them with those federal and state agencies and local stakeholders. These negotiations could be delayed or abandoned.

Any failure of our network of water and wastewater pipes and water reservoirs could result in losses and damages that may affect our financial condition and reputation.

Our operating subsidiaries distribute water and wastewater through an extensive network of pipes and store water in reservoirs located across the United States. A failure of major pipes or reservoirs could result in injuries and property damage for which we may be liable. The failure of major pipes and reservoirs may also result in the need to shut down some facilities or parts of our network in order to conduct repairs. Such failures and shutdowns may limit our ability to supply water in sufficient quantities to our customers and to meet the water and wastewater delivery requirements prescribed by governmental regulators, including state PUCs with jurisdiction over our operations, and adversely affect our financial condition, results of operations, cash flow, liquidity and reputation. Any business interruption or other losses might not be covered by insurance policies or be recoverable in rates, and such losses may make it difficult for us to secure insurance in the future at acceptable rates.

Contamination of our sources of water could result in service interruptions and human exposure to hazardous substances and subject our subsidiaries to civil or criminal enforcement actions, private litigation and clean-up obligations.

Our water supplies are subject to contamination, including contamination from naturally-occurring compounds, chemicals in groundwater systems, pollution resulting from man-made sources, such as perchlorate and methyl tertiary butyl ether (MTBE), and possible terrorist attacks. In the event that our water supply is contaminated, we may have to interrupt the use of that water supply until we are able to substitute the supply of water from another water source, including, in some cases, through the purchase of water from a third-party supplier. In addition, we may incur significant costs in order to treat the contaminated source through expansion of our current treatment facilities, or development of new treatment methods. If we are unable to substitute water supply in a cost-effective manner, our financial condition, results of operations, cash flow, liquidity and our reputation may be adversely affected. We might not be able to recover costs associated with treating or decontaminating water supplies through rates, or such recovery may not occur in a timely manner. Moreover, we could be held liable for environmental damage as well as damages arising from toxic tort or other lawsuits or criminal enforcement actions or other consequences arising out of human exposure to hazardous substances in our drinking water supplies.

Our liquidity and earnings could be adversely affected by increases in our production costs, including the cost of chemicals, electricity, fuel or other significant materials used in the water and wastewater treatment process.

We incur significant production costs in connection with the delivery of our water and wastewater services. Our production costs are driven by inputs such as chemicals used to treat water and wastewater as well as electricity and fuel, which are used to operate pumps and other equipment used in water treatment and delivery and wastewater collection, treatment and disposal. We also incur production costs for waste disposal. For 2006,

Table of Contents

production costs accounted for 14.4% of our total operating costs. These costs can and do increase unexpectedly and in substantial amounts, as occurred in California during 2001 when the cost of electricity rose substantially.

Our Regulated Businesses might not be able to recover increases in the costs of chemicals, electricity, fuel, other significant inputs or waste disposal through rates, or such recovery may not occur in a timely manner. Our Non-Regulated Businesses may not be able to recover these costs in contract prices or other terms. The inability to recover these higher costs can affect our financial condition, results of operations, cash flow and liquidity.

Our reliance on third-party suppliers poses significant risks to our business and prospects.

We contract with third parties for goods and services that are essential to our operations, such as maintenance services, pipes, chemicals, electricity, water, gasoline, diesel and other materials. We are subject to substantial risks because of our reliance on these suppliers. For example:

- our suppliers may not provide raw materials that meet our specifications in sufficient quantities;
- our suppliers may provide us with water that does not meet applicable quality standards or is contaminated;
- our suppliers may face production delays due to natural disasters or strikes, lock-outs or other such actions;
- one or more suppliers could make strategic changes in the lines of products and services they offer; and
- some of our suppliers are small companies which are more likely to experience financial and operational difficulties than larger, well-established companies, because of their limited financial and other resources.

As a result of any of these factors, we may be required to find alternative suppliers for the raw materials and services on which we rely. Accordingly, we may experience delays in obtaining appropriate raw materials and services on a timely basis and in sufficient quantities from such alternative suppliers at a reasonable price, which could interrupt services to our customers and adversely affect our revenues, financial condition, results of operations, cash flow and liquidity.

Risks associated with potential acquisitions or investments may adversely affect us.

We will continue to seek to acquire or invest in additional regulated water or wastewater systems, including by acquiring systems in markets in the United States, where we do not currently operate our Regulated Businesses, and through tuck-ins. We will also continue to seek to enter into public/private partnerships, including O&M, military and design, build and operate, which we refer to as DBO, contracts and services that complement our businesses. These transactions may result in:

- incurrence of debt and contingent liabilities;
- failure to have or to maintain effective internal control over financial reporting;
- fluctuations in quarterly results;

- exposure to unknown risk and liabilities, such as environmental liabilities; and
- other acquisition-related expenses.

We may also experience difficulty in obtaining required regulatory approvals for acquisitions, and any regulatory approvals we obtain may require us to agree to costly and restrictive conditions imposed by regulators. Future sales of our common stock by RWE, as well as the restrictions in the registration rights agreement to be entered into with RWE, may make it more difficult or costly for us to raise additional equity to fund an acquisition or to issue shares as consideration in connection with an acquisition. We may not identify all

Table of Contents

significant risks when conducting due diligence for the transaction, and we could be exposed to potential liabilities for which we will not be indemnified. There may be difficulties integrating new businesses, including bringing newly acquired businesses up to the necessary level of regulatory compliance. The demands of identifying and transitioning newly acquired businesses or pursuing investment opportunities may also divert management s attention from other business concerns and otherwise disrupt our business. Any of these risks may adversely affect our financial condition, results of operations and cash flows.

We have recorded a significant amount of goodwill, and we may never realize the full value of our intangible assets causing us to record impairments that may negatively affect our results of operations.

Our total assets include substantial goodwill. At June 30, 2007, our goodwill totaled $2,962.6 million. The goodwill is associated primarily with the acquisition of American Water by an affiliate of RWE in 2003 and the acquisition of E Town Corporation in 2001, representing the excess of the purchase price the purchaser paid over the fair value of the net tangible and intangible assets acquired. Goodwill is recorded at fair value on the date of an acquisition and, in accordance with Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets, or SFAS No. 142, is reviewed annually or more frequently if changes in circumstances indicate the carrying value may not be recoverable. Annual impairment reviews are performed in the fourth quarter. We have been required to reflect, as required by SFAS No. 142 and other applicable accounting rules, a non-cash charge to operating results for goodwill impairment in the amounts of $192.9 million in 2004, $396.3 million in 2005 and $227.8 million in 2006. These amounts include impairments relating to discontinued operations.

Our annual goodwill impairment test is completed during the fourth quarter. We have processes to monitor for interim triggering events. During the third quarter of 2007, as a result of our debt being placed on review for a possible downgrade and the proposed RWE Divestiture, management determined at that time that it was appropriate to update its valuation analysis before the next scheduled annual test.

Based on this assessment, we are performing an interim impairment test and expect to record an impairment charge to goodwill to our Regulated Businesses in the amount of approximately $243.3 million in the third quarter of 2007. The decline was primarily due to a slightly lower long-term earnings forecast caused by updated customer demand and usage expectations and expectations for timing of capital expenditures and rate recovery.

We may be required to recognize additional impairments in the future, depending on, among other factors, a decline over a period of time in the valuation multiples of comparable water utilities, a decline in the market value of our common stock and its value relative to our book equity at the consummation of the concurrent initial public offering or a decline over a period of time of our stock price following the consummation of the concurrent initial public offering. A decline in our forecasted results in our business plan, such as changes in rate case results or capital investment budgets or changes in our interest rates may also result in an incremental impairment charge. Further recognition of impairments of a significant portion of goodwill would negatively affect our results of operations and total capitalization, the effect of which could be material and could make it more difficult for us to secure financing on attractive terms and maintain compliance with our debt covenants.

Our Regulated Businesses compete with other regulated utilities, as well as strategic and financial buyers, for acquisition opportunities, which may hinder our ability to grow our business.

We compete with other regulated utilities, as well as strategic and financial buyers, for acquisition opportunities, including tuck-ins. Our competitors may impede our growth by purchasing water utilities near our existing operations, thereby preventing us from acquiring them. Competing utilities and strategic and financial buyers have challenged, and may in the future challenge, our applications for new service territories. Our growth could be hindered if we are not able to compete effectively for new territories with other companies or strategic and financial buyers that have lower costs of operations or that can submit more attractive bids.

Table of Contents

The assets of our Regulated Businesses are subject to condemnation through eminent domain.

Municipalities and other government subdivisions have historically been involved in the provision of water and wastewater services in the United States, and organized movements may arise from time to time in one or more of the service areas in which our Regulated Businesses operate to convert our assets to public ownership and operation through the governmental power of eminent domain. Should a municipality or other government subdivision seek to acquire our assets through eminent domain, we may resist the acquisition. Contesting an exercise of condemnation through eminent domain may result in costly legal proceedings and may divert the attention of the affected Regulated Business s management from the operation of its business.

The last sale of one of our water and wastewater systems under threat of condemnation occurred in 2003 in California. On March 1, 2007, our subsidiary, California American Water Company, was served by the San Lorenzo Valley Water District with court papers seeking to condemn our water and wastewater system in Felton, California, which serves approximately 1,300 customers. While we are contesting the condemnation, we might not prevail. If a municipality or other government subdivision succeeds in acquiring the assets of one or more of our Regulated Businesses through eminent domain, there is a risk that we will not receive adequate compensation for the business, that we will not be able to keep the compensation, or that we will not be able to divest the business without incurring significant one-time charges.

In order to consummate the proposed RWE Divestiture, we and RWE were required to obtain approvals from thirteen state PUCs. There can be no guarantee that some state PUC approvals already granted to us will not be appealed, withdrawn, modified or stayed.

To consummate the proposed RWE Divestiture, we and RWE obtained regulatory approvals from state PUCs in 13 states. The state PUC approval obtained in Illinois has been appealed and the appeal period to challenge our state PUC approvals remains open in California, New York, New Jersey and Pennsylvania. Thus, there can be no guarantee that our state PUC approvals in those states will not be appealed. Moreover, some of our existing state PUC approvals may be withdrawn or altered in the future by the state PUCs since they retain authority to withdraw or modify their prior decisions. There also can be no guarantee that, in conjunction with an appeal or otherwise, a stay or other form of injunctive relief will not be granted by a state PUC or reviewing court.

In addition, two of the regulatory approvals that we and RWE obtained expire 24 months from the date of effectiveness of the registration statement for the concurrent initial public offering and another approval expires 36 months from that date. If RWE does not fully divest its ownership of American Water within 24 or 36 months of the effectiveness of the registration statement for the concurrent initial public offering, then we and RWE may be required to seek an extension of such approvals, as applicable, which process may result in delays, costs and the imposition of additional conditions on us or on RWE.

In order to obtain the state PUC approvals to consummate the proposed RWE Divestiture we were required to accept certain conditions and restrictions that could increase our costs.

Some of the regulatory approvals contain conditions and restrictions, including reporting obligations; obligations to maintain appropriate credit worthiness; restrictions on changes of control, prohibitions on the pass-through of our initial Sarbanes-Oxley Act compliance costs; prohibitions on the pass-through of costs of the Transactions; service quality and staffing level requirements; and the maintenance of specific collective bargaining agreements and retirement and certain other post employment benefit programs. These conditions and restrictions could increase our costs and adversely affect our business.

Table of Contents

Our Non-Regulated Businesses, through American Water (excluding its regulated subsidiaries), provide performance guarantees and other forms of financial security to our public-sector clients that could be claimed by our clients or potential clients if we do not meet certain obligations.

Under the terms of some of our indebtedness and some of our agreements with the municipalities and other governmental entities, which we serve pursuant to O&M contracts, American Water (excluding its regulated subsidiaries) provides guarantees of the performance of our Non-Regulated Businesses, including financial guarantees or deposits to ensure performance of certain obligations. At June 30, 2007, we had guarantees and deposits totaling approximately $511.0 million, and this amount is likely to increase if our Non-Regulated Businesses grow. The presence of these contingent liabilities on our balance sheet may adversely affect our financial condition and make it more difficult for us to secure financing on attractive terms. In addition, if the obligor on the guaranteed instrument fails to perform certain obligations to the satisfaction of the party that holds the guarantee, that party may seek to enforce the guarantee against us or proceed against the deposit. In that event, our financial condition, results of operations, cash flow and liquidity could be adversely affected.

We operate a number of water and wastewater systems under O&M contracts and face the risk that the owners of those systems, which will negatively affect us as the operators of the systems.

We operate a number of water and wastewater systems under O&M contracts. Pursuant to these contracts, we operate the system according to the standards set forth in the applicable contract, where it is generally the responsibility of the owner to undertake capital improvements. In some cases, we may not be able to convince the owner to make needed improvements in order to maintain compliance with applicable regulations. Although violations and fines incurred by water and wastewater systems may be the responsibility of the owner of the system under these contracts, those non-compliance events may reflect poorly on us as the operator of the system and damage our reputation, and in some cases, may result in liability to the same extent as if we were the owner.

Our Non-Regulated Businesses are party to long-term contracts to operate and maintain water and wastewater systems under which we may incur costs in excess of payments received.

Some of our Non-Regulated Businesses enter into long-term contracts pursuant to which they agree to operate and maintain a municipality s or other party s water or wastewater treatment and delivery facilities in exchange for an annual fee. Our Non-Regulated Businesses are generally subject to the risk that costs associated with operating and maintaining the facilities may exceed the fees received from the municipality or other contracting party. In addition, directly or through our non-regulated subsidiaries, we often guarantee our Non-Regulated Businesses obligations under those contracts. Losses under these contracts or guarantees may adversely affect our financial condition, results of operations, cash flow and liquidity.

We rely on our IT systems to assist with the management of our business and customer and supplier relationships, and a disruption of these systems could adversely affect our business.

Our IT systems are an integral part of our business, and a serious disruption of our IT systems could significantly limit our ability to manage and operate our business efficiently, which in turn could cause our business and competitive position to suffer and cause our results of operations to be reduced. We depend on our IT systems to bill customers, process orders, provide customer service, manage construction projects, manage our financial records, track assets, remotely monitor certain of our plants and facilities and manage human resources, inventory and accounts receivable collections. Our IT systems also allow us to purchase products from our suppliers and bill customers on a timely basis, maintain cost-effective operations and provide service to our customers. Our IT systems are vulnerable to damage or interruption from:

- power loss, computer systems failures and internet, telecommunications or data network failures;
- operator negligence or improper operation by, or supervision of, employees;
- physical and electronic loss of customer data or security breaches, misappropriation and similar events;

Table of Contents

- computer viruses;
- intentional acts of vandalism and similar events; and
- hurricanes, fires, floods, earthquakes and other natural disasters.

Such damages or interruptions may result in physical and electronic loss of customer or financial data, security breaches, misappropriation and similar events.

In addition, we may not be successful in developing or acquiring technology that is competitive and responsive to the needs of our business and we might lack sufficient resources to make the necessary investments in technology to allow us to continue to operate at our current level of efficiency.

Our indebtedness could affect our business adversely and limit our ability to plan for or respond to changes in our business, and we may be unable to generate sufficient cash flow to satisfy our liquidity needs.

As of June 30, 2007, after giving effect to the Transactions, our pro forma indebtedness was $5,391.1 million, and our working capital, defined as current assets less current liabilities, was in a deficit position. Our indebtedness could have important consequences, including:

- limiting our ability to obtain additional financing to fund future working capital or capital expenditures;
- exposing us to interest rate risk with respect to the portion of our indebtedness that bears interest at a variable rate;
- limiting our ability to pay dividends on our common stock or make payments in connection with our other obligations;
- likely requiring that a portion of our cash flow from operations be dedicated to the payment of the principal of and interest on our debt, thereby reducing funds available for future operations, acquisitions, dividends on our common stock or capital expenditures;
- limiting our ability to take advantage of significant business opportunities, such as acquisition opportunities, and to react to changes in market or industry conditions; and
- placing us at a competitive disadvantage compared to those of our competitors that have less debt.

In order to meet our capital expenditure needs, we may be required to make additional borrowings under our credit facilities or be required to issue new debt securities in the capital markets. We can provide no assurances that we will be able to access the debt capital markets or do so on favorable terms. If new debt is added to our current debt levels, the related risks we now face could intensify limiting our ability to refinance existing debt on favorable terms.

We will depend primarily on operations to fund our expenses and to pay the principal and interest on our outstanding debt. Our ability to meet our expenses thus depends on our future performance, which will be affected by financial, business, economic, competitive, legislative, regulatory and other factors beyond our control. If we do not have enough money to pay the principal and interest on our outstanding debt, we may be required to refinance all or part of our existing debt, sell assets, borrow additional funds or sell additional equity. If our business does not generate sufficient cash flow from operations or if we are unable to incur indebtedness sufficient to enable us to fund our liquidity needs, we may be unable to plan for or respond to changes in our business that would prevent us from maintaining or increasing our business and cause our operating results and prospects to be affected adversely.

Our failure to comply with restrictive covenants under our credit facilities could trigger prepayment obligations.

Our failure to comply with the restrictive covenants under our credit facilities could result in an event of default, which, if not cured or waived, could result in us being required to repay or refinance (on less favorable terms) these borrowings before their due date. If we are forced to repay or refinance (on less favorable terms) these borrowings, our results of operations and financial condition could be adversely affected by increased costs and rates. In 2007, we were not in compliance with reporting covenants contained in some of the debt agreements of our subsidiaries. Such defaults under the reporting covenants were caused by our delay in producing our quarterly and audited annual consolidated financial statements. We have obtained all necessary waivers under the agreements. We can provide no assurance that we will comply in the future with all our reporting covenants and will not face an event of default under our debt agreements, or that such default will be cured or waived.

Work stoppages and other labor relations matters could adversely affect our results of operations.

Currently, approximately 3,400 employees, or approximately 50% of our total workforce, are unionized and represented by 18 different unions. Approximately one-third of our 75 union collective bargaining agreements expire annually, with 24 agreements covering 803 employees scheduled to expire before the end of 2007. We might not be able to renegotiate labor contracts on terms that are favorable to us and negotiations or dispute resolutions undertaken in connection with our labor contracts could be delayed or become subject to the risk of labor actions or work stoppages. Labor actions, work stoppages or the threat of work stoppages and our failure to obtain favorable labor contract terms during renegotiations may all adversely affect our financial condition, results of operations, cash flow and liquidity.

We currently have material weaknesses in internal control over financial reporting. If we fail to remedy our material weaknesses or otherwise maintain effective internal control over financial reporting, we may not be able to report our financial results accurately or on a timely basis. Any inability to report and file our financial results in an accurate and timely manner could harm our business and adversely impact the trading price of our common stock.

After the consummation of the concurrent initial public offering, we will become a public company. As a public company, we will be required to comply with the Sarbanes-Oxley Act and other rules and regulations that govern public companies. In particular, we will be required to certify our compliance with Section 404 of the Sarbanes-Oxley Act for the year ended December 31, 2008, which will require us to perform system and process evaluation and testing of our internal control over financial reporting to allow management and our registered public accounting firm to report on the effectiveness of our internal control over financial reporting. Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with generally accepted accounting principles. However, since 2003, we have been an indirect wholly owned subsidiary of RWE, a stock corporation incorporated in the Federal Republic of Germany, and were not required to maintain a system of internal control consistent with the requirements of the SEC and the Sarbanes-Oxley Act, nor to prepare our own financial statements. As a public reporting company, we will be required, among other things, to maintain a system of effective internal control over financial reporting suitable to prepare our publicly reported financial statements in a timely and accurate manner, and also to evaluate and report on such system of internal control.

A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company s annual or interim financial statements will not be prevented or detected on a timely basis. In connection with the preparation of our consolidated financial statements as of December 31, 2006, we and our independent registered public accountants have identified the following material weaknesses in our internal control over financial reporting:

- Inadequate internal staffing and skills;
- Inadequate controls over financial reporting processes;
- Inadequate controls over month-end closing processes, including account reconciliations;

Inadequate controls over maintenance of contracts and agreements;

Inadequate controls over segregation of duties and restriction of access to key accounting applications; and

Inadequate controls over tax accounting and accruals.

We will need to allocate additional resources to enhance the quality of our staff and to remediate the deficiencies in our internal controls listed above.

Each of these weaknesses could result in a material misstatement of our annual or interim consolidated financial statements. Moreover, we cannot assure you that we have identified all, or that we will not in the future have additional, material weaknesses, any of which may subject us to additional regulatory scrutiny, and cause future delays in filing our financial statements and periodic reports with the SEC. Any such delays in the filing of our financial statements and periodic reports may result in a loss of public confidence in the reliability of our financial statements and sanctions imposed on us by the SEC. We believe that such misstatements or delays could negatively impact our liquidity, access to capital markets, financial condition and the market value of our common stock or cause a downgrade in the credit ratings of American Water or American Water Capital Corp., our finance subsidiary, referred to as AWCC. These material weaknesses contributed to our inability to comply with reporting covenants in our debt agreements and those of our subsidiaries, and could hinder our ability to comply with such covenants in the future if we are not successful in remediating such weaknesses.

Risks Related to the Equity Units

You will bear the entire risk of a decline in the price of American Water s common stock.

Although as a holder of corporate units or treasury units you will be the beneficial owner of the related applicable ownership interests in senior notes, treasury securities or the applicable ownership interests in the treasury portfolio, as the case may be, you do have an obligation to buy shares of American Water s common stock pursuant to the purchase contract that is a part of the corporate units and treasury units. On the purchase contract settlement date, unless you pay cash to satisfy your obligation under the purchase contracts or the purchase contracts are terminated due to our bankruptcy, insolvency or reorganization, (i) in the case of corporate units, either (x) the principal of the appropriate applicable ownership interests in the treasury portfolio when paid at maturity or (y) either the proceeds attributable to the applicable ownership interest in senior notes derived from the successful remarketing of the senior notes or, if no successful remarketing has occurred, the put price paid upon the automatic put of the senior notes to us, or (ii) in the case of treasury units, the principal of the related treasury securities when paid at maturity, will automatically be used to purchase a specified number of shares of American Water s common stock on your behalf.

The number of shares of American Water s common stock that you will receive upon the settlement of a purchase contract is not fixed but instead will depend on the average of the closing price per share of American Water s common stock on the 20 consecutive trading days ending on the third trading day immediately preceding the purchase contract settlement date, which we refer to as the applicable market value. There can be no assurance that the market value of common stock received by you on the purchase contract settlement date will be equal to or greater than the price per share paid by you for American Water s common stock. If the applicable market value of the common stock is less than $, the market value of the common stock issued to you pursuant to each purchase contract on the purchase contract settlement date (assuming that the market value is the same as the applicable market value of the common stock) will be less than the effective price per share paid by you for the common stock on the date of issuance of the equity units. Accordingly, you assume the entire risk that the market value of the common stock may decline and that, depending upon the extent of the decline, you could lose all or substantially all of your investment in the securities.

The opportunity for equity appreciation provided by an investment in the equity units is less than that provided by a direct investment in American Water s common stock.

Your opportunity for equity appreciation afforded by investing in the equity units is less than your opportunity for equity appreciation if you directly invested in American Water s common stock. This opportunity is less because the market value of the common stock to be received by you pursuant to the purchase contract on the purchase contract settlement date (assuming that the market value is the same as the applicable market value of the common stock) will only exceed the price per share paid by you for American Water s common stock on the purchase contract settlement date if the applicable market value of the common stock exceeds the threshold appreciation price (which represents an appreciation of % over the reference price). If the applicable market value of American Water s common stock exceeds the reference price but falls below the threshold appreciation price, you realize no equity appreciation of the common stock for the period during which you own the purchase contract. Furthermore, if the applicable market value of American Water s common stock equals or exceeds the threshold appreciation price, you would receive on the purchase contract settlement date only approximately % of the value of the shares of common stock you could have purchased with $50 at the initial public offering price of American Water s common stock in the concurrent initial public offering.

The trading prices for the corporate units and treasury units will be directly affected by the trading prices of American Water s common stock.

The trading prices of corporate units and treasury units in the secondary market will be directly affected by the trading prices of American Water s common stock, the general level of interest rates and our credit quality. It is impossible to predict whether the price of the common stock or interest rates will rise or fall. Trading prices of the common stock will be influenced by our operating results and prospects and by economic, financial and other factors. In addition, general market conditions, including the level of, and fluctuations in the trading prices of stocks generally, and sales of substantial amounts of common stock by us in the market after the offering of the equity units, or the perception that such sales could occur, could affect the price of American Water s common stock. Generally, a decline in the trading price of American Water s common stock would result in a corresponding decline in the trading prices of the corporate units and the treasury units. Fluctuations in interest rates may give rise to arbitrage opportunities based upon changes in the relative value of the common stock underlying the purchase contracts and of the other components of the equity units. Any such arbitrage could, in turn, affect the trading prices of the corporate units, treasury units, senior notes and American Water s common stock.

If you hold corporate units or treasury units, you will not be entitled to any rights with respect to American Water s common stock, but you will be subject to all changes made with respect to the common stock.

If you hold corporate units or treasury units, you will not be entitled to any rights with respect to American Water s common stock (including, without limitation, voting rights and rights to receive any dividends or other distributions on the common stock), but you will be subject to all changes affecting the common stock. You will only be entitled to rights on the common stock if and when we deliver shares of common stock in exchange for corporate units or treasury units on the purchase contract settlement date, or as a result of early settlement, as the case may be, and the applicable record date, if any, for the exercise of rights occurs after that date. For example, if an amendment is proposed to American Water s articles of incorporation or by-laws requiring stockholder approval and the record date for determining the stockholders of record entitled to vote on the amendment occurs prior to delivery of the common stock, you will not be entitled to vote on the amendment, although you will nevertheless be subject to any changes in the powers, preferences or special rights of American Water s common stock.

You may suffer dilution of the shares of common stock issuable upon settlement of the purchase contracts.

The number of shares of common stock that you are entitled to receive on the purchase contract settlement date or as a result of early settlement of a purchase contract is subject to adjustment for certain events arising from stock splits and combinations, cash or stock dividends and certain other actions by us that modify our capital structure. We will not adjust the number of shares of common stock that you are to receive on the purchase contract settlement date or as a result of early settlement of a purchase contract for other events, including offerings of common stock for cash by us or in connection with acquisitions. The purchase contract agreement does not restrict us from issuing additional common stock during the term of the purchase contracts, and we have no obligation to consider your interests for any reason. If American Water issues additional shares of common stock, it may materially and adversely affect the price of its common stock and, because of the relationship of the number of shares to be received on the purchase contract settlement date to the price of the common stock, such other events may adversely affect the trading price of the corporate units or treasury units. See Future sales of American Water s shares, or the perception by the market that future sales of American Water s shares may occur, could depress the market price of American Water s common stock.

You may have to pay taxes with respect to distributions on the common stock that you do not receive.

The number of shares of common stock that you are entitled to receive on the purchase contract settlement date or as a result of early settlement of a purchase contract is subject to adjustment for certain events arising from stock splits and combinations, stock dividends, cash dividends and certain other actions by us that modify our capital structure. See Description of the Purchase Contracts Anti-Dilution Adjustments. If the settlement rate is adjusted as a result of a distribution that is taxable to American Water s common stockholders, such as a cash dividend, you would be required to include an amount in income for federal income tax purposes, notwithstanding the fact that you do not actually receive such distribution. Non-U.S. holders of the equity units may, in certain circumstances, be deemed to have received a distribution subject to U.S. federal withholding tax requirements. See United States Federal Income Tax Consequences U.S. Holders Purchase Contracts Adjustment to Settlement Rate and Non-U.S. Holders Dividends.

The secondary market for the corporate units, treasury units or senior notes may be illiquid.

It is not possible to predict how corporate units, treasury units or senior notes will trade in the secondary market or whether the market will be liquid or illiquid. There is currently no secondary market for either the corporate units, treasury units or senior notes. We intend to apply to have the corporate units listed on the New York Stock Exchange under the symbol . If the treasury units or the senior notes are separately traded to a sufficient extent that applicable exchange listing requirements are met, we will try to list the treasury units or the senior notes on the same exchange as the corporate units. There can be no assurance as to the liquidity of any market that may develop for the corporate units, the treasury units or the senior notes, your ability to sell these securities or whether a trading market, if it develops, will continue. In addition, in the event a sufficient number of holders of corporate units were to convert their treasury units to corporate units or their corporate units to treasury units, as the case may be, the liquidity of corporate units or treasury units could be adversely affected. There can be no assurance that the corporate units will not be delisted from the New York Stock Exchange or that trading in the corporate units will not be suspended as a result of your election to create treasury units by substituting collateral, which could cause the number of corporate units to fall below the requirement for listing securities on the New York Stock Exchange.

The delivery of make-whole shares upon a cash merger early settlement may not adequately compensate you.

If a cash merger occurs and you exercise your merger early settlement right, you will have the right to accelerate and settle the purchase contract early at the settlement rate in effect immediately prior to the closing of the cash merger, plus an additional make-whole amount of shares (which amount we refer to as the make-whole shares) unless the price paid per share of our common stock in the cash merger is less than or equal to $ or more than $ (in each case, subject to adjustment). A description of how the make-whole shares will be determined is set forth under Description of the Purchase Contracts Early Settlement Upon Cash Merger Calculation of Make-Whole Shares. Although the make-whole shares are designed to compensate you for the lost value of your equity units as a result of certain types of mergers, this feature may not adequately compensate you for such loss.

We may defer contract adjustment payments.

We may, at our option and upon prior written notice to the holders of the equity units and the purchase contract agent, defer the payment of contract adjustment payments on the related purchase contracts forming a part of the equity units until no later than the purchase contract settlement date. However, deferred contract adjustment payments will accrue additional contract adjustment payments at the rate of % per year (compounded quarterly) until paid. If the purchase contracts are terminated due to our bankruptcy, insolvency or reorganization or are settled early, the right to receive contract adjustment payments and deferred contract adjustment payments, if any, will also terminate and, except in the case of a merger early settlement, you will not receive any accrued and unpaid contract adjustment payments.

The senior notes are structurally subordinated to all the obligations of our subsidiaries other than AWCC. AWCC s ability to service its debt is dependent on the performance of our other subsidiaries.

The senior notes will be issued by AWCC, our finance subsidiary. American Water has signed a support agreement with AWCC. The senior notes are not guaranteed by any of our subsidiaries and are the obligations only of AWCC and American Water, by virtue of the support agreement. Accordingly, the senior notes are structurally subordinated to the liabilities, including trade payables, lease commitments and moneys borrowed, of American Water s subsidiaries other than AWCC. American Water has no material assets or operations other than its equity interests in its subsidiaries, and AWCC has no material assets or operations except for its limited operations as a finance vehicle for our businesses. We expect that payments of interest and principal that AWCC makes on the senior notes (or that American Water makes pursuant to the support agreement) will be made only to the extent that our operating subsidiaries can distribute cash or other property to American Water and, through American Water, to AWCC.

Although the terms of the senior notes restrict our ability and the ability of our subsidiaries to incur certain liens and to enter into certain sale and leaseback transactions, the incurrence of other indebtedness or other liabilities by any of our subsidiaries is not prohibited in connection with the senior notes and could adversely affect our ability to pay our obligations on the senior notes. As of June 30, 2007, total liabilities of our subsidiaries other than AWCC were $5,002.3 million. As of June 30, 2007, the indebtedness of our subsidiaries other than AWCC, excluding intercompany liabilities and obligations of a type not required to be reflected on a balance sheet in accordance with generally accepted accounting principles, that would effectively have been senior to the senior notes, was approximately $1,982.8 million. We anticipate that from time to time our subsidiaries will incur additional debt and other liabilities. Any debt incurred by our subsidiaries other than AWCC will be structurally senior to the senior notes.

We have not agreed to any financial covenants in connection with the senior notes. Consequently, we are not required in connection with the senior notes to meet any financial tests, such as those that measure our working capital, interest coverage, fixed charge or net worth, in order to maintain compliance with the terms of the senior notes.

Our ability to service our obligations under the senior notes depends on our ability to receive cash distributions from our operating subsidiaries. There can be no assurance that we will continue to receive such distributions or, if they are received, that they will be in amounts similar to past distributions.

AWCC, the issuer of the senior notes, is our finance subsidiary and has no substantial assets. American Water has entered into a support agreement with AWCC pursuant to which it has agreed to pay to any debt investor or lenders of AWCC any principal or interest amounts due by AWCC to such debt investor or lender that AWCC fails to pay on a timely basis. Because substantially all of our operations are conducted through our subsidiaries other than AWCC, AWCC will not be able to make interest and principal payments on the senior notes (and American Water will not be able to fulfill its obligations under the support agreement) unless American Water receives sufficient cash distributions from its operating subsidiaries and contributes such distributions to AWCC. The distributions received from our operating subsidiaries might not permit AWCC or American Water to make required payments of interest and principal under the senior notes or pursuant to the support agreement, as applicable, on a timely basis, or at all.

Your rights to the pledged securities will be subject to our security interest.

Although you will be the beneficial owner of the applicable ownership interests in senior notes, treasury securities or applicable ownership interests in the treasury portfolio, as applicable, those securities will be pledged to us through the collateral agent to secure your obligations under the related purchase contracts. Thus, your rights to the pledged securities will be subject to our security interest. Additionally, notwithstanding the automatic termination of the purchase contracts, in the event that we become the subject of a case under the U.S. Bankruptcy Code, the delivery of the pledged securities to you may be delayed by the imposition of the automatic stay under Section 362 of the Bankruptcy Code and claims arising out of the senior notes, like all other claims in bankruptcy proceedings, will be subject to the equitable jurisdiction and powers of the bankruptcy court.

AWCC may redeem the senior notes upon the occurrence of a tax event.

AWCC has the option to redeem the senior notes, on not less than 30 days nor more than 60 days prior written notice, in whole but not in part at any time before the earlier of the date of a successful remarketing of the senior notes underlying the corporate units or the purchase contract settlement date, if a tax event occurs and continues under the circumstances described in this prospectus, which we call a tax event redemption. If AWCC exercises this option to redeem the senior notes, AWCC will pay the redemption price, as described herein, in cash to the holders of the senior notes. The redemption price payable to you as a holder of corporate units will be distributed to the collateral agent, who in turn will apply a portion of the redemption price to purchase the treasury portfolio on your behalf, and will remit the remainder of the redemption price, if any, to you, and the treasury portfolio will be substituted for the senior notes as collateral to secure your obligations under the purchase contracts related to the corporate units. If your senior notes do not underlie corporate units, you will receive the redemption payment directly. There can be no assurance as to the effect on the market price for the corporate units if we substitute the treasury portfolio as collateral in place of any senior notes so redeemed. A tax event redemption will be a taxable event to the holders of the senior notes. See United States Federal Income Tax Consequences Senior Notes Sale, Exchange or Other Disposition of Senior Notes.

The United States federal income tax consequences of the purchase, ownership and disposition of the equity units are unclear.

Although the Internal Revenue Service (the IRS) has issued a Revenue Ruling addressing the treatment of units similar to the equity units, no statutory, judicial or administrative authority directly addresses all aspects of the treatment of the equity units or instruments similar to the equity units for United States federal income tax purposes, and no assurance can be given that the conclusions in the Revenue Ruling would apply to the equity units. As a result, the United States federal income tax consequences of the purchase, ownership and disposition of equity units are not entirely clear. In addition, any gain on a disposition of a senior note or a corporate unit to the extent such gain is allocable to the applicable ownership interest in senior notes prior to the date six months after the interest rate on the senior notes is reset will generally be treated as ordinary interest income; thus, the ability to offset such interest income with a loss, if any, on a purchase contract may be limited. For additional tax-related risks, see United States Federal Income Tax Consequences in this prospectus.

The purchase contract and pledge agreement will not be qualified under the Trust Indenture Act and the obligations of the purchase contract agent are limited.

The purchase contract and pledge agreement between American Water and the purchase contract agent will not be qualified as an indenture under the Trust Indenture Act of 1939, and the purchase contract agent will not be required to qualify as a trustee under the Trust Indenture Act. Thus, you will not have the benefit of the protection of the Trust Indenture Act with respect to the purchase contract and pledge agreement or the purchase contract agent. The senior notes constituting a part of the corporate units will be issued pursuant to an indenture, which will be qualified under the Trust Indenture Act. Accordingly, if you hold corporate units, you will have the

Table of Contents

benefit of the protections of the Trust Indenture Act only to the extent applicable to the applicable ownership interests in senior notes included in the corporate units. The protections generally afforded the holder of a security issued under an indenture that has been qualified under the Trust Indenture Act include:

- disqualification of the indenture trustee for conflicting interests, as defined under the Trust Indenture Act;
- provisions preventing a trustee that is also a creditor of the issuer from improving its own credit position at the expense of the security holders immediately prior to or after a default under such indenture; and
- the requirement that the indenture trustee deliver reports at least annually with respect to certain matters concerning the indenture trustee and the securities.

You will be required to accrue original issue discount on the senior notes for United States federal income tax purposes.

Because of the manner in which the interest rate on the senior notes is reset, the senior notes should be classified as contingent payment debt instruments subject to the noncontingent bond method for accruing original issue discount for United States federal income tax purposes. Assuming that the senior notes are so treated, you will be required to accrue original issue discount on the senior notes or the applicable ownership interests in senior notes that are a component of the corporate units in your gross income on a constant yield-to-maturity basis, regardless of your usual method of tax accounting. For all accrual periods beginning before the earlier of the reset effective date and , 2010, the original issue discount that accrues on the senior notes will exceed the stated interest payments on the senior notes. For additional tax-related risks relating to the senior notes, see United States Federal Income Tax Consequences U.S. Holders Senior Notes in this prospectus.

Risks Related to American Water s Common Stock

There has been no prior public trading market for shares of American Water s common stock since our acquisition by RWE, and an active trading market may not develop following the completion of the concurrent initial public offering.

Since our acquisition of RWE in 2003, there has been no public market for American Water s shares. It is likely that the initial public offering price for American Water s shares will differ from the market price for the shares after the concurrent initial public offering. We cannot assure you that an active trading market for American Water s shares will develop. A significant portion of American Water s shares may not trade following the concurrent initial public offering because RWE will own approximately % of the shares after the offering (or approximately % of the shares if the underwriters option to purchase additional shares in such offering is exercised in full). If no trading market develops, securities analysts may not initiate or maintain research coverage of American Water, which could further depress the market for the shares. The price of American Water s shares could decline if one or more equity analysts downgrade its common stock or if those analysts issue other unfavorable commentary or cease publishing reports about American Water or its business. Furthermore, our operating results and prospects from time to time may be below the expectations of market analysts and investors. As a result, investors may not be able to sell their shares at or above the initial public offering price or at the time that they would like to sell.

The market price for American Water s common stock may be volatile, which could cause the value of your investment to decline.

The initial public offering price for the shares of American Water common stock being sold in the concurrent initial public offering will be determined by negotiations between the representatives of the underwriters and RWE and may not be indicative of prices that will prevail in the open market following such offering. You may not be able to resell your shares at or above the initial public offering price due to fluctuations in the market price of the common stock caused by changes in our operating performance or prospects and other factors, including broad market fluctuations. Some specific factors that may have a significant effect on the market price of American Water s common stock include:

- actual or anticipated fluctuations in our operating results or future prospects;
- the public s reaction to American Water s press releases, its other public announcements and its filings with the SEC;
- strategic actions by American Water or its competitors, such as acquisitions or restructurings;
- new laws or regulations or new interpretations of existing laws or regulations applicable to our business;
- changes in accounting standards, policies, guidance, interpretations or principles;
- adverse conditions in the financial markets or general economic conditions, including those resulting from war, incidents of terrorism and responses to such events;
- sales of common stock by American Water, RWE or members of American Water s management team; and
- changes in stock market analyst recommendations or earnings estimates regarding American Water s common stock, other comparable companies or the water services industry generally.

There has not been a public market for American Water s common stock since its acquisition by RWE in 2003. We cannot predict the extent to which investor interest will lead to the development of an active trading market on the New York Stock Exchange or otherwise or how liquid that market might become. If an active trading market does not develop, you may have difficulty selling any of our common stock that you buy. Consequently, you may not be able to sell your shares at prices equal to or greater to the initial public offering price in the concurrent initial public offering.

Future sales of American Water s shares, or the perception by the market that future sales of American Water s shares may occur, could depress the market price of American Water s common stock.

Future sales, or the perception of the availability for sale in the public market, of substantial amounts of American Water s common stock could adversely affect the prevailing market price of its common stock and could impair our ability to raise capital through future sales of equity securities at a time and price that we deem appropriate. Following the Transactions, there will be shares of American Water s common stock outstanding.

The shares of common stock sold by RWE in the concurrent initial public offering will be freely transferable without restriction or further registration under the Securities Act. The remaining shares of common stock owned by RWE will be restricted securities within the meaning of Rule 144 under the Securities Act but will be eligible for resale subject to applicable volume, manner of sale, holding period and other limitations of Rule 144 and the lock-up provisions described below. RWE has certain registration rights with respect to the common stock that they will retain following the concurrent initial public offering and, subject to the lock-up provisions described in the prospectus, intends to fully divest its ownership of American Water as soon as reasonably practicable, subject to market conditions.

In addition, the equity units are effectively exchangeable into up to freely tradable shares of American Water s common stock on the third anniversary of this offering. Following the consummation of the concurrent initial public offering, we intend to grant restricted stock units and stock options under our 2007 Omnibus Equity Compensation Plan, and are considering establishing an employee stock purchase plan, for which we would reserve shares of our common stock to be issued and sold thereunder.

Table of Contents

American Water, our executive officers and directors and RWE have agreed to a lock-up, meaning that, subject to specified exceptions, neither we nor they will sell any shares or engage in any hedging transactions without the prior consent of the representatives of the underwriters for 180 days after the date of this prospectus. Following the expiration of this 180-day lock-up period, all of the shares of American Water s common stock held by our executive officers and directors and by RWE will be eligible for future sale, subject to the applicable volume, manner of sale, holding period and other limitations of Rule 144.

We expect to pursue issuances of our common stock in order to meet our capital expenditure needs. We may also issue shares of American Water s common stock, or other securities, from time to time as consideration for future acquisitions and investments. The number of shares of our common stock or the number or aggregate principal amount, as the case may be, of other securities that we may issue may in turn be significant. To the extent such shares or other securities are issued in private banking transactions, we may also grant registration rights covering those shares or other securities in connection with any such acquisitions and investments. Any additional capital raised through the sale of our equity securities may dilute your percentage ownership in us. See Shares Eligible for Future Sale for a discussion of the shares of common stock that may be sold into the public market in the future.

You may never receive dividends on your investment in American Water s common stock, which may limit your returns.

American Water currently intends to declare and pay regular quarterly cash dividends on its common stock. See Dividend Policy. However, American Water is not legally or contractually required to pay dividends, and its board of directors may revise or discontinue its dividend policy at any time. In particular, American Water s dividend policy may change upon a change in control.

Our ability to pay dividends will depend on our ability to generate cash flow from operations in the future. This ability, to a certain extent, is subject to general economic, financial, competitive, regulatory and other factors that are beyond our control. In addition, American Water is a holding company with no substantial assets. Because substantially all of American Water s operations are conducted through subsidiaries, American Water will not be able to pay dividends unless it receives sufficient cash distributions from its operating subsidiaries. We cannot assure you, however, that our subsidiaries will generate sufficient cash flow from operations, or have sufficient surplus or net profits, as the case may be, to make cash contributions to us in an amount sufficient to enable us to pay our indebtedness, pay dividends or to fund our other liquidity needs. American Water s operating subsidiaries are subject to regulation by applicable state PUCs which may limit the ability of these subsidiaries to make distributions to American Water. Some of our debt agreements restrict our ability, subject to specified exceptions, to pay dividends. We cannot assure you that the agreements governing our future indebtedness will permit us to pay dividends on American Water s common stock. See Description of Certain Indebtedness. If American Water does not have sufficient cash to fund dividend payments, we would either reduce or eliminate dividends or rely on cash provided by financing activities to fund dividend payments, and such financing may or may not be available.

Our principal stockholder is in a position to affect our ongoing operations, corporate transactions and other matters, and its interests may conflict with or differ from your interests as a stockholder.

Upon the consummation of the concurrent initial public offering, RWE will own approximately % of American Water s common stock (or approximately % if the underwriters option to purchase additional shares is exercised in full). As a result, RWE effectively will be able to significantly influence the outcome on virtually all matters submitted to a vote of our stockholders, including the election of directors. So long as RWE continues to own a significant portion of the outstanding shares of American Water s common stock, it will continue to be able to significantly influence the election of our directors, subject to compliance with applicable NYSE requirements, our decisions, policies, management and affairs and corporate actions requiring stockholder approval, including the approval of transactions involving a change in control. The interests of RWE and its affiliates may not coincide with the interests of our other stockholders.

Table of Contents

Provisions in our amended and restated certificate of incorporation, our bylaws, Delaware law and the laws of the states in which we operate may inhibit or discourage a takeover attempt and negatively affect the value of your shares.

Provisions of our charter documents, the General Corporation Law of the State of Delaware, the state in which we are organized, and the laws of the states in which we operate could discourage potential acquisition proposals or make it more difficult for a third party to acquire control of our company, even if doing so might be beneficial to our stockholders. See Description of Capital Stock. Upon the consummation of the concurrent initial public offering, our amended and restated certificate of incorporation and bylaws will provide for various procedural and other requirements that could make it more difficult for stockholders to effect certain corporate actions, or may deter, delay or prevent a third party from acquiring us. These provisions will include:

- limitations on who may call special meetings of stockholders;
- the inability of stockholders to act by written consent;
- advance notice requirements for nominations for election to the board of directors and for stockholder proposals; and
- the authority of our board of directors to issue, without stockholder approval, shares of preferred stock with such terms as our board of directors may determine and to issue additional shares of American Water s common stock.

In addition, certain of the states in which we operate have enacted laws that require regulatory approval for the acquisition of control of regulated utilities. The threshold for a change in control is a fact-specific inquiry that varies by state. For instance, in some states any person acquiring more than 9.9% of American Water s common stock would need the prior approval of the applicable state PUC or a determination from such state PUC that control has not been acquired. In addition to ownership, other states may analyze the degree of influence or control an acquiror may exert over the company. Any person acquiring American Water s common stock in the concurrent initial public offering, through this offering of our equity units or in any other purchase of American Water s common stock in a quantity sufficient to trigger a change in control under state law would need the prior approval of the applicable state PUC. For example, in Kentucky, KY. Rev. Stat. Ann. §278.020 requires that no person may acquire control of American Water without obtaining necessary regulatory approvals.

These provisions may discourage acquisition proposals and may make it more difficult or expensive for a third party to acquire a majority of our outstanding voting stock or may delay, prevent or deter a merger, acquisition, tender offer or proxy contest, which may negatively affect our stock price.

Table of Contents

FORWARD-LOOKING STATEMENTS

We have made statements under the captions Summary, Risk Factors, Management s Discussion and Analysis of Financial Condition and Results of Operations, Business and in other sections of this prospectus that are forward-looking statements. In some cases, these forward-looking statements can be identified by words with prospective meanings such as intend, plan, estimate, believe, anticipate, expect, predict, p forecast, outlook, future, potential, continue, may, can, should and could and similar expressions. Forward-looking statements m among other things, our future financial performance, our growth strategies, our ability to repay debt, our ability to finance current operations and growth initiatives, trends in our industry, regulatory or legal developments or rate adjustments.

Forward-looking statements are predictions based on our current expectations and assumptions regarding future events. They are not guarantees of any outcomes, financial results or levels of performance, and you are cautioned not to place undue reliance upon them. These forward-looking statements are subject to a number of risks and uncertainties, and new risks and uncertainties of which we are not currently aware or which we do not currently perceive may arise in the future from time to time. Should any of these risks or uncertainties materialize, or should any of our expectations or assumptions prove incorrect, then our results may vary materially from those discussed in the forward-looking statements herein. Factors that could cause actual results to differ from those discussed in forward-looking statements include, but are not limited to, the factors discussed under the caption Risk Factors and the following factors:

- weather conditions, patterns or events, including drought or abnormally high rainfall;
- changes in general economic, business and financial market conditions;
- changes in laws, governmental regulations and policies, including environmental, health and water quality and public utility regulations and policies;
- the decisions of governmental and regulatory bodies, including decisions to raise or lower rates;
- the timeliness of regulatory commissions actions concerning rates;
- migration into or out of our service territories;
- our ability to obtain permits for expansion projects;
- changes in customer demand for, and patterns of use of, water, such as may result from conservation efforts;
- the availability of adequate and cost-effective supplies of chemicals, electricity, fuel, water and other raw materials that are needed for our operations;
- our ability to successfully acquire and integrate water and wastewater systems that are complementary to our operations and the growth of our business;
- our ability to manage the expansion of our business;

our ability to control operating expenses and to achieve efficiencies in our operations;

access to sufficient capital on satisfactory terms;

fluctuations in interest rates;

restrictive covenants in or changes to the credit ratings on our current or future debt that could increase our financing costs or affect our ability to borrow, make payments on debt or pay dividends;

changes in our credit rating;

changes in capital requirements;

the incurrence of impairment charges;

difficulty in obtaining insurance at acceptable rates and on acceptable terms and conditions;

Table of Contents

- ability to retain and attract qualified employees;
- cost overruns relating to improvements or the expansion of our operations; and
- civil disturbance or terrorist threats or acts or public apprehension about future disturbances or terrorist threats or acts.

Any forward-looking statements we make speak only as of the date of this prospectus. Except as required by law, we do not have any obligation, and we specifically disclaim any undertaking or intention, to update any forward-looking statements, whether as a result of new information, future events or otherwise.

INDUSTRY AND MARKET DATA

Unless otherwise indicated, information contained in this prospectus concerning the water and wastewater industry, its segments and related markets and our general expectations concerning such industry and its segments and related markets are based on management estimates. Such estimates are derived from publicly available information released by third-party sources, as well as data from our internal research and on assumptions made by us based on such data and our knowledge of such industry and markets, which we believe to be reasonable. We have estimated the number of people served by our water and wastewater systems (i) by multiplying the number of residential water and wastewater connections by average people per household based on 2000 United States Census data by state (average people per household varies by state but is generally between 2.4 to 3.0 individuals per household); (ii) by adjusting for some other customer classes, including commercial customers, and for bulk water sales and (iii) by reconciling drinking water and wastewater connections to avoid double counting population served where the same user has both drinking water and wastewater service. In some instances, population estimates for our Non-Regulated Businesses are based on either (i) specific population estimates from the client or (ii) population estimates based on the average volume of water processed by the applicable facilities. While we are not aware of any misstatements regarding the industry or similar data presented herein, such data involve risks and uncertainties and are subject to change based on various factors, including those discussed under the heading Risk Factors in this prospectus.

Table of Contents

USE OF PROCEEDS

We estimate that we will receive net proceeds from the sale of equity units in this offering of $500.0 million, after deducting expenses and underwriting discounts and commissions. We intend to use a portion of the net proceeds from this offering of equity units to fund the repayment of approximately $479.9 million of RWE redemption notes, with the balance of the net cash proceeds of approximately $4.3 million to be used for general corporate purposes. The RWE redemption notes bear interest equal to LIBOR plus 0.225% per annum, mature on March 20, 2009 and were used to fund the partial early redemption of $1,750.0 million of preferred stock held by RWE.

This offering of equity units is contingent upon the concurrent initial public offering described below.

Table of Contents

COMMON STOCK OFFERING

Concurrently with this offering of equity units, RWE, through its direct wholly owned subsidiary Thames Water Aqua Holdings GmbH, will sell, by means of a separate prospectus, shares of American Water s common stock, subject to customary closing conditions.

RWE estimates that it will receive net proceeds from that sale of American Water s common stock of $, after deducting expenses and underwriting discounts and commissions.

DIVIDEND POLICY

We intend to pay quarterly cash dividends on our common stock at an initial rate of $ per share per annum. The first such dividend will be declared and paid in the first quarter following the completion of the concurrent initial public offering. The declaration, payment and amount of future dividends to holders of our common stock will be at the discretion of our board of directors and will depend on many factors, including our financial condition and results of operations, liquidity requirements, capital requirements of our subsidiaries, legal requirements, regulatory constraints and other factors deemed relevant by our board of directors.

American Water is a holding company with no significant business operations of its own. All of our business operations are conducted through our subsidiaries. Dividends and loans from, and cash generated by, our subsidiaries will be our principal sources of cash to repay indebtedness, fund operations and pay dividends. Accordingly, our ability to pay dividends to our stockholders will depend on the earnings and distributions of funds from our subsidiaries. See Risk Factors Risks Related to American Water s Common Stock To pay dividends at intended levels, we will require a significant amount of cash. Our ability to generate cash depends on many factors beyond our control, including the ability to receive cash distributions from our subsidiaries. We may not receive sufficient distributions from our subsidiaries to pay dividends with respect to shares of American Water s common stock.

Table of Contents

CAPITALIZATION

The following table sets forth our cash and cash equivalents and capitalization as of June 30, 2007 on an actual basis and on a pro forma basis to give effect to the Transactions as if they had occurred on June 30, 2007.

You should read this table in conjunction with, and this table is qualified in its entirety by reference to, the sections in this prospectus entitled Summary Historical Consolidated and Unaudited Pro Forma Financial Data, Use of Proceeds, Unaudited Pro Forma Condensed Consolidated Financial Information, Selected Historical Consolidated Financial Data, Management s Discussion and Analysis of Financial Condition and Results of Operations, and our consolidated financial statements and the notes thereto included elsewhere in this prospectus.

	As of June 30, 2007 (dollars in thousands)	
	Historical	Pro forma
Cash and cash equivalents	$ 51,445	$ 55,719
Short-term debt		
RWE notes(1)	141,000	
Short-term debt	167	167
Total short-term debt	141,167	167
Long-term debt of American Water		
Redeemable preferred stock(2)	1,750,000	
Long-term debt of AWCC		
Private activity bonds and government funded debt	86,860	86,860
Senior notes	1,212,000	1,212,000
New senior notes(3)		1,500,000
RWE notes(4)	81,000	
Equity units (5)		500,000
Long-term debt of other subsidiaries		
Private activity bonds and government funded debt	1,126,493	1,126,493
Mortgage bonds	802,840	802,840
Senior notes	53,500	53,500
Redeemable preferred stock at redemption value (6)	24,856	24,856
Notes payable and other	3,859	3,859
Unamortized debt discount, net	80,545	80,545
Total long-term debt	5,221,953	5,390,953
Total debt	5,363,120	5,391,120
Equity		
Common stockholders equity(7)(8)	4,520,149	4,484,793
Preferred stock without mandatory redemption requirements	4,568	4,568
Total equity	4,524,717	4,489,361
Total capitalization including short-term debt and current portion of long-term debt	$ 9,887,837	$ 9,880,481

(1) In connection with the Refinancing, we will repay $141.0 million of short-term indebtedness owed to RWE.

(2) In connection with the Refinancing, on September 20, 2007, we redeemed $1,750.0 million of our preferred stock.

(3) In connection with the Refinancing, AWCC will issue $1,500.0 million of new senior notes.

(4) In connection with the Refinancing, we will repay $81.0 million of long-term indebtedness owed to RWE.

(5) In connection with the Refinancing, AWCC is hereby issuing approximately $500.0 million of equity units.

(6) Includes current portion of redeemable preferred stock.

(7) Does not include the common stock issuable upon settlement of the purchase contract included in the equity units being offered hereby.
(8) Does not include the approximately $243.3 million goodwill impairment we expect to record in the third quarter of 2007 or the $150.0 million equity contribution from RWE on September 27, 2007.

Table of Contents

RATIO OF EARNINGS TO COMBINED FIXED CHARGES AND PREFERRED DIVIDENDS

American Water and AWCC s ratio of earnings to combined fixed charges and preferred dividends for each of the periods indicated is as follows:

For purposes of calculating the ratio of earnings to combined fixed charges and preferred dividends, earnings consists of income (loss) from continuing operations before income taxes including the effect of allowance for funds used during construction, referred to as AFUDC, plus fixed charges. Fixed charges consist of interest expense, amortization of debt issuance costs, interest on mandatory redeemable preferred stock, and a portion of rent expense that management believes is representative of the interest component of rental expense. Fixed charges have not been reduced for the effect of AFUDC.

The ratio of earnings to combined fixed charges and preferred dividends was less than 1.00x for the periods indicated in the table below.

	For the Year Ended December 31,					For the Six Months Ended
	2002(1)	2003	2004	2005	2006	June 30, 2007
American Water	(Predecessor)					
Ratio of Earnings to Combined Fixed Charges and Preferred Dividends(2)		1.35	1.38			1.57
Pro Forma Ratio of Earnings to Combined Fixed Charges and Preferred Dividends(2)						1.57
AWCC						
Ratio of Earnings to Combined Fixed Charges and Preferred Dividends	1.00	1.00	1.00	1.00	1.00	1.00
Pro Forma Ratio of Earnings to Combined Fixed Charges and Preferred Dividends					1.00	1.00

(1) Derived from the consolidated financial statements of Thames Water Holdings, Incorporated, which principally reflect the historical financial data of Elizabethtown Water Company.

(2) For the years ended December 31, 2002, 2005 and 2006 earnings was insufficient to cover fixed charges and there was a deficiency of $149.5 million, $224.3 million and $109.1 million, respectively. On a pro forma basis after giving effect to the Transactions earnings would have been insufficient to cover fixed charges and there would have been a deficiency of $42.8 million for the year ended December 31, 2006.

48

Table of Contents

UNAUDITED PRO FORMA CONDENSED CONSOLIDATED FINANCIAL INFORMATION

The following unaudited pro forma condensed consolidated financial information have been developed by applying pro forma adjustments to the historical audited and unaudited consolidated financial statements of American Water appearing elsewhere in this prospectus. See the explanatory note to the unaudited pro forma condensed consolidated financial statements. The unaudited pro forma condensed consolidated statements of operations give effect to the Transactions as if they had occurred on January 1, 2006. The unaudited pro forma condensed consolidated balance sheet gives effect to the Transactions (other than the non-cash equity contributions to the Company by RWE, which are each reflected in the historical balance sheet) as if they had occurred on June 30, 2007. The Transactions consist of the following:

- The Merger, comprising:
  - The merger of Thames US Holdings into American Water with American Water being the surviving entity.
- The Refinancing, comprising:
  - The non-cash equity contribution to the Company by RWE of $1,194.5 million of debt of our subsidiaries held by RWE on December 15, 2006, the non-cash equity contribution to the Company by RWE of $100.0 million of debt of our subsidiaries held by RWE on March 29, 2007 and the $550.0 million cash equity contribution to the Company by RWE on March 29, 2007, which was used to pay down $232.5 million of short-term debt and the remainder used for general working capital purposes;
  - The $1,750.0 million issuance of RWE redemption notes on September 20, 2007, which was used to fund the early redemption of $1,750.0 million of preferred stock held by RWE;
  - The issuance of approximately $1,500.0 million aggregate principal amount of new senior notes, less issuance costs, which will fund the repayment of $1,270.1 million aggregate principal amount of RWE redemption notes and $222.0 million (including after tax gains of $1.3 million) aggregate principal amount of RWE Notes; and
  - The issuance of approximately $500.0 million of equity units, less issuance costs, to fund the repayment of approximately $479.9 million of RWE redemption notes, with the balance of the net cash proceeds of approximately $4.3 million to be used for general corporate purposes.
- The -for- split of common stock effected prior to this offering.

Upon completion of the concurrent initial public offering the Company expects to pay approximately $2.8 million in completion bonuses to various key members of management. As of June 30, 2007, approximately $2.1 million has been accrued, as a portion of the completion bonuses are not contingent on the successful completion of the offering and may be paid as cash bonuses. The unaccrued portion of the completion bonuses has not been reflected in the unaudited pro forma condensed consolidated financial information.

The unaudited pro forma adjustments and financial information do not include the approximately $243.3 million goodwill impairment we expect to record in the third quarter of 2007 or the $150.0 million equity contribution from RWE on September 27, 2007.

Assumptions underlying the pro forma adjustments are described in the accompanying notes, which should be read in conjunction with these unaudited pro forma condensed consolidated financial statements.

The unaudited pro forma adjustments and financial information:

are based upon available information and certain assumptions that we believe are reasonable under the circumstances;

are presented for informational purposes only;

do not purport to represent what our results of operations or financial condition would have been had the Transactions actually occurred on the dates indicated; and

Table of Contents

do not purport to project our results of operations or financial condition for any future period or as of any future date.

The unaudited pro forma condensed consolidated financial statements should be read in conjunction with the information contained in Use of Proceeds, Capitalization, Selected Historical Consolidated Financial Data, Management s Discussion and Analysis of Financial Condition and Results of Operations and the consolidated financial statements and related notes thereto appearing elsewhere in this prospectus. All pro forma adjustments and their underlying assumptions are described more fully in the notes to our unaudited pro forma condensed consolidated financial statements.

Table of Contents

American Water Works Company, Inc. and Subsidiary Companies

Unaudited Pro Forma Condensed Consolidated Statement of Operations

For the Year Ended December 31, 2006

	Historical	Pro forma adjustments	Pro forma
	(dollars in thousands, except for share and per share amounts)		
Operating revenues	$ 2,093,067	$	$ 2,093,067
Operating expenses			
Operation and maintenance	1,174,544	1,700 (A)	1,176,244
Depreciation and amortization	259,181		259,181
General taxes	185,065		185,065
Loss (gain) on sale of assets	79		79
Impairment charges	221,685		221,685
Total operating expenses, net	1,840,554	1,700	1,842,254
Operating income (loss)	252,513	(1,700)	250,813
Other income (deductions)			
Interest	(365,970)	(4,370)(B)	(297,067)
		74,676 (C)	
		(1,403)(H)	
Amortization of debt expense	(5,062)	(968)(B)	(6,030)
Other, net	9,581		9,581
Total other income (deductions)	(361,451)	67,935	(293,516)
Income (loss) from continuing operations before income taxes	(108,938)	66,235	(42,703)
Provision for income taxes	46,912	26,194 (E)	73,106
Income (loss) from continuing operations	$ (155,850)	$ 40,041	$ (115,809)
Unaudited pro forma earnings per share:			
Basic	$ (155,850)		
Diluted	$ (155,850)		
Weighted average shares used in calculating earnings per share:			
Basic	1,000	(F)	
Diluted	1,000	(G)	

See accompanying notes to the Unaudited Pro Forma Condensed Consolidated Financial Statements.

Table of Contents

American Water Works Company, Inc. and Subsidiary Companies

Unaudited Pro Forma Condensed Consolidated Statement of Operations

For the Six Months Ended June 30, 2007

	Historical	Pro forma adjustments	Pro forma
	(dollars in thousands, except for share and per share amounts)		
Operating revenues	$ 1,027,277	$	$ 1,027,277
Operating expenses			
Operation and maintenance	581,999	510 (A)	582,509
Depreciation and amortization	132,764		132,764
General taxes	93,819		93,819
Loss (gain) on sale of assets	(6,113)		(6,113)
Impairment charges			
Total operating expenses, net	802,469	510	802,979
Operating income (loss)	224,808	(510)	224,298
Other income (deductions)			
Interest	(142,970)	(2,203)(B)	(141,759)
		4,116 (C)	
		(702)(H)	
Amortization of debt expense	(2,397)	(484)(B)	(2,881)
Other, net	7,351		7,351
Total other income (deductions)	(138,016)	727	(137,289)
Income (loss) from continuing operations before income taxes	86,792	217	87,009
Provision for income taxes	34,378	85 (E)	34,463
Income (loss) from continuing operations	$ 52,414	$ 132	$ 52,546
Unaudited pro forma earnings per share:			
Basic	$ 52,414		
Diluted	$ 52,414		
Weighted average shares used in calculating earnings per share:			
Basic	1,000	(F)	
Diluted	1,000	(G)	

See accompanying notes to the Unaudited Pro Forma Condensed Consolidated Financial Statements.

Table of Contents

American Water Works Company, Inc. and Subsidiary Companies

Unaudited Pro Forma Condensed Consolidated Balance Sheet

June 30, 2007

	Historical	Pro forma adjustments	Pro forma
		(dollars in thousands)	
ASSETS			
Property, plant and equipment			
Utility plant at original cost, net of accumulated depreciation	$ 8,806,066	$	$ 8,806,066
Nonutility property, net of accumulated depreciation	109,525		109,525
Total property, plant and equipment	8,915,591		8,915,591
Current assets			
Cash and cash equivalents	51,445	4,274 (B)(I)	55,719
Other current assets	440,550		440,550
Total current assets	491,995	4,274	496,269
Regulatory and other long-term assets			
Goodwill	2,962,564		2,962,564
Other regulatory and other long-term assets	701,435	12,300 (D)	713,735
Total regulatory and other long-term assets	3,663,999	12,300	3,676,299
TOTAL ASSETS	$ 13,071,585	$ 16,574	$ 13,088,159
CAPITALIZATION & LIABILITIES			
Capitalization			
Common stockholders equity	$ 4,520,149	$ 1,346 (I) (23,389)(H) (13,653)(D) 340 (J)	$ 4,484,793
Preferred stock without mandatory redemption requirements	4,568		4,568
Long-term debt			
Long-term debt	3,335,579	(81,000)(I)	3,254,579
Redeemable preferred stock at redemption value	1,774,299	(1,750,000)(I)	24,299
New senior notes		1,500,000 (B)	1,500,000
Equity units		500,000 (B)	500,000
Total capitalization	9,634,595	133,644	9,768,239

Current liabilities			
Short-term debt and current portion of long-term debt	253,242	(141,000)(I)	112,242
Other current liabilities	373,216	881 (E) 4,425 (E)	378,522
Total current liabilities	626,458	(135,694)(I)	490,764
Total regulatory and other long-term liabilities	2,031,085	(4,425)(E) 23,389 (H) (340)(J)	2,049,709
Contributions in aid of construction	779,447		779,447
TOTAL CAPITALIZATION AND LIABILITIES	$ 13,071,585	$ 16,574	$ 13,088,159

See accompanying notes to the Unaudited Pro Forma Condensed Consolidated Financial Statements.

Table of Contents

American Water Works Company, Inc. and Subsidiary Companies

Notes to the Unaudited Pro Forma Condensed Consolidated Financial Statements

Explanatory Note: On September 28, 2007, Thames US Holdings was merged with and into American Water, with American Water as the surviving entity. American Water is an indirect wholly owned subsidiary of RWE. The historical consolidated financial statements of American Water represent the consolidated results of the Company, formerly issued under the name Thames Water Aqua US Holdings, Inc. and Subsidiary Companies.

(A) Reflects the granting of of unvested stock options and restricted stock units to our employees in conjunction with this offering. The awards will be issued under the American Water 2007 Omnibus Equity Compensation Plan and will be recorded as equity awards. The awards vest over a 3-year period commencing January 1, 2007 and unvested stock options and restricted stock units are expected to vest over the three-year period based on our assessment of the probability of achieving performance conditions. The grant date value of the stock options at issuance was using the following assumptions in a Black-Scholes model: Exercise Price, Expected Term, Discount Rate, Volatility, Dividend Yield.

(B) The sources and uses of funds in connection with the Refinancing and the related impact on interest expense related to the Transactions are summarized below, which are defined and further discussed elsewhere in this prospectus.

	Principal	Rate	Interest expense 12 months	Interest expense 6 months	Debt expense amortization 12 months	Debt expense amortization 6 months
			(dollars in thousands)			
SOURCES:						
RWE redemption notes(1)	$ 1,750,000	5.72%				
New senior notes(1)	1,500,000	6.00%(2)				
Equity units(1)	500,000	6.00%(2)				
Total sources	$ 3,750,000		$ 120,000	$ 60,000		
USES:						
Redeemable preferred stock(1)	$ 1,750,000		$ (103,250)	$ (51,625)		
RWE redemption notes(1)	1,750,000					
RWE notes(1)	219,773		(12,380)	(6,172)		
Financing costs	25,953				($ 968)	($ 484)
Total	3,745,226		(115,630)	(57,797)	(968)	(484)
Net source (use)	$ 4,274		$ 4,370	$ 2,203	($ 968)	($ 484)

(1) The issuance of $1,750.0 million of RWE redemption notes on September 20, 2007 was used to fund the early redemption of $1,750.0 million of preferred stock held by RWE. $1,270.1 million of the proceeds of the new senior notes and $479.9 million of the proceeds of the equity units will be used to fund the early repayment of the RWE redemption notes. $219.8 million of the proceeds of the new senior notes will be used to fund the repayment of $222.0 million (including after tax gains of $1.3 million, net of $0.9 million of tax) of RWE notes.

(2) Reflects the assumed blended interest rates in the case of the new senior notes and the notes associated with the equity units. A $^{1}/8$% change to the assumed interest rates would impact earnings before tax by approximately $2.5 million for the year ended December 31, 2006 and $1.3 million for the six months ended June 30, 2007.

(C) Reflects the non-cash equity contribution to the Company by RWE of $1,194.5 million of debt of our subsidiaries held by RWE on December 15, 2006, the non-cash equity contribution to the Company by RWE of $100.0 million of debt of our subsidiaries held by RWE and the $550.0 million of cash equity contribution to the Company by RWE on March 29, 2007. The cash was used to pay down $232.5 million of short-term debt with the remainder used for general working capital purposes.

Table of Contents

The resulting reduction in interest expense is computed as follows:

	RWE Notes	RWE Notes	Revolver (dollars in thousand)	Commercial Paper	Total
Principal redemption	$ 1,194,454	$ 100,000	$ 232,500	$ 232,500	
Calculated effective rate	4.89%	4.00%	5.30%	5.44%	
Reduction in interest expense for the year ended December 31, 2006	$ 58,353	$ 4,000	$ 12,323		$ 74,676
Reduction in interest expense for the six months ended June 30, 2007		$ 989	(2)	$ 3,127(1)	$ 4,116

(1) Reflects actual interest accrued from January 1, 2007 to March 29, 2009.

(2) The revolving credit facility was fully paid as of December 31, 2006.

(D) Reflects issuance costs that are expected to total $26.0 million, of which $13.7 million relating to the equity units has been reflected as a reduction to additional paid in capital, and $12.3 million associated with new senior notes (including $10.1 million with respect to the new senior notes and $2.2 million related to the notes associated with the equity units) has been reflected as other assets and will be amortized over the respective terms of each of the new notes.

(E) Represents the reduction in income tax expense resulting from the Transactions at the estimated blended tax rate of 39.6%. The deferred tax liability of $4.4 million associated with the preferred stock dividend was reclassified from long-term to short-term liabilities, and the $0.9 million estimated tax expense on the gains from early extinguishment of debt is reflected as a current liability.

(F) The number of common shares used to compute pro forma basic earnings per common share is , which is the number of shares of American Water s common stock assumed to be outstanding on the issuance date.

(G) The number of shares used to compute pro forma diluted earnings per share will be based on the number of shares of American Water s common stock described in (F) above, plus the potential dilution that could occur if restricted stock units granted under the American Water 2007 Omnibus Equity Compensation Plan were exercised or converted into common stock. The number of shares used in computing pro forma diluted earnings per share have been adjusted to reflect number of restricted units assumed to have been issued.

(H) The equity units have an assumed overall annual payment rate of %. The assumed interest rate on the underlying notes is % and the remainder is attributable to the contract adjustment payments, which includes imputed interest of $1.4 million (which is not disclosed in footnote (B) above calculated on the basis of $23.4 million present value of the obligation to make contract adjustment payments and the estimated interest rate of 6%). The estimated present value of the obligation to make contract adjustment payments of $23.4 million is recorded as a long-term liability with a corresponding reduction of additional paid-in capital.

(I) Reflects the repurchase of RWE notes, the issuance and repayment of the RWE redemption notes, the issuance of equity units, the issuance of senior notes and the early redemption of preferred stock. The proceeds from the new senior notes will be used to fund the repayment of

$222.0 million (including after tax gains of $1.3 million) aggregate principal amount of RWE notes and to fund the repayment of $1,270.1 million of RWE redemption notes with the remaining net proceeds to be used for general corporate purposes. The gain of $1.3 million, after income taxes, on the early extinguishment of the RWE notes is calculated as the difference between the assumed interest rate of the 10-year tranche of the new senior notes and the weighted-average interest rate on the RWE notes. The gain has been recorded as a capital contribution from RWE.

(J) Reflects the adjustment of the restricted stock units from liability-classified awards to equity-classified awards as of the completion of this offering resulting in a reclassification of $0.3 million of current liabilities to additional paid-in capital.

Table of Contents

SELECTED HISTORICAL CONSOLIDATED FINANCIAL DATA

The following table presents our selected historical consolidated financial data at the dates and for the periods indicated. The statements of operations data for the years ended December 31, 2004, 2005, and 2006 and the balance sheet data as of December 31, 2005 and 2006 have been derived from our audited consolidated financial statements included elsewhere in this prospectus. The historical financial data as of December 31, 2004 have been derived from our audited consolidated financial statements not included in this prospectus. The financial data as of June 30, 2006 and 2007 and for the six months ended June 30, 2006 and 2007 have been derived from our unaudited interim consolidated financial statements included elsewhere in this prospectus. See footnote 1 to the table below. Operating results for the six months ended June 30, 2006 and 2007 have been prepared on a basis consistent with our audited consolidated financial statements and reflect all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of the financial position and results for the periods presented. The results of any interim period are not necessarily indicative of the results that may be expected for any other interim period or for the entire fiscal year. The financial data as of and for the year ended December 31, 2002 have been derived from the consolidated financial statements of Thames Water Holdings, Incorporated, which we refer to as Predecessor, the statement of operation for the year ended December 31, 2003, and the financial data as of December 31, 2003 and 2004 have been derived from our historical financial statements, in each case, which are not included in this prospectus.

Our historical consolidated financial data are not necessarily indicative of our future performance or what our financial position and results of operations would have been if we had operated as a separate, stand-alone entity during the periods shown. This financial data should be read in conjunction with, and is qualified in its entirety by reference to, the information in the section in this prospectus entitled Summary Historical Consolidated and Unaudited Pro Forma Financial Data , Use of Proceeds , Capitalization , Unaudited Pro Forma Condensed Consolidated Financial Information , Management s Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the notes thereto included elsewhere in this prospectus.

	For the years ended December 31,					For the six months ended June 30,	
	2002(1) (Predecessor) (unaudited)	2003 (unaudited)	2004	2005	2006	2006 (unaudited)	2007 (unaudited)
	(dollars in thousands, except for share and per share data)						
Statement of operations data(2):							
Operating revenues	$ 198,835	$ 1,890,291	$ 2,017,871	$ 2,136,746	$ 2,093,067	$ 1,007,691	$ 1,027,277
Operating expenses							
Operation and maintenance	99,571	1,089,071	1,121,970	1,201,566	1,174,544	562,072	581,999
Depreciation and amortization	20,659	210,588	225,260	261,364	259,181	128,728	132,764
General taxes	24,480	164,677	170,165	183,324	185,065	94,756	93,819
Loss (gain) on sale of assets(3)		(16,771)	(8,611)	(6,517)	79	(1,795)	(6,113)
Impairment charges	182,256	3,555	78,688	385,434	221,685		
Total operating expenses, net	326,966	1,451,120	1,587,472	2,025,171	1,840,554	783,761	802,469
Operating income (loss)	(128,131)	439,171	430,399	111,575	252,513	223,930	224,808
Other income (deductions)							
Interest	(26,734)	(280,501)	(315,944)	(345,257)	(365,970)	(178,968)	(142,970)
Amortization of debt expense		(3,872)	(3,377)	(4,367)	(5,062)	(1,678)	(2,397)
Other, net(4)	5,343	(52,387)	14,350	13,898	9,581	4,927	7,351
Total other income (deductions)	(21,391)	(336,760)	(304,971)	(335,726)	(361,451)	(175,719)	(138,016)
Income (loss) from continuing operations before income taxes	(149,522)	102,411	125,428	(224,151)	(108,938)	48,211	86,792

Provision for income taxes	8,895	60,271	66,328	50,979	46,912	20,056	34,378
Income (loss) from continuing operations	$ (158,417)	$ 42,140	$ 59,100	$ (275,130)	$ (155,850)	$ 28,155	$ 52,414
Income (loss) from continuing operations per basic common share(5)	$ (158,417)	$ 42,140	$ 59,100	$ (275,130)	$ (155,850)	$ 28,155	$ 52,414
Income (loss) from continuing operations per common diluted share(5)	$ (158,417)	$ 42,140	$ 59,100	$ (275,130)	$ (155,850)	$ 28,155	$ 52,414
Basic weighted average common shares(5)	1,000	1,000	1,000	1,000	1,000	1,000	1,000
Diluted weighted average common shares(5)	1,000	1,000	1,000	1,000	1,000	1,000	1,000

	For the years ended December 31, 2004	2005	2006	For the six months ended June 30, 2006 (unaudited)	2007 (unaudited)
	(dollars in thousands, except for share and per share data)				
Other data:					
Cash flows provided by (used in):					
Operating activities	$ 458,408	$ 525,435	$ 323,748	$ 66,723	$ 136,181
Investing activities	(545,903)	(530,165)	(691,438)	(241,724)	(279,441)
Financing activities	95,254	(9,049)	332,367	133,391	164,951
Construction expenditures	(546,241)	(558,446)	(688,843)	(235,818)	(307,726)
Ratio of earnings to combined fixed charges and preferred dividends(6)	1.38				1.57

	2002(1) (Predecessor) (unaudited)	As of December 31, 2003 (unaudited)	2004	2005	2006	As of June 30, 2007 (unaudited)
Balance sheet data:						
Cash and cash equivalents	$ 24,232	$ 71,097	$ 78,856	$ 65,077	$ 29,754	$ 51,445
Utility plant and property, net of depreciation	772,052	7,377,195	7,754,434	8,101,769	8,605,341	8,806,066
Total assets	1,297,587	12,629,354	12,728,410	12,542,029	12,783,059	13,071,585
Other short term and long term debt	806,770	5,063,344	5,101,891	5,030,078	4,103,532	3,588,821
Redeemable preferred stock	12,000	1,787,777	1,775,224	1,774,691	1,774,475	1,774,299
Total debt	818,770	6,851,121	6,877,115	6,804,769	5,878,007	5,363,120
Common stockholder equity	106,229	3,198,144	3,129,555	2,804,716	3,817,397	4,520,149
Preferred stock without mandatory redemption requirements		5,687	4,651	4,571	4,568	4,568

(1) Principally reflects the historical financial data of Elizabethtown Water Company.

(2) On September 28, 2007, Thames US Holdings was merged with and into American Water, with American Water as the surviving entity. American Water is an indirect wholly owned subsidiary of RWE. The historical consolidated financial statements of American Water represent the consolidated results of the Company, formerly issued under the name Thames Water Aqua US Holdings, Inc. and Subsidiary Companies.

(3) Represents primarily losses (gains) on sales of publicly traded securities and dispositions of assets not needed in utility operations.

(4) Includes allowance for other funds used during construction, allowance for borrowed funds used during construction and preferred dividends of subsidiaries.

(5) The number of shares used to compute income (loss) from continuing operations per basic share and income (loss) from continuing operations per diluted common share for the fiscal years ended December 31, 2004, 2005 and 2006 and the six months ended June 30, 2006 and 2007 is 1,000 (the number of common shares outstanding during such period) as no dilutive options or instruments were outstanding during these periods.

(6) For purposes of calculating the ratio of earnings to fixed charges, earnings consists of income (loss) from continuing operations before income taxes including the effect of allowance for funds used during construction, plus fixed charges. Fixed charges consist of interest expense, amortization of debt issuance costs, interest on mandatory redeemable preferred stock, and a portion of rent expense that management believes is representative of the interest component of rental expense. Fixed charges have not been reduced for the effect of AFUDC. For the years ended December 31, 2005 and 2006 earnings was insufficient to cover fixed charges and there was a deficiency of $224.3 million and $109.1 million, respectively. On a pro forma basis after giving effect to the Transactions earnings would have been insufficient to cover fixed charges and there would have been a deficiency of $42.8 million for the year ended December 31, 2006.

Table of Contents

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL

CONDITIONS AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations covers periods prior to the consummation of the Transactions. Accordingly, the discussion and analysis of historical periods does not reflect the significant impact that the Transactions will have on us. You should read the following discussion together with the financial statements and the notes thereto included elsewhere in this prospectus. This discussion contains forward-looking statements that are based on management s current expectations, estimates and projections about our business and operations. The cautionary statements made in this prospectus should be read as applying to all related forward-looking statements whenever they appear in this prospectus. Our actual results may differ materially from those currently anticipated and expressed in such forward-looking statements as a result of a number of factors, including those we discuss under Risk Factors and elsewhere in this prospectus. You should read Risk Factors and Forward-Looking Statements.

Overview

Founded in 1886, American Water is the largest investor-owned United States water and wastewater utility company, as measured both by operating revenue and population served. Our nearly 6,900 employees provide approximately 16.2 million people with drinking water, wastewater and other water-related services in 32 states and Ontario, Canada. In 2006, we generated $2,093.1 million in total operating revenue, representing approximately four times the operating revenue of the next largest investor-owned company in the United States water and wastewater business, and $252.5 million in operating income, which includes $221.7 million of impairment charges relating to continuing operations, and a net loss of $162.2 million.

Our primary business involves the ownership of water and wastewater utilities that provide water and wastewater services to residential, commercial and industrial customers. Our Regulated Businesses that provide these services are generally subject to economic regulation by state PUCs in the states in which they operate. The federal government and the states also regulate environmental health and safety and water quality matters. Our Regulated Businesses currently provide services in 20 states and in 2006 served approximately 3.3 million customers, or connections to our water and wastewater networks. We report the results of this business in our Regulated Businesses. In 2006, our Regulated Businesses generated $1,854.6 million in operating revenue, prior to inter-segment eliminations, representing 88.6% of our consolidated operating revenue.

We also provide services that are not subject to economic regulation by state PUCs. Our Non-Regulated Businesses include our:

- Contracts Operations Group, which enters into public/private partnerships, including O&M and DBO contracts for the provision of services to water and wastewater facilities for municipalities, the United States military and other customers;
- Applied Water Management Group, which works with customers to design, build and operate small water and wastewater treatment plants; and
- Homeowner Services Group, which provides services to domestic homeowners to protect against the cost of repairing broken or leaking pipes inside and outside their homes.

We report the results of this business in our Non-Regulated Business Segment. In 2006, our Non-Regulated Businesses generated $248.5 million in operating revenue, prior to inter-segment eliminations.

History

Prior to being acquired by RWE in 2003, we were the largest publicly traded water utility company in the United States. In 2003, we were acquired by RWE and became a private company. Prior to the Merger, Thames US Holdings, formerly an indirect wholly owned subsidiary of RWE, was the holding company for us and our regulated and unregulated subsidiaries throughout the United States and Ontario, Canada. Our consolidated statements of operations, statements of cash flow and changes in common stockholder s equity and

58

comprehensive income (loss) for the years ended December 31, 2004, 2005 and 2006 and the six months ended June 30, 2006 and 2007 and consolidated balance sheets as of December 31, 2005 and 2006 and as of June 30, 2007 have been derived from the consolidated financial statements and accounting records of Thames US Holdings and its subsidiaries.

Our consolidated statements of operations for the years ended December 31, 2004, 2005 and 2006 and the six months ended June 30, 2006 and 2007 reflect expense allocations for some central corporate functions historically provided to us by RWE, including information systems, human resources, accounting and treasury activities and legal services. These allocations reflect expenses specifically identifiable as relating to our business as well as our share of expenses allocated to us based on capital employed, capital expenditures, headcount, revenues, production volumes, fixed costs, environmental accruals or other methods management considers to be reasonable. We and RWE consider these allocations to be a reasonable reflection of our utilization of the services provided by RWE. However, our expenses as a separate, stand-alone company may be higher or lower than the amounts reflected in our consolidated statements of operations.

The RWE acquisition resulted in certain changes in our business. For example, our operations and management were managed through Thames Water Plc, which we refer to as Thames Water, a former subsidiary of RWE. Also, we agreed not to file rate cases with some state PUCs for specified periods of time as a condition of the acquisition. As of June 30, 2007, all rate stay-out provisions had expired.

As a result of significantly increased costs, our inability to file rate cases and impairment charges, we recorded net losses in the amount of $64.9 million, $325.0 million and $162.2 million for the years ended December 31, 2004, 2005 and 2006, respectively.

In 2005, RWE decided to divest American Water through the sale of shares in one or more public offerings. In order to become a public company once again, we have had to incur substantial initial costs, including costs associated with ensuring adequate internal control over financial reporting in order to achieve compliance with the Sarbanes-Oxley Act. These substantial initial costs are not recoverable in rates charged to our customers. See Our Internal Control and Remediation Initiatives.

We performed valuations of our long-lived assets, investments and goodwill, as of December 31, 2004, 2005 and 2006. As a result of the valuation analyses, we recorded pretax charges of $216.0 million, $420.4 million and $227.8 million, including impairment charges from discontinued operations, for the years ended December 2004, 2005 and 2006, respectively. As a result, this reduced net income by $200.5 million, $388.6 million and $223.6 million in 2004, 2005 and 2006, respectively.

The Company estimates the fair value of our long-lived assets, investments and goodwill using available market values, discounted cash flow models from our business plan or a combination of market and discounted cash flow values. Annual impairment reviews are performed in the fourth quarter. There are a number of significant assumptions reflected in our valuation analyses. These include market interest rates used for discounting future cash flows, market value assumptions using market valuation multiples of comparable water utilities and revenue and operating income growth assumptions in our business plan. We base these assumptions on our best estimates of the Company s future performance and available market information at the time. Any decline over a period of time in the valuation multiples of comparable water utilities, a decline in the market value of our common stock and its value relative to our book equity at the consummation of the concurrent initial public offering or a decline over a period of time of our stock price following the consummation of the concurrent initial public offering could result in additional impairments. A decline in our forecasted results in our business plan, such as changes in rate case results or capital investment budgets or an increase in interest rates, may also result in an incremental impairment charge. In accordance with GAAP, the Company reviews goodwill annually, or more frequently, if changes in circumstances indicate the carrying value may not be recoverable. See Critical Accounting Policies and Estimates.

Table of Contents

Our Internal Control and Remediation Initiatives

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with generally accepted accounting principles. However, since 2003, we have been an indirect wholly owned subsidiary of RWE, a stock corporation organized under the laws of the Federal Republic of Germany, and were not required to maintain a system of internal control consistent with the requirements of the SEC and the Sarbanes-Oxley Act, nor to prepare our own financial statements. As a public reporting company, we will be required, among other things, to maintain a system of effective internal control over financial reporting suitable to prepare our publicly reported financial statements in a timely and accurate manner, and also to evaluate and report on such system of internal control. In particular, we will be required to certify our compliance with Section 404 of the Sarbanes-Oxley Act for the year ended December 31, 2008, which will require us to perform system and process evaluation and testing of our internal control over financial reporting to allow management and our independent registered public accounting firm to report on the effectiveness of our internal control over financial reporting.

In connection with the preparation of our consolidated financial statements as of December 31, 2006, we and our independent registered public accountants have identified the following material weaknesses in our internal control over financial reporting:

- Inadequate internal staffing and skills;
- Inadequate controls over financial reporting processes;
- Inadequate controls over month-end closing processes, including account reconciliations;
- Inadequate controls over maintenance of contracts and agreements;
- Inadequate controls over segregation of duties and restriction of access to key accounting applications; and
- Inadequate controls over tax accounting and accruals.

Since joining the Company in 2006, Donald L. Correll, our Chief Executive Officer, and Ellen C. Wolf, our Chief Financial Officer, have assigned a high priority to the evaluation and remediation of our internal controls, and have taken numerous steps to remediate these material weaknesses and to evaluate and strengthen our other internal controls over financial reporting. Some of the actions taken include:

- Increasing our internal financial staff numbers and skill levels, and using external resources to supplement our internal staff where necessary;
- Implementing detailed processes and procedures related to our period end financial closing processes, key accounting applications and our financial reporting processes;
- Implementing or enhancing systems used in the financial reporting processes and month-end close processes;

Conducting extensive training on existing and newly developed processes and procedures as well as explaining to employees Sarbanes-Oxley Act requirements and the value of internal controls;

Enhancing our internal audit staff;

Hiring a director of internal control and a director of taxes;

Implementing a tracking mechanism and new policy and procedure for approval of all contracts and agreements; and

Retaining a nationally recognized accounting and auditing firm to assist management in developing policies and procedures surrounding internal controls over financial reporting, to evaluate and test these internal controls and to assist in the remediation of internal control deficiencies.

Table of Contents

We have allocated significant additional resources, including the hiring of additional staff, to remediate the material weaknesses identified above. As of June 30, 2007, the Company has incurred $33.8 million to remediate these material weaknesses and to document and test key financial reporting controls. We will need to allocate additional resources to enhance the quality of our staff and to remediate these material weaknesses. As a condition to state PUC approval of the RWE Divestiture, we agreed that costs incurred in connection with our initial internal control and remediation initiatives would not be recoverable in rates charged to our customers.

Elements of our remediation activities can only be accomplished over time, and our initiatives provide no assurances that they will result in an effective internal control environment. Our board of directors, in coordination with our audit committee, will continually assess the progress and sufficiency of these initiatives and make adjustments, as necessary.

Factors Affecting Our Results of Operations

As the largest investor-owned United States water and wastewater utility company, as measured both by operating revenue and population served, our financial condition and results of operations are influenced by a variety of industry-wide factors, including the following:

- economic utility regulation of investor-owned utilities;
- the need for infrastructure investment;
- compliance with environmental, health and safety standards;
- production costs;
- customer growth;
- an overall trend of declining water usage per customer; and
- weather and seasonality.

Since our acquisition by RWE in 2003, our results of operations have also been significantly influenced by goodwill impairments.

Factors that may affect the results of operations of our Regulated Businesses operating performance are mitigated by state PUCs granting us appropriate rate relief that is designed to allow us to recover prudently incurred expenses and to earn an appropriate rate of return on our investment.

Economic Utility Regulation

Our subsidiaries in the states in which we operate our Regulated Businesses are generally subject to extensive economic regulation by their respective state PUCs. Although specific authority might differ from state to state, in most states, these state PUCs must approve rates, accounting treatments, long-term financing programs, significant capital expenditures and plant additions, transactions between the regulated subsidiary and affiliated entities, reorganizations and mergers and acquisitions, in many instances prior to their completion. Regulatory policies not only vary from state to state, they may change over time. These policies will affect the timing as well as the extent of recovery of expenses and the realized return on invested capital.

Our operating revenue is typically determined by reference to the volume of water supplied to a customer multiplied by a price-per-gallon set by a tariff approved by the relevant state PUC. The process to obtain approval for a change in rates, or rate case, involves filing a petition with the state PUC on a periodic basis as determined by our capital expenditures needs and our operating costs. Rate cases and other rate-related proceedings can take several months to a year or more to complete. Therefore, there is frequently a delay, or regulatory lag, between the time one of our regulated subsidiaries makes a capital investment or incurs an operating expense increase and when those costs are reflected in rates. The management team at each of our regulated subsidiaries works to minimize regulatory lag.

Our results of operations are significantly affected by rates authorized by the state PUCs in the states in which we operate, and we are subject to risks and uncertainties associated with delayed or inadequate rate recovery. In addition to the formal rate case filings, we generate revenues through other cost recovery procedures. For example, some states in which we operate allow utility subsidiaries to recover system infrastructure replacement costs without the necessity of filing a full rate proceeding. Since infrastructure replacement is a significant element of capital expenditures made by our subsidiaries, such programs can reduce regulatory lag.

Table of Contents

Currently, Pennsylvania, Illinois, Missouri, Indiana, New York, California and Ohio have allowed the use of these infrastructure surcharges. These surcharges adjust periodically based on qualified capital expenditures being completed or anticipated in a future period. These surcharges are typically reset to zero when new base rates are effective and incorporate the costs of these infrastructure expenditures. We anticipate an increase in revenues of approximately $16.0 million in 2007, assuming constant sales volumes, as a result of these infrastructure surcharges.

Some states have permitted use of some form of forecast or forward looking test year instead of historical data to set rates. Examples of these states include Illinois, Kentucky, Ohio, New York and California. In addition, a number of states in which we operate have allowed the utility to update historical data for some changes that occur for some limited period of time subsequent to the historical test year. This allows the utility to take account of some more current costs or capital investments in the rate-setting process. Examples of these states include New Mexico, Texas, Missouri, Iowa, Virginia, Pennsylvania, Maryland, West Virginia, New Jersey and Arizona.

Another regulatory mechanism to address issues of regulatory lag includes the ability, in some circumstances, to recover in rates a return on utility plant before it is actually in service, instead of capitalizing an allowance for funds used during construction. Examples of states that have allowed such recovery include Iowa, Texas, Pennsylvania, Ohio, Kentucky and California.

The infrastructure surcharge, the forward looking test year and the allowance of a return on utility plant before it is actually in service, are examples of mechanisms that present an opportunity to limit the risks associated with regulatory lag. We employ each of these mechanisms as part of our rate case management program to ensure efficient recovery of our costs and investment and ensure positive short-term liquidity and long-term profitability.

As a condition to our acquisition by RWE in 2003, we agreed not to file rate cases in some of the states where our Regulated Businesses operate, and our recent inactivity in rate-making is therefore not indicative of our future performance securing appropriate and timely rate recovery through the filing of rate cases. As of June 30, 2007, all material rate stay-out provisions had expired. We have four general rate cases pending that were filed in 2006 that would provide $79.1 million in additional annualized revenues, assuming constant sales volumes, if approved as filed. During the first six months of 2007, our subsidiaries filed general rate cases in seven states that would provide $125.5 million in additional annualized revenues, assuming constant sales volumes, if approved as filed. In the first six months of 2007 we received authorizations for $81.0 million of additional annualized revenues from rates, assuming constant sales volumes. We have filed (or expect to file soon) general rate cases in six additional states before the end of 2007 that would provide $52.6 million in additional annualized revenues, assuming constant sales volumes, if approved as filed. In addition, we expect to continue to receive additional revenues through infrastructure replacement surcharges. There is no assurance that the complete amount, or any portion thereof, of any requested increases will be granted.

Infrastructure Investment

The water and wastewater utility industry is highly capital intensive. Over the next five years, we estimate that Company-funded capital investment will total between $4,000 and $4,500 million. We anticipate spending between $700 and $900 million yearly on Company-funded capital investment for the foreseeable future, depending upon the timing of major capital projects. Our capital investment includes both infrastructure renewal programs, where we replace existing infrastructure, as needed, and construction of facilities to meet new customer growth. Over the next five years, we estimate we will invest approximately $1,800 million to replace aging infrastructure including mains, meters, and supply and treatment facilities. We estimate that we will invest approximately $1,300 million in facilities to serve new customer growth over this same period. In addition, we estimate that complying with water quality standards and other regulatory requirements will require approximately $750 million of investment. Projects to enhance system reliability, security and efficiency, or to meet other needs are projected to account for approximately an additional $400 million of investment over this same period.

These capital investments are needed on an ongoing basis to comply with existing and new regulations, renew aging treatment and network assets, provide capacity for new growth and enhance system reliability, security and quality of service. The need for continuous investment presents a challenge due to the potential for regulatory lag, or the delay in recovering our operating expenses and earning an appropriate rate of return on our invested capital and a return of our invested capital. Because the decisions of state PUCs and the timing of those decisions can have a significant impact on the operations and earnings of our Regulated Businesses, we maintain a rate case management program guided by the goals of obtaining efficient recovery of costs of capital and utility operation and maintenance costs, including costs incurred for compliance with environmental, health and safety and water quality regulation. As discussed above under Economic Utility Regulation, we pursue methods to minimize the adverse impact of regulatory lag and have worked with state PUCs and legislatures to implement a number of approaches to achieve this result, including promoting the implementation of forms of forward-looking test years and infrastructure surcharges.

Compliance with Environmental, Health and Safety Standards

Our water and wastewater operations are subject to extensive United States federal, state and local and, in the case of our Canadian operations, Canadian laws and regulations, governing the protection of the environment, health and safety, the quality of the water we deliver to our customers, water allocation rights, and the manner in which we collect, treat and discharge wastewater. These requirements include the Safe Drinking Water Act, the Clean Water Act and similar state and Canadian laws and regulations. We are also required to obtain various environmental permits from regulatory agencies for our operations. State PUCs also set conditions and standards for the water and wastewater services we deliver. We incur substantial costs associated with compliance with environmental, health and safety and water quality regulation to which our Regulated Businesses are subject.

Environmental, health and safety and water quality regulations are complex and change frequently, and the overall trend has been that they have become more stringent over time. We face the risk that as newer or stricter standards are introduced, they could increase our operating expenses. In the past, we have generally been able to recover expenses associated with compliance for environmental, health and safety standards, but this recovery is affected by regulatory lag and the corresponding uncertainties surrounding rate recovery.

Production Costs

Our water and wastewater services require significant production inputs and result in significant production costs. These costs include fuel and power, which is used to operate pumps and other equipment, purchased water and chemicals used to treat water and wastewater. We also incur production costs for waste disposal. For 2006, production costs accounted for approximately 14.4% of our total operating costs. Prices associated with these inputs impact our results of operations until rate relief is granted.

Customer Growth

Customer growth in our Regulated Businesses is driven by (i) organic population growth within our authorized service areas and (ii) by adding new customers to our regulated customer base by acquiring water and wastewater utility systems through acquisitions. Generally, we add customers through tuck-ins of small water and/or wastewater systems, typically serving fewer than 10,000 customers, in close geographic proximity to where we currently operate our Regulated Businesses. We also seek large acquisitions that allow us to acquire multiple water and wastewater utility systems in our existing markets and markets where we currently do not operate our Regulated Businesses. During 2004, 2005, and 2006, we had cash outflows of $1.6 million, $5.0 million and $12.5 million, respectively, for acquisitions of water and wastewater systems which allowed us to expand our regulated customer base. Our most recent significant acquisition was the 2002 purchase of the water and wastewater assets of Citizens Communications Company, adding approximately 300,000 customers in six states in which we had existing operations. We intend to continue to expand our regulated footprint geographically by acquiring water and wastewater systems in our existing markets and some markets in the United States where we do not currently operate our Regulated Businesses. Our experienced development team

Table of Contents

evaluates potential acquisition targets across the country, particularly in higher-growth areas. Before entering new markets, we will evaluate the regulatory environment to ensure that we will have the opportunity to achieve an appropriate return on our investment while maintaining our high standards for quality, reliability and compliance with environmental, health and safety and water quality standards. These acquisitions may include large acquisitions of companies that have operations in multiple markets. For further information, see Our Business Our Regulated Businesses Acquisitions .

Declining Water Usage Per Customer

Increased water conservation, including through the use of more efficient household fixtures and appliances among residential consumers, combined with declining household sizes in the United States, has contributed to a trend of declining water usage per residential customer.

The average annual change in residential water usage per customer from January 1998 through December 2006 (as a percentage of January 1998 usage) in the larger states served by our Regulated Businesses ranged from -0.76% per year in New Jersey at the low end to as high as -1.72% per year in West Virginia.

Because the characteristics of residential water use are driven by many factors, including socio-economic and other demographic characteristics of our service areas, climate, seasonal weather patterns and water rates, these declining trends vary by state and service area and change over time. The trend of declining residential water usage per customer is higher in the predominantly rural states served by our Regulated Businesses. We do not believe that the trend in any particular state or region will have a disproportionate impact on our results of operations.

Our Regulated Businesses are heavily dependent upon operating revenue generated from rates we charge to our residential customers for the volume of water they use. Declining usage will have a negative impact on our long-term operating revenues, if we are unable to secure rate increases or to grow our residential customer base to the extent necessary to offset the residential usage decline.

Weather and Seasonality

Our ability to meet the existing and future water demands of our customers depends on an adequate supply of water. Drought, overuse of sources of water, the protection of threatened species or habitats or other factors may limit the availability of ground and surface water. Also, customer usage of water is affected by weather conditions, in particular during the summer. Our water systems experience higher demand in the summer due to the warmer temperatures and increased usage by customers for lawn irrigation and other outdoor uses. Summer weather that is cooler and wetter than average generally serves to suppress customer water demand, and can have a downward effect on our operating revenue and operating income. Conversely, when weather conditions are extremely dry, our systems may be affected by drought-related warnings and/or water usage restrictions imposed by governmental agencies, also serving to reduce water allocation due to passing-flow requirements, customer demand and operating revenue. These restrictions may be imposed at a regional or state level and may affect our service areas regardless of our readiness to meet unrestricted customer demands. We employ a variety of measures to ensure that we have adequate sources of water supply, both in the short term and over the long term. For additional detail concerning these measures, see Business Our Regulated Businesses Overview of Networks, Facilities and Water Supply.

The geographic diversity of our service areas tends to mitigate some of the effect of weather extremes. In any given summer, some areas are likely to experience drier than average weather while other areas will experience wetter than average weather.

Goodwill Impairment

At June 30, 2007, our goodwill totaled $2,962.6 million. The goodwill is associated primarily with the acquisition of American Water by an affiliate of RWE in 2003 and the acquisition of E Town Corporation in

Table of Contents

2001, representing the excess of the purchase price the purchaser paid over the fair value of the net tangible and intangible assets acquired. As required by applicable accounting rules and principles, we have been required to reflect a non-cash charge to operating results for goodwill impairment in the amounts of $192.9 million in 2004, $396.3 million in 2005 and $227.8 million in 2006. These amounts include impairments relating to discontinued operations.

Our annual goodwill impairment test is completed during the fourth quarter. We have processes to monitor for interim triggering events. During third quarter of 2007, as a result of our debt being placed on review for a possible downgrade and the proposed RWE Divestiture, management determined at that time it was appropriate to update its valuation analysis before the next scheduled annual test.

Based on this assessment, we are performing an interim impairment test and expect to record an impairment charge to goodwill to its Regulated Businesses in the amount of approximately $243.3 million in the third quarter of 2007. The decline was primarily due to a slightly lower long-term earnings forecast caused by updated customer demand and usage expectations and expectations for timing of capital expenditures and rate recovery.

We may be required to recognize additional impairments in the future due to, among other things, a decline in the market value of our stock, a decline in our forecasted results as compared to the business plan, changes in interest rates or a change in rate case results. Further recognition of additional material impairments of goodwill would negatively affect our results of operations and total capitalization.

Table of Contents

Results of Operations

The following table sets forth our consolidated statement of operations data for the years ended December 31, 2004, 2005, and 2006 and the six months ended June 30, 2006 and 2007:

	For the years ended December 31,			For the six months ended June 30,	
	2004	2005	2006	2006 unaudited	2007 unaudited
	(dollars in thousands except for share and per share data)				
Operating revenues	$ 2,017,871	$ 2,136,746	$ 2,093,067	$ 1,007,691	$ 1,027,277
Operating expenses					
Operation and maintenance	1,121,970	1,201,566	1,174,544	562,072	581,999
Depreciation and amortization	225,260	261,364	259,181	128,728	132,764
General taxes	170,165	183,324	185,065	94,756	93,819
Loss (gain) on sale of assets	(8,611)	(6,517)	79	(1,795)	(6,113)
Impairment charges	78,688	385,434	221,685		
Total operating expenses, net	1,587,472	2,025,171	1,840,554	783,761	802,469
Operating income (loss)	430,399	111,575	252,513	223,930	224,808
Other income (deductions)					
Interest	(315,944)	(345,257)	(365,970)	(178,968)	(142,970)
Allowance for other funds used during construction	5,476	5,810	5,980	3,145	3,169
Allowance for borrowed funds used during construction	2,923	2,420	2,652	1,366	1,512
Amortization of debt expense	(3,377)	(4,367)	(5,062)	(1,678)	(2,397)
Preferred dividends of subsidiaries	(410)	(227)	(215)	(112)	(113)
Other, net	6,361	5,895	1,164	528	2,783
Total other income (deductions)	(304,971)	(335,726)	(361,451)	(175,719)	(138,016)
Income (loss) from continuing operations before income taxes	125,428	(224,151)	(108,938)	48,211	86,792
Provision for income taxes	66,328	50,979	46,912	20,056	34,378
Income (loss) from continuing operations	59,100	(275,130)	(155,850)	28,155	52,414
Income (loss) from discontinued operations, net of tax	(124,018)	(49,910)	(6,393)	1,703	(551)
Net income (loss)	$ (64,918)	$ (325,040)	$ (162,243)	$ 29,858	$ 51,863
Net income (loss) per common share:					
Basic					
Income (loss) from continuing operations	$ 59,100	$ (275,130)	$ (155,850)	$ 28,155	$ 52,414
Income (loss) from discontinued operations, net of tax	$ (124,018)	$ (49,910)	$ (6,393)	$ 1,703	$ (551)
Net income (loss)	$ (64,918)	$ (325,040)	$ (162,243)	$ 29,858	$ 51,863
Diluted					
Income (loss) from continuing operations	$ 59,100	$ (275,130)	$ (155,850)	$ 28,155	$ 52,414

Income (loss) discontinued operations, net of tax	$ (124,018)	$ (49,910)	$ (6,393)	$ 1,703	$ (551)
Net income (loss)	$ (64,918)	$ (325,040)	$ (162,243)	$ 29,858	$ 51,863
Average common shares outstanding during the period:					
Basic	1,000	1,000	1,000	1,000	1,000
Diluted	1,000	1,000	1,000	1,000	1,000

66

Table of Contents

The following table summarizes certain financial information for our Regulated and Non-Regulated Businesses for the periods indicated (without giving effect to inter-segment eliminations):

	For the years ended December 31,						For the six months ended June 30,			
	2004		2005		2006		2006		2007	
	Regulated Businesses	Non-Regulated Businesses	Regulated Businesses	Non-Regulated Businesses	Regulated Businesses	Non-Regulated Businesses	Regulated Businesses (unaudited)	Non-Regulated Businesses (unaudited)	Regulated Businesses (unaudited)	Non-Regulated Businesses (unaudited)
	(dollars in thousands)									
Operating revenues	$ 1,748,004	$ 290,037	$ 1,836,061	$ 310,771	$ 1,854,618	$ 248,451	$ 883,017	$ 129,428	$ 927,910	$ 106,960
Adjusted EBIT[1]	$ 482,127	$ 17,117	$ 469,921	$ (106)	$ 468,701	$ (4,725)	$ 220,555	$ 342	$ 210,052	$ 14,031

(1) Refer to Note 21 of the audited consolidated financial statements for the Company s definition of Adjusted EBIT.

Our primary business involves the ownership of water and wastewater utilities that provide water and wastewater services to residential, commercial and industrial customers. As such, our results of operations are significantly impacted by rates authorized by the state PUCs in the states in which we operate. The table below details the annualized revenues (assuming constant sales volumes) resulting from rate authorizations, including distribution infrastructure and other surcharges, granted in 2004, 2005, 2006 and through June 30, 2007.

	Annualized Rate Increases Granted During the years			
	2004	2005	2006	2007
	(dollars in millions)			
State				
New Jersey	$ 29.7	$	$	$ 56.2
Pennsylvania	28.6	5.8	8.0	6.6
Missouri	(0.4)		6.8	2.6
Illinois			0.9	1.7
Indiana	2.7	0.9	1.8	
California	7.2	8.4	15.1	0.5
West Virginia	1.8	10.0		
Other	9.5	9.9	8.7	13.4
Total	$ 79.1	$ 35.0	$ 41.3	$ 81.0

Comparison of Results of Operations for the Six Months Ended June 30, 2007 to the Six Months Ended June 30, 2006

Operating revenues. Our consolidated operating revenues increased $19.6 million, or 1.9%, from $1,007.7 million for the six months ended June 30, 2006, to $1,027.3 million for the six months ended June 30, 2007. An increase in operating revenues for our Regulated Businesses was somewhat offset by a decrease in operating revenues for our Non-Regulated Businesses. The increase in the Regulated Businesses operating revenues was primarily due to rate increases obtained through general rate cases in New Jersey, California, Arizona and other states, totaling approximately $26.5 million. In addition, rate increases obtained through infrastructure surcharges, primarily in Pennsylvania, Missouri, Illinois and Indiana, totaled approximately $8.0 million. Water service operating revenues increased due to growth of 0.9% in our Regulated Businesses customer base. Water sales volume associated with existing customers increased by 0.4% for our Regulated Businesses.

Table of Contents

The following table sets forth the percentage of our Regulated Businesses operating revenues and water sales volume by customer class:

	For the six months ended June 30,			
	Operating Revenues		Water Sales Volume	
	2006	2007	2006	2007
Water service:				
Residential	57.3%	57.7%	51.6%	52.3%
Commercial	19.5%	19.0%	21.9%	21.8%
Industrial	5.1%	5.0%	11.1%	10.8%
Public and other	13.1%	12.6%	15.4%	15.1%
Other water revenues	1.1%	1.7%		
Total water revenues	96.1%	96.0%	100.0%	100.0%
Wastewater service	3.7%	3.8%		
Management fees	0.2%	0.2%		
	100.0%	100.0%		

Water Services Water service operating revenues from residential customers for the six months ended June 30, 2007 amounted to $535.3 million, a 5.9% increase over the same period in 2006 primarily due to rate increases and changes in sales volume. The volume of water sold to residential customers increased by 2.2% for the six months ended June 30, 2007 to 99.1 billion gallons, from 96.9 billion gallons for the same period in 2006, largely as a result of favorable weather conditions and an increased residential customer base.

Water service operating revenues from commercial customers for the six months ended June 30, 2007 amounted to $176.0 million, a 2.3% increase over the same period in 2006, primarily due to rate increases and c