

YORK WATER CO
Form 10-K
March 06, 2018

UNITED STATES
SECURITIES AND EXCHANGE
COMMISSION
Washington, D.C. 20549

FORM 10-K
(Mark One)

ANNUAL REPORT PURSUANT TO
SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31,
2017

OR
TRANSITION REPORT PURSUANT TO
SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934
For the transition period from
_____ to _____

Commission file number 001-34245

THE YORK WATER COMPANY

(Exact name of registrant as specified in its
charter)

PENNSYLVANIA 31A 242500

(State or other
jurisdiction of
incorporation (I.R.S. Employer Identification
or No.)
organization)

130 EAST
MARKET
STREET, 17401
YORK,
PENNSYLVANIA
(Address of
principal
executive (Zip Code)
offices)

Registrant's telephone number, including area
code (717) 845-3601

Securities ~~None~~ The NASDAQ Global Select
registered ~~in~~ the Market
of

pursuant to Section 12(b) of the Act (Name of Each Exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act
COMMON STOCK
to NO PAR VALUE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

YES NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

YES NO

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

YES NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act (check one):

Large
accelerated Non-accelerated filer
filer

(Do not check if a smaller reporting company)

Small
Reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES NO

The aggregate market value of the Common Stock, no par value, held by nonaffiliates of the registrant on June 30, 2017 was \$447,682,707. As of March 6, 2018 there were 12,881,018 shares of Common Stock, no par value, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Company's 2018 Annual Meeting of Shareholders are incorporated by reference into Part I and Part III.

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FORWARD-LOOKING STATEMENTS

Certain statements contained in this annual report and in documents incorporated by reference constitute "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934 and Section 27A of the Securities Act of 1933. Words such as "may," "should," "believe," "anticipate," "estimate," "expect," "intend," "plan" and similar expressions are intended to identify forward-looking statements. These forward-looking statements include certain information relating to the Company's business strategy; statements including, but not limited to:

- the amount and timing of rate increases and other regulatory matters including the recovery of costs recorded as regulatory assets;
- expected profitability and results of operations;
- trends;
- goals, priorities and plans for, and cost of, growth and expansion;
- strategic initiatives;
- availability of water supply;
- water usage by customers; and
- the ability to pay dividends on common stock and the rate of those dividends.

The forward-looking statements in this Annual Report reflect what the Company currently anticipates will happen. What actually happens could differ materially from what it currently anticipates will happen. The Company does not intend to make a public announcement when forward-looking statements in this Annual Report are no longer accurate, whether as a result of new information, what actually happens in the future or for any other reason. Important matters that may affect what will actually happen include, but are not limited to:

- changes in weather, including drought conditions or extended periods of heavy rainfall;
- levels of rate relief granted;
- the level of commercial and industrial business activity within the Company's service territory;
- construction of new housing within the Company's service territory and increases in population;
- changes in government policies or regulations, including the tax code;
- the ability to obtain permits for expansion projects;
- material changes in demand from customers, including the impact of conservation efforts which may impact the demand of customers for water;
- changes in economic and business conditions, including interest rates, which are less favorable than expected;
- loss of customers;
- changes in, or unanticipated, capital requirements;
- the impact of acquisitions;
- changes in accounting pronouncements;
- changes in the Company's credit rating or the market price of its common stock;
- the ability to obtain financing; and
- other matters set forth in Item 1A, "Risk Factors" of this Annual Report.

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THE YORK WATER COMPANY

PART I

Item 1. Business.

The York Water Company (the "Company") is the oldest investor-owned water utility in the United States and is duly organized under the laws of the Commonwealth of Pennsylvania. The Company has operated continuously since 1816. The primary business of the Company is to impound, purify to meet or exceed safe drinking water standards and distribute water. The Company also owns and operates three wastewater collection systems and two wastewater treatment systems. The Company operates within its franchised water territory, which covers 39 municipalities within York County, Pennsylvania and nine municipalities within Adams County, Pennsylvania. The Company's wastewater operations include portions of four municipalities in York County, Pennsylvania. The Company is regulated by the Pennsylvania Public Utility Commission, or PPUC, for both water and wastewater in the areas of billing, payment procedures, dispute processing, terminations, service territory, debt and equity financing and rate setting. The Company must obtain PPUC approval before changing any practices associated with the aforementioned areas.

Water service is supplied through the Company's own distribution system. The Company obtains the bulk of its water supply from both the South Branch and East Branch of the Codorus Creek, which together have an average daily flow of 73.0 million gallons. This combined watershed area is approximately 117 square miles. The Company has two reservoirs, Lake Williams and Lake Redman, which together hold up to approximately 2.2 billion gallons of water. The Company supplements its reservoirs with a 15-mile pipeline from the Susquehanna River to Lake Redman which provides access to an additional supply of 12.0 million gallons of untreated water per day. The Company also owns seven wells which are capable of providing a safe yield of approximately 366,000 gallons per day to supply water to its customers in Carroll Valley Borough and Cumberland Township, Adams County. As of December 31, 2017, the Company's average daily availability was 35.4 million gallons, and average daily consumption was approximately 18.4 million gallons. The Company's service territory had an estimated population of 198,000 as of December 31, 2017. Industry within the Company's service territory is diversified, manufacturing such items as fixtures and furniture, electrical machinery, food products, paper, ordnance units, textile products, air conditioning systems, laundry detergent, barbells and motorcycles.

The Company's water business is somewhat dependent on weather conditions, particularly the amount and timing of rainfall. Revenues are particularly vulnerable to weather conditions in the summer months. Prolonged periods of hot and dry weather generally cause increased water usage for watering lawns, washing cars, and keeping golf courses and sports fields irrigated. Conversely, prolonged periods of dry weather could lead to drought restrictions from governmental authorities. Despite the Company's adequate water supply, customers may be required to cut back water usage under such drought restrictions which would negatively impact revenues. The Company has addressed some of this vulnerability by instituting minimum customer charges which are intended to cover fixed costs of operations under all likely weather conditions.

The Company's business does not require large amounts of working capital and is not dependent on any single customer or a very few customers for a material portion of its business. Increases in revenues are generally dependent on the Company's ability to obtain rate increases from the PPUC in a timely manner and in adequate amounts and to increase volumes of water sold through increased consumption and increases in the number of customers served. The Company continuously looks for water and wastewater acquisition and expansion opportunities both within and outside its current service territory as well as additional opportunities to enter into bulk water contracts with municipalities and other entities to supply water.

The Company has agreements with several municipalities to provide sewer billing and collection services. The Company also has a service line protection program on a targeted basis in order to further diversify its business. Under this optional program, customers pay a fixed monthly fee, and the Company will repair or replace damaged

customer service lines, as needed, subject to an annual maximum dollar amount. The Company continues to review and consider opportunities to expand both initiatives.

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Competition

As a regulated utility, the Company operates within an exclusive franchised territory that is substantially free from direct competition with other public utilities, municipalities and other entities. Although the Company has been granted an exclusive franchise for each of its existing community water and wastewater systems, the ability of the Company to expand or acquire new service territories may be affected by currently unknown competitors obtaining franchises to surrounding systems by application or acquisition. These competitors may include other investor-owned utilities, nearby municipally-owned utilities and sometimes competition from strategic or financial purchasers seeking to enter or expand in the water and wastewater industry. The addition of new service territory and the acquisition of other utilities are generally subject to review and approval by the PPUC.

Water and Wastewater Quality and Environmental Regulations

Provisions of water and wastewater service are subject to regulation under the federal Safe Drinking Water Act, the Clean Water Act and related state laws, and under federal and state regulations issued under these laws. In addition, the Company is subject to federal and state laws and other regulations relating to solid waste disposal, dam safety and other aspects of its operations.

The federal Safe Drinking Water Act establishes criteria and procedures for the U.S. Environmental Protection Agency, or EPA, to develop national quality standards. Regulations issued under the Act, and its amendments, set standards on the amount of certain contaminants allowable in drinking water. Current requirements are not expected to have a material impact on the Company's operations or financial condition as it already meets or exceeds standards. In the future, the Company may be required to change its method of treating drinking water, and may incur additional capital investments if new regulations become effective.

Under the requirements of the Pennsylvania Safe Drinking Water Act, or SDWA, the Pennsylvania Department of Environmental Protection, or DEP, monitors the quality of the finished water supplied to customers. The DEP requires the Company to submit weekly reports showing the results of daily bacteriological and other chemical and physical analyses. As part of this requirement, the Company conducts over 70,000 laboratory tests annually. Management believes that the Company complies with the standards established by the agency under the SDWA. The DEP assists the Company by regulating discharges into the Company's watershed area to prevent and eliminate pollution.

The federal Groundwater Rule establishes rules for community water supplies serving between 100 and 500 customers. This rule requires additional testing of water from well sources, and under certain circumstances requires demonstration and maintenance of effective disinfection. The Company holds public water supply permits issued by the DEP, which establishes the groundwater source operating conditions for its wells, including demonstrated 4-log treatment of viruses. All of the satellite systems operated by the Company are in compliance with the federal Groundwater Rule.

The Clean Water Act regulates discharges from water and wastewater treatment facilities into lakes, rivers, streams and groundwater. The Company complies with this Act by obtaining and maintaining all required permits and approvals for discharges from its water and wastewater facilities and by satisfying all conditions and regulatory requirements associated with the permits.

The DEP monitors the quality of wastewater discharge effluent under the provisions of the National Pollutant Discharge Elimination System, or NPDES. The Company submits monthly reports to the DEP showing the results of its daily effluent monitoring and removal of sludge and biosolids. The Company is not aware of any significant environmental remediation costs necessary from the handling and disposal of waste material from its wastewater operations.

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Lead and copper may enter drinking water primarily through plumbing materials. The Company is required to comply with the Lead and Copper Rule established by the EPA and administered by the DEP. The Company must monitor drinking water at customer taps for compliance with this rule. If lead concentrations exceed an action level, the Company must undertake a number of additional actions to control corrosion, inform the public about steps they should take to protect their health and may be required to replace lead service lines under its control. See "Management's Discussion and Analysis – Environmental Matters" for a discussion of the Company's most recently completed testing.

The DEP and the Susquehanna River Basin Commission, or SRBC, regulate the amount of water withdrawn from streams in the watershed to assure that sufficient quantities are available to meet the needs of the Company and other regulated users. Through its Division of Dam Safety, the DEP regulates the operation and maintenance of the Company's impounding dams. The Company routinely inspects its dams and prepares annual reports of their condition as required by DEP regulations. The DEP reviews these reports and inspects the Company's dams. The DEP most recently inspected the Company's dams in 2017 and noted no significant violations.

Since 1980, the DEP has required any new dam to have a spillway that is capable of passing the design flood without overtopping the dam. The design flood is either the Probable Maximum Flood, or PMF, or some fraction of it, depending on the size and location of the dam. PMF is very conservative and is calculated using the most severe combination of meteorological and hydrologic conditions reasonably possible in the watershed area of a dam.

The Company engaged a professional engineer to analyze the spillway capacities at the Lake Williams and Lake Redman dams and validate the DEP's recommended flood design for the dams. Management presented the results of the study to the DEP in December 2004, and DEP then requested that the Company submit a proposed schedule for the actions to address the spillway capacities. Thereafter, the Company retained an engineering firm to prepare preliminary designs for increasing the spillway capacities to pass the PMF through armoring the dams with roller compacted concrete. Management has met with the DEP on a regular basis to review the preliminary design and discuss scheduling, permitting, and construction requirements. The Company is currently completing preliminary work on the dams as well as the final design and the permitting process. The Company expects to finalize its plans in 2018 and begin armoring one of the dams in 2019. The second dam is expected to be armored in a year or two following the first dam armoring. The cost to armor each dam is expected to be approximately \$5.5 million.

Capital expenditures and operating costs required as a result of water quality standards and environmental requirements have been traditionally recognized by state public utility commissions as appropriate for inclusion in establishing rates. The capital expenditures currently required as a result of water quality standards and environmental requirements have been budgeted in the Company's capital program and represent less than 10% of its expected total capital expenditures over the next five years. The Company is currently in compliance with wastewater environmental standards and does not anticipate any major capital expenditures for its current wastewater business.

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Growth

During the five year period ended December 31, 2017, the Company continued to grow the number of customers and its distribution facilities.

The following table sets forth certain of the Company's summary statistical information.

| (In thousands of dollars) | For the Years Ended December 31, | | | | |
|--|----------------------------------|------------|------------|------------|------------|
| | 2017 | 2016 | 2015 | 2014 | 2013 |
| Revenues: | | | | | |
| Residential | \$31,184 | \$30,142 | \$29,682 | \$29,079 | \$26,796 |
| Commercial and industrial | 13,729 | 13,760 | 13,822 | 13,267 | 12,299 |
| Other | 3,676 | 3,682 | 3,585 | 3,554 | 3,288 |
| Total | \$48,589 | \$47,584 | \$47,089 | \$45,900 | \$42,383 |
| Average daily water consumption (gallons per day) | 18,378,000 | 18,798,000 | 18,507,000 | 18,327,000 | 19,094,000 |
| Miles of water mains at year-end | 973 | 967 | 958 | 951 | 945 |
| Miles of wastewater mains at year-end | 19 | 8 | 8 | 8 | 3 |
| Additional water distribution mains installed/acquired (ft.) | 31,709 | 46,368 | 40,873 | 28,523 | 28,051 |
| Wastewater collection mains acquired (ft.) | 57,386 | - | - | 28,250 | - |
| Number of customers at year-end | 69,604 | 67,052 | 66,087 | 65,102 | 64,118 |
| Population served at year-end | 198,000 | 196,000 | 194,000 | 192,000 | 190,000 |

Executive Officers of the Registrant

The Company presently has 102 full time employees including the officers detailed in the information set forth under the caption "Executive Officers of the Company" of the 2018 Proxy Statement incorporated herein by reference.

Available Information

The Company makes available free of charge, on or through its website (www.yorkwater.com), its annual report on Form 10-K, its quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after the Company electronically files such material with, or furnishes it to, the SEC.

Shareholders may request, without charge, copies of the Company's financial reports. Such requests, as well as other investor relations inquiries, should be addressed to:

| | |
|------------------------------|---------------------------------------|
| Molly E. Norton | The York Water Company (717) 718-2942 |
| Investor Relations & | 130 East Market Street (800) 750-5561 |
| Communications Administrator | York, PA 17401 mollyn@yorkwater.com |

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Item 1A. Risk Factors.

The rates we charge our customers are subject to regulation. If we are unable to obtain government approval of our requests for rate increases, or if approved rate increases are untimely or inadequate to cover our investments in utility plant and equipment and projected expenses, our results of operations may be adversely affected.

Our ability to maintain and meet our financial objectives is dependent upon the rates we charge our customers, which are subject to approval by the PPUC. We file rate increase requests with the PPUC, from time to time, to recover our investments in utility plant and equipment and projected expenses. Any rate increase or adjustment must first be justified through documented evidence and testimony. The PPUC determines whether the investments and expenses are recoverable, the length of time over which such costs are recoverable, or, because of changes in circumstances, whether a remaining balance of deferred investments and expenses is no longer recoverable in rates charged to customers. Once a rate increase application is filed with the PPUC, the ensuing administrative and hearing process may be lengthy and costly. The timing of our rate increase requests are therefore dependent upon the estimated cost of the administrative process in relation to the investments and expenses that we hope to recover through the rate increase. In addition, the amount or frequency of rate increases may be decreased or lengthened as a result of changes in income tax laws regarding tax-basis depreciation as it applies to our capital expenditures or qualifying repair tax deductible expenditures, and by the interpretation of the Tax Cuts and Jobs Act of 2017 by the PPUC.

We can provide no assurances that future requests will be approved by the PPUC; and, if approved, we cannot guarantee that these rate increases will be granted in a timely or sufficient manner to cover the investments and expenses for which we sought the rate increase. If we are unable to obtain PPUC approval of our requests for rate increases, or if approved rate increases are untimely or inadequate to cover our investments in utility plant and equipment and projected expenses, our results of operations may be adversely affected.

We are subject to federal, state and local regulation that may impose costly limitations and restrictions on the way we do business.

Various federal, state and local authorities regulate many aspects of our business. Among the most important of these regulations are those relating to the quality of water we supply our customers, water allocation rights and the quality of the effluent we discharge from our wastewater treatment facility. Government authorities continually review these regulations, particularly the drinking water quality regulations, and may propose new or more restrictive requirements in the future. We are required to perform water and wastewater quality tests that are monitored by the PPUC, the EPA, and the DEP, for the detection of certain chemicals and compounds in our water and effluent. If new or more restrictive limitations on permissible levels of substances and contaminants in our water and wastewater are imposed, we may not be able to adequately predict the costs necessary to meet regulatory standards. If we are unable to recover the cost of implementing new water and wastewater treatment procedures in response to more restrictive quality regulations through our rates that we charge our customers, or if we fail to comply with such regulations, it could have a material adverse effect on our financial condition and results of operations.

We are also subject to water allocation regulations that control the amount of water that we can draw from water sources. The SRBC and the DEP regulate the amount of water withdrawn from streams in the watershed for water supply purposes to assure that sufficient quantities are available to meet our needs and the needs of other regulated users. In addition, government drought restrictions could cause the SRBC or the DEP to temporarily reduce the amount of our allocations. If new or more restrictive water allocation regulations are implemented or our allocations are reduced due to weather conditions, it may have an adverse effect on our ability to supply the demands of our customers, and in turn, on our revenues and results of operations.

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Our business is subject to seasonal fluctuations, which could affect demand for our water service and our revenues.

Demand for our water during the warmer months is generally greater than during cooler months due primarily to additional requirements for water in connection with cooling systems, swimming pools, irrigation systems and other outside water use. Throughout the year, and particularly during typically warmer months, demand will vary with temperature and rainfall levels. If temperatures during the typically warmer months are cooler than expected, or there is more rainfall than expected, the demand for our water may decrease and adversely affect our revenues.

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

We depend on an adequate water supply to meet the present and future demands of our customers and to continue our expansion efforts. Unexpected conditions may interfere with our water supply sources. Drought and overuse may limit the availability of surface and ground water. These factors might adversely affect our ability to supply water in sufficient quantities to our customers and our revenues and earnings may be adversely affected. Additionally, cool and wet weather, as well as drought restrictions and our customers' conservation efforts, may reduce consumption demands, also adversely affecting our revenue and earnings. Furthermore, freezing weather may also contribute to water transmission interruptions caused by pipe and main breakage. If we experience an interruption in our water supply, it could have a material adverse effect on our financial condition and results of operations.

Some scientific experts are predicting a worsening of weather volatility in the future, possibly created by the climate change greenhouse gases. Changing severe weather patterns could require additional expenditures to reduce the risk associated with any increasing storm, flood and drought occurrences.

The issue of climate change continues to receive attention worldwide. Many climate change predictions, if true, present several potential challenges to water and wastewater utilities, such as increased frequency and duration of droughts, increased precipitation and flooding, potential degradation of water quality, and the resulting changes in demand for services. The changes may result in lower revenue, the need for additional capital expenditures, or increased costs. Because of the uncertainty of weather volatility related to climate change, we cannot predict its potential impact on our business, financial condition, or results of operations. Although any potential expenditures and costs may be recovered in the form of higher rates, there can be no assurance that the PPUC would approve rate increases to enable us to recover such expenditures and costs. We cannot assure you that our costs of complying with any climate change related measures will not harm our business, financial condition, or results of operations.

General economic conditions may affect our financial condition and results of operations.

A general economic downturn may lead to a number of impacts on our business that may affect our financial condition and results of operations. Such impacts may include: a reduction in discretionary and recreational water use by our residential water customers, particularly during the summer months when such discretionary usage is normally at its highest; a decline in usage by industrial and commercial customers as a result of decreased business activity; an increased incidence of customers' inability to pay or delays in paying their utility bills, or an increase in customer bankruptcies, which may lead to higher bad debt expense and reduced cash flow; a lower customer growth rate due to a decline in new housing starts; and a decline in the number of active customers due to housing vacancies or abandonments. A deterioration in general economic conditions may also lead to an investment market downturn, which may result in our pension plans' asset market values suffering a decline and significant volatility. A decline in our pension plans' asset market values could increase our required cash contributions to these plans and pension expense in subsequent years.

The current concentration of our business in central and southern Pennsylvania makes us particularly susceptible to adverse developments in local economic and demographic conditions.

Our service territory presently includes 39 municipalities within York County, Pennsylvania and nine municipalities within Adams County, Pennsylvania. Our revenues and operating results are therefore especially subject to local economic and demographic conditions in the area. A change in any of these conditions could make it more costly or difficult for us to conduct our business. In addition, any such change would have a disproportionate effect on us, compared to water and wastewater utility companies that do not have such a geographic concentration.

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Contamination of our water supply may cause disruption in our services and adversely affect our revenues.

Our water supply is subject to contamination from the migration of naturally-occurring substances in groundwater and surface systems and pollution resulting from man-made sources. 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 flow of water from an uncontaminated water source through our interconnected transmission and distribution facilities. 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. Our inability to substitute water supply from an uncontaminated water source, or to adequately treat the contaminated water source in a cost-effective manner, may have an adverse effect on our revenues.

If our sources of water or water at customer sites become contaminated, it could subject us to reduction in usage, regulatory actions, damage to our reputation and private litigation.

As described in "Management's Discussion and Analysis – Environmental Matters", during our triennial testing, completed in 2016, we determined that we exceeded the action level for lead in rules issued by the EPA. The Company is operating under a consent order agreement with the DEP to address the test results, including replacing all known company-owned lead service lines in the next three years. While we believe that our response has been appropriate, we may incur significant costs in responding to this incident and may not be able to recover such costs through rates or from insurers.

Our primary business is to impound, purify to meet or exceed safe drinking water standards and distribute water. Contamination of the water provided to our customers exposes us to risks, including regulatory or government action, customer exposure to contamination or hazardous substances in the water, and resulting private claims and litigation. Negative impacts to our reputation may occur even if we are not responsible for any contamination or its consequences. Pending or future claims against us and reputational damage could have a material adverse impact on our business, financial condition, and results of operations.

The necessity for increased security has and may continue to result in increased operating costs.

We have taken steps to increase security measures at our facilities and heighten employee awareness of threats to our water supply. We have also tightened our security measures regarding the delivery and handling of certain chemicals used in our business. We have and will continue to bear increased costs for security precautions to protect our facilities, operations and supplies. We are not aware of any specific threats to our facilities, operations or supplies. However, it is possible that we would not be in a position to control the outcome of such events should they occur.

The growing dependence on digital technology has increased the risks related to cybersecurity.

Computers and the Internet have led to increased productivity and improved customer service. Unfortunately, progress in this area has brought with it cybersecurity risks. Recently, the frequency and severity of cyber-attacks on companies has increased resulting in a disruption to business operations and the corruption or misappropriation of proprietary data. We have and will continue to bear increased costs for security precautions to protect our information technology. However, if such an attack was to occur and could not be prevented, customer information could be misappropriated, our networks may be down for an extended period of time disrupting our business, and it could require costly replacement of hardware and software. We carry cyber liability insurance, however, our limits may not be sufficient to cover all losses or liabilities.

We depend on the availability of capital for expansion, construction and maintenance.

Our ability to continue our expansion efforts and fund our construction and maintenance program depends on the availability of adequate capital. There is no guarantee that we will be able to obtain sufficient capital in the future or

that the cost of capital will not be too high for future expansion and construction. In addition, approval from the PPUC must be obtained prior to our sale and issuance of securities. If we are unable to obtain approval from the PPUC on these matters, or to obtain approval in a timely manner, it may affect our ability to effect transactions that are beneficial to us or our shareholders. A single transaction may itself not be profitable but might still be necessary to continue providing service or to grow the business.

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The failure to maintain our existing credit rating could affect our cost of funds and related liquidity.

Standard & Poor's Ratings Services rates our outstanding debt and has given a credit rating to us. Their evaluations are based on a number of factors, which include financial strength as well as transparency with rating agencies and timeliness of financial reporting. Failure to maintain our current credit rating could adversely affect our cost of funds and related liquidity.

We may face competition from other water suppliers or wastewater service providers that may hinder our growth and reduce our profitability.

We face competition from other water suppliers for acquisitions, which may limit our growth opportunities. Furthermore, even after we have been the successful bidder in an acquisition, competing water suppliers or wastewater service providers may challenge our application for extending our franchise territory to cover the target company's market. Finally, third parties either supplying water on a contract basis to municipalities or entering into agreements to operate municipal water or wastewater systems might adversely affect our business by winning contracts that may be beneficial to us. If we are unable to compete successfully with other water suppliers and wastewater service providers for these acquisitions, franchise territories and contracts, it may impede our expansion goals and adversely affect our profitability.

An important element of our growth strategy is the acquisition of water and wastewater systems. Any pending or future acquisitions we decide to undertake will involve risks.

The acquisition and integration of water and wastewater systems is an important element in our growth strategy. This strategy depends on identifying suitable acquisition opportunities and reaching mutually agreeable terms with acquisition candidates. The negotiation of potential acquisitions as well as the integration of acquired businesses could require us to incur significant costs. Further, acquisitions may result in dilution for the owners of our common stock, our incurrence of debt and contingent liabilities and fluctuations in quarterly results. In addition, the businesses and other assets we acquire may not achieve the financial results that we expect, which could adversely affect our profitability.

We have restrictions on our dividends. There can also be no assurance that we will continue to pay dividends in the future or, if dividends are paid, that they will be in amounts similar to past dividends.

The terms of our debt instruments impose conditions on our ability to pay dividends. We have paid dividends on our common stock each year since our inception in 1816 and have increased the amount of dividends paid each year since 1997. Our earnings, financial condition, capital requirements, applicable regulations and other factors, including the timeliness and adequacy of rate increases, will determine both our ability to pay dividends on our common stock and the amount of those dividends. There can be no assurance that we will continue to pay dividends in the future or, if dividends are paid, that they will be in amounts similar to past dividends.

If we are unable to pay the principal and interest on our indebtedness as it comes due or we default under certain other provisions of our loan documents, our indebtedness could be accelerated and our results of operations and financial condition could be adversely affected.

Our ability to pay the principal and interest on our indebtedness as it comes due will depend upon our current and future performance. Our performance is affected by many factors, some of which are beyond our control. We believe that our cash generated from operations, and, if necessary, borrowings under our existing credit facilities will be sufficient to enable us to make our debt payments as they become due. If, however, we do not generate sufficient cash, we may be required to refinance our obligations or sell additional equity, which may be on terms that are not as favorable to us. No assurance can be given that any refinancing or sale of equity will be possible when needed or that we will be able to negotiate acceptable terms. In addition, our failure to comply with certain provisions contained in

our trust indentures and loan agreements relating to our outstanding indebtedness could lead to a default under these documents, which could result in an acceleration of our indebtedness.

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We depend significantly on the services of the members of our senior management team, and the departure of any of those persons could cause our operating results to suffer.

Our success depends significantly on the continued individual and collective contributions of our senior management team. If we lose the services of any member of our senior management or are unable to hire and retain experienced management personnel, our operating results could suffer.

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

Approximately one-third of our workforce is unionized under a contract with a labor union. In light of rising costs for healthcare and retirement benefits, contract negotiations in the future may be difficult. We are subject to a risk of work stoppages and other labor actions as we negotiate with the union to address these issues, which could affect our business, financial condition, and results of operations. Although we believe we have a good relationship with our union workforce and have a strike contingency plan, we cannot be assured that issues with our labor force will be resolved favorably to us in the future or that we will not experience work stoppages.

There is a limited trading market for our common stock; you may not be able to resell your shares at or above the price you pay for them.

Although our common stock is listed for trading on the NASDAQ Global Select Market, the trading in our common stock has substantially less liquidity than many other companies quoted on the NASDAQ Global Select Market. A public trading market having the desired characteristics of depth, liquidity and orderliness depends on the presence in the market of willing buyers and sellers of our common stock at any given time. This presence depends on the individual decisions of investors and general economic and market conditions over which we have no control. Because of the limited volume of trading in our common stock, a sale of a significant number of shares of our common stock in the open market could cause our stock price to decline.

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

Our water system includes two impounding dams. While we maintain active and robust dam maintenance and inspection programs, a failure of the dams could result in injuries and damage to residential and/or commercial property downstream for which we may be responsible, in whole or in part. The failure of a dam could 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. We carry liability insurance on our dams, however, our limits may not be sufficient to cover all losses or liabilities incurred due to the failure of one of our dams. The estimated costs to maintain and upgrade our dams are included in our capital budget. Although such costs have previously been recoverable in rates, there is no guarantee that these costs will continue to be recoverable and in what magnitude they will be recoverable.

Wastewater operations entail significant risks and may impose significant costs.

Wastewater collection and treatment and septage pumping and sludge hauling involve various unique risks. If collection or treatment systems fail or do not operate properly, or if there is a spill, untreated or partially treated wastewater could discharge onto property or into nearby streams and rivers, causing various damages and injuries, including environmental damage. These risks are most acute during periods of substantial rainfall or flooding, which are the main causes of sewer overflow and system failure. Liabilities resulting from such damages and injuries could materially and adversely affect our business, financial condition, and results of operations.

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The final determination of our income tax liability may be materially different from our income tax provision.

Significant judgment is required in determining our provision for income taxes. The calculation of the provision for income taxes is subject to our interpretation of applicable business tax laws in the federal and state jurisdictions in which we file. In addition, our income tax returns are subject to periodic examination by the Internal Revenue Service, or IRS, and other taxing authorities.

In December 2014, we changed our tax method of accounting to permit the expensing of qualifying asset improvement costs that were previously being capitalized and depreciated for tax purposes. Our determination of what qualifies as a capital cost versus a repair expense tax deduction is subject to subsequent adjustment and may impact the income tax benefits that have been recognized. Although we believe our income tax estimates are appropriate, there is no assurance that the final determination of our income tax liability will not be materially different, either higher or lower, from what is reflected in our income tax provision. In the event we are assessed additional income taxes, our business, financial condition, and results of operations could be adversely affected.

In December 2017, the Tax Cuts and Jobs Act of 2017, or 2017 Tax Act, was signed into law. The 2017 Tax Act significantly changes how corporations are taxed. Significant judgments are required to be made in interpreting the provisions of the 2017 Tax Act and estimates may be required to comply with the provisions of the 2017 Tax Act. The U.S. Treasury Department, the IRS, and other standard-setting bodies could interpret or issue guidance on how provisions of the 2017 Tax Act will be applied or otherwise administered that is different from our interpretation. As additional regulatory guidance is issued by the applicable taxing authorities, as accounting treatment is clarified, as we perform additional analysis on the application of the law, and as we refine estimates in calculating the effect, our final analysis, which will be recorded in the period completed, may be different from our current provisional amounts, which could materially affect our tax obligations and effective tax rate.

We are subject to market and interest rate risk on our \$12,000,000 variable interest rate debt issue.

We are subject to interest rate risk in conjunction with our \$12,000,000 variable interest rate debt issue. This exposure, however, has been hedged with an interest rate swap. This hedge will protect the Company from the risk of changes in the benchmark interest rates, but does not protect the Company's exposure to the changes in the difference between its own variable funding rate and the benchmark rate. A breakdown of the historical relationships between the cost of funds of the Company and the benchmark rate underlying the interest rate swap could result in higher interest rates adversely affecting our financial results.

The holders of the \$12,000,000 variable rate Pennsylvania Economic Development Financing Authority (PEDFA) Series A Bonds may tender their bonds at any time. When the bonds are tendered, they are subject to an annual remarketing agreement, pursuant to which a remarketing agent attempts to remarket the tendered bonds pursuant to the terms of the Indenture. In order to keep variable interest rates down and to enhance the marketability of the Series A Bonds, the Company entered into a Reimbursement, Credit and Security Agreement with PNC Bank, National Association ("the Bank") dated as of May 1, 2008. This agreement provides for a direct pay letter of credit issued by the Bank to the trustee for the Series A Bonds. The letter of credit expires June 30, 2019 and is reviewed annually for a potential extension of the expiration date. The Bank is responsible for providing the trustee with funds for the timely payment of the principal and interest on the Series A Bonds and for the purchase price of the Series A Bonds that have been tendered or deemed tendered for purchase and have not been remarketed. If the Bank is unable to meet its obligations, the Company would be required to buy any bonds which had been tendered.

Item 1B. Unresolved Staff Comments.

None.

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Item 2. Properties.

Source of Water Supply

The Company owns two impounding dams located in York and Springfield Townships adjoining the Borough of Jacobus to the south. The lower dam, the Lake Williams Impounding Dam, creates a reservoir covering approximately 165 acres containing about 870 million gallons of water. The upper dam, the Lake Redman Impounding Dam, creates a reservoir covering approximately 290 acres containing about 1.3 billion gallons of water.

In addition to the two impounding dams, the Company owns a 15-mile pipeline from the Susquehanna River to Lake Redman that provides access to a supply of an additional 12.0 million gallons of water per day.

The Company also owns three satellite water systems in Adams County, Pennsylvania. The Carroll Valley Water System consists of two groundwater wells capable of providing a safe yield of approximately 100,000 gallons per day with a current average daily consumption of 16,000 gallons per day. The Western Cumberland Water System consists of three groundwater wells capable of providing a safe yield of 144,000 gallons per day with a current average daily consumption of 19,000 gallons per day. The Eastern Cumberland Water System (formerly The Meadows) consists of two groundwater wells capable of providing a safe yield of 122,000 gallons per day with a current average daily consumption of 28,000 gallons per day.

As of December 31, 2017, the Company's present average daily availability was 35.4 million gallons, and daily consumption was approximately 18.4 million gallons.

Pumping Stations

The Company's main pumping station is located in Spring Garden Township on the south branch of the Codorus Creek about four miles downstream from the Company's lower impounding dam. The pumping station presently houses pumping equipment consisting of three electrically driven centrifugal pumps and two diesel-engine driven centrifugal pumps with a combined pumping capacity of 68.0 million gallons per day. The pumping capacity is more than double peak requirements and is designed to provide an ample safety margin in the event of pump or power failure. A large diesel backup generator is installed to provide power to the pumps in the event of an emergency. The untreated water is pumped approximately two miles to the filtration plant through pipes owned by the Company.

The Susquehanna River Pumping Station is located on the western shore of the Susquehanna River several miles south of Wrightsville, PA. The pumping station is equipped with three Floway Vertical Turbine pumps rated at 6 million gallons per day each. The pumping station pumps water from the Susquehanna River approximately 15 miles through a combination of 30 inch and 36 inch ductile iron main to the Company's upper impounding dam, located at Lake Redman.

In 2018, the new Lake Redman Pumping Station, located in York Township adjacent to Lake Redman, was put into service. The pumping station is designed to provide a redundant source with the capacity to pump 20 million gallons per day of untreated water through a company-owned 36 inch force main approximately 3.5 miles to the filtration plant, meeting the Company's daily consumption needs.

Treatment Facilities

The Company's water filtration plant is located in Spring Garden Township about one-half mile south of the City of York. Water at this plant is filtered through twelve dual media filters having a rated capacity of 39.0 million gallons per day, or MGD, with a maximum supply of 42.0 MGD for short periods if necessary. Based on an average daily consumption in 2017 of approximately 18.4 million gallons, the Company believes the pumping and filtering facilities

are adequate to meet present and anticipated demands.

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The Company's sediment recycling facility is located adjacent to its water filtration plant. This state of the art facility employs cutting edge technology to remove fine, suspended solids from untreated water. The Company estimates that through this energy-efficient, environmentally friendly process, approximately 600 tons of sediment will be removed annually, thereby improving the quality of the Codorus Creek watershed.

The Company's two wastewater treatment facilities are located in East Manchester and Lower Windsor Townships. The two wastewater treatment plants are each small, packaged, extended aeration activated sludge facilities with a combined average daily flow capacity of 167,000 gallons. With a projected maximum daily demand of 77,000 gallons, the plants' flow paths offer both capacity and operational redundancy for maintenance, high flow events, and potential growth.

Distribution and Collection

The distribution system of the Company has approximately 973 miles of water main lines which range in diameter from 2 inches to 36 inches. The distribution system includes 31 booster stations and 33 standpipes and reservoirs capable of storing approximately 58.0 million gallons of potable water. All booster stations are equipped with at least two pumps for protection in case of mechanical failure. Following a deliberate study of customer demand and pumping capacity, the Company installed standby generators at all critical booster stations to provide an alternate energy source or emergency power in the event of an electric utility interruption.

The three wastewater collection systems of the Company have a combined approximate 95,000 feet of 6 inch and 8 inch gravity collection mains and 5,000 feet of 6 inch pressure force main along with three sewage pumping stations each rated at 80 gallons per minute.

Other Properties

The Company's distribution center and material and supplies warehouse are located in Springettsbury Township, and are composed of three one-story concrete block buildings aggregating 30,680 square feet.

The administrative and executive offices of the Company are located in one three-story and one two-story brick and masonry buildings, containing a total of approximately 21,861 square feet, in the City of York, Pennsylvania.

All of the Company's properties described above are held in fee by the Company. There are no material encumbrances on such properties.

In 1976, the Company entered into a Joint Use and Park Management Agreement with York County under which the Company licensed use of certain of its lands and waters for public park purposes for a period of 50 years. Under the agreement, York County has agreed not to erect a dam upstream on the East Branch of the Codorus Creek or otherwise obstruct the flow of the creek.

Item 3. Legal Proceedings.

There are no material legal proceedings involving the Company.

Item 4. Mine Safety Disclosures.

Not applicable.

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PART II

Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Market for Common Stock and Dividends

The common stock of The York Water Company is traded on the NASDAQ Global Select Market (Symbol "YORW"). Quarterly price ranges and cash dividends per share for the last two years follow:

| | 2017 | | | 2016 | | |
|-------------------------|---------|---------|-----------|---------|---------|-----------|
| | High | Low | Dividend* | High | Low | Dividend* |
| 1 st Quarter | \$39.00 | \$33.10 | \$ 0.1602 | \$30.99 | \$23.79 | \$ 0.1555 |
| 2 nd Quarter | 39.86 | 31.70 | 0.1602 | 33.40 | 26.54 | 0.1555 |
| 3 rd Quarter | 36.77 | 31.90 | 0.1602 | 32.24 | 27.68 | 0.1555 |
| 4 th Quarter | 39.00 | 33.25 | 0.1666 | 39.85 | 28.61 | 0.1602 |

*Cash dividends per share reflect dividends declared at each dividend date.

Prices listed in the above table are sales prices as listed on the NASDAQ Global Select Market. Shareholders of record (excluding individual participants in securities positions listings) as of December 31, 2017 numbered approximately 2,011.

Dividend Policy

Dividends on the Company's common stock are declared by the Board of Directors and are normally paid in January, April, July and October. Dividends are paid based on shares outstanding as of the stated record date, which is ordinarily the last day of the calendar month immediately preceding the dividend payment.

The dividend paid on the Company's common stock on January 16, 2018 was the 588th consecutive dividend paid by the Company. The Company has paid consecutive dividends for its entire history, since 1816. The policy of the Company's Board of Directors is currently to pay cash dividends on a quarterly basis. The dividend rate has been increased annually for twenty-one consecutive years. The Company's Board of Directors declared dividend number 589 in the amount of \$0.1666 per share at its January 2018 meeting. The dividend is payable on April 16, 2018 to shareholders of record as of February 28, 2018. Future cash dividends will be dependent upon the Company's earnings, financial condition, capital demands and other factors and will be determined by the Company's Board of Directors. See Note 4 to the Company's financial statements included herein for restrictions on dividend payments.

Purchases of Equity Securities by the Company

The Company did not repurchase any of its securities during the fourth quarter of 2017.

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Performance Graph

The following line graph presents the annual and cumulative total shareholder return for The York Water Company Common Stock over a five-year period from 2012 through 2017, based on the market price of the Common Stock and assuming reinvestment of dividends, compared with the cumulative total shareholder return of companies in the S&P 500 Index and a peer group made up of publicly traded water utilities, also assuming reinvestment of dividends. The peer group companies include: American States, American Water, Aqua America, Artesian Resources, California Water Service, Connecticut Water, Middlesex Water and San Jose Water.

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|-------------------------------|--------|--------|--------|--------|--------|--------|
| The York Water Company | 100.00 | 122.52 | 139.56 | 153.90 | 240.54 | 217.44 |
| S&P 500 Index - Total Returns | 100.00 | 132.39 | 150.51 | 152.59 | 170.84 | 208.14 |
| Peer Group | 100.00 | 118.03 | 144.80 | 163.55 | 199.92 | 256.47 |

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Item 6. Selected Financial Data.

(All dollar amounts are stated in thousands of dollars.)

| For the Year | Summary of Operations | | | | |
|--|-----------------------|------------|------------|------------|------------|
| | 2017 | 2016 | 2015 | 2014 | 2013 |
| Operating revenues | \$48,589 | \$47,584 | \$47,089 | \$45,900 | \$42,383 |
| Operating expenses | 26,116 | 24,696 | 24,428 | 23,823 | 21,622 |
| Operating income | 22,473 | 22,888 | 22,661 | 22,077 | 20,761 |
| Interest expense | 4,484 | 5,037 | 4,976 | 4,996 | 5,267 |
| Gain on sale of land | - | 36 | - | 316 | - |
| Other income (expenses), net | (472) | (632) | (456) | (1,036) | (28) |
| Income before income taxes | 17,517 | 17,255 | 17,229 | 16,361 | 15,466 |
| Income taxes | 4,543 | 5,409 | 4,740 | 4,877 | 5,812 |
| Net income | \$12,974 | \$11,846 | \$12,489 | \$11,484 | \$9,654 |
| Per Share of Common Stock | | | | | |
| Book value | \$9.28 | \$8.87 | \$8.51 | \$8.15 | \$7.98 |
| Earnings per share: | | | | | |
| Basic | 1.01 | 0.92 | 0.97 | 0.89 | 0.75 |
| Diluted | 1.01 | 0.92 | 0.97 | 0.89 | 0.75 |
| Weighted average number of shares outstanding during the year: | | | | | |
| Basic | 12,849,123 | 12,845,955 | 12,831,687 | 12,879,912 | 12,928,040 |
| Diluted | 12,849,171 | 12,845,973 | 12,831,687 | 12,879,912 | 12,928,040 |
| Cash dividends declared per share | 0.6472 | 0.6267 | 0.6040 | 0.5788 | 0.5580 |
| Utility Plant | | | | | |
| Original cost, net of acquisition adjustments | \$362,533 | \$339,745 | \$325,691 | \$313,003 | \$298,670 |
| Construction expenditures | 24,602 | 13,158 | 13,844 | 14,139 | 9,852 |
| Other | | | | | |
| Total assets | \$332,030 | \$320,494 | \$310,533 | \$300,708 | \$280,123 |
| Long-term debt including current portion | 90,142 | 84,653 | 84,562 | 82,312 | 82,741 |

For Management's Discussion and Analysis of Financial Condition and Results of Operations, please refer to Item 7 of this Annual Report.

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Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

(All dollar amounts are stated in thousands of dollars.)

Overview

The York Water Company (the "Company") is the oldest investor-owned water utility in the United States, operated continuously since 1816. The Company also operates three wastewater collection systems and two wastewater treatment systems. The Company is a purely regulated water and wastewater utility. Profitability is largely dependent on water revenues. Due to the size of the Company and the limited geographic diversity of its service territory, weather conditions, particularly rainfall, economic, and market conditions can have an adverse effect on revenues. Market conditions and the economy in general have been improving, albeit slowly. While there was little organic growth in the customer base, the Company increased revenues in 2017 compared to 2016 as a result of the distribution system improvement charge, or DSIC, and the West York Borough wastewater acquisition.

The Company's business does not require large amounts of working capital and is not dependent on any single customer or a very few customers for a material portion of its business. In 2017, operating revenue was derived from the following sources and in the following percentages: residential, 64%; commercial and industrial, 28%; and other, 8% which is primarily from the provision for fire service, but includes other water and wastewater service-related income. The diverse customer mix helps to reduce volatility in consumption.

The Company seeks to grow revenues by increasing the volume of water sold through increases in the number of customers served, making timely and prudent investments in infrastructure replacements, expansion and improvements, and timely filing for rate increases. The Company continuously looks for acquisition and expansion opportunities both within and outside its current service territory as well as through contractual services and bulk water supply. The Company's wastewater business provides additional opportunities to expand.

The Company has entered into agreements with several municipalities to provide sewer billing and collection services. The Company also has a service line protection program on a targeted basis. The Company continues to review and consider opportunities to expand both initiatives to further diversify the business.

In addition to increasing revenue, the Company consistently focuses on minimizing costs without sacrificing water quality or customer service. Paperless billing, expanding online services, negotiation of favorable electric, banking and other costs, as well as taking advantage of the 2017 Tax Act and the IRS tangible property regulations are examples of the Company's recent efforts to minimize costs.

Performance Measures

Company management uses financial measures including operating revenues, net income, earnings per share and return on equity to evaluate its financial performance. Additional statistical measures including number of customers, customer complaint rate, annual customer rates and the efficiency ratio are used to evaluate performance quality. These measures are calculated on a regular basis and compared with historical information, budget and the other publicly-traded water and wastewater companies.

The Company's performance in 2017 was strong under the above measures. The collection of a distribution system improvement charge, or DSIC, and increases in the number of customers primarily as a result of acquisitions resulted in higher revenue and offset the higher operating expenses recorded in 2017. Other net expenses were lower in 2017, mainly due to an increased allowance for funds used during construction. The Company incurred lower income taxes mainly due to a higher volume of assets improvements eligible for the tax benefit under the IRS tangible property regulations, or TPR. The overall effect was an increase in net income in 2017 over 2016 of 9.5% and a return on year

end common equity of 10.9%, higher than the 2016 result of 10.4% and the five year historical average of 10.3%.

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The efficiency ratio, which is calculated as net income divided by revenues, is used by management to evaluate its ability to control expenses. Over the five previous years, the Company's ratio averaged 24.3%. In 2017, the ratio was higher than the average at 26.7% due primarily to lower income taxes than are included in the historical average. Management is confident that its ratio will compare favorably to that of its peers. Management continues to look for ways to decrease expenses and increase efficiency as well as to file for rate increases promptly when needed.

2017 Compared with 2016

Net income for 2017 was \$12,974, an increase of \$1,128, or 9.5%, over net income of \$11,846 for 2016. The primary contributing factors to the increase in net income were higher operating revenues, lower income taxes, and an increased allowance for funds used during construction, which were partially offset by higher operating expenses.

Operating revenues for the year increased \$1,005, or 2.1%, from \$47,584 for 2016 to \$48,589 for 2017. The primary reasons for the increase were \$899 of revenues from the DSIC and \$626 from the recent West York Borough wastewater acquisition. Growth in the water customer base also added to revenues. The average number of water customers served in 2017 increased as compared to 2016 by 1,061 customers, from 66,000 to 67,061 customers. The average number of wastewater customers served in 2017 increased as compared to 2016 by 1,371 customers, from 641 to 2,012 customers, due to the acquisition. The increase in revenue was partially offset by lower per capita consumption. Total per capita consumption for 2017 was approximately 4.6% lower than 2016. The Company expects revenues for 2018 to show a modest increase over 2017 due to the DSIC, and the continued increase in the number of water and wastewater customers from acquisitions and growth within the Company's service territory. Other regulatory actions, including the impact of the 2017 Tax Act, and weather patterns could impact results.

Operating expenses for the year increased \$1,420, or 5.7%, from \$24,696 for 2016 to \$26,116 for 2017. The increase was primarily due to higher expenses of approximately \$718 for West York Borough wastewater operating expenses and \$347 for depreciation. Also adding to the increase were \$120 for health insurance, \$109 for maintenance, \$101 for decreased wages and benefits that were able to be capitalized, and \$75 for wages. Other expenses increased by a net of \$55. The increase was partially offset by approximately \$57 for the absence of rate case expenses and \$48 for lower shareholder expenses. In 2018, the Company expects depreciation expense to continue to rise due to additional investment in utility plant, and other expenses to increase at a moderate rate as costs to treat water and to maintain and extend the distribution system continue to rise and the full cost to operate the West York Borough wastewater collection system are incurred. Overall, increases in operating expenses are expected to outpace growth in revenue in the short-term.

Interest on debt for the year increased \$83, or 1.6%, from \$5,265 for 2016 to \$5,348 for 2017. The increase was due to interest on line of credit borrowings and higher short-term interest rates on the variable rate debt. The average debt outstanding under the lines of credit was \$3,132 for 2017 and \$0 for 2016. The weighted average interest rate on the lines of credit was 1.76% for 2017. Interest expense for 2018 is expected to be higher due to continued borrowings under lines of credit and increases in short-term interest rates.

Allowance for funds used during construction increased \$636, from \$228 in 2016 to \$864 in 2017, due to a higher volume of eligible construction mainly related to the pumping station and force main project. Allowance for funds used during construction for 2018 is expected to decrease due to the completion of the project.

A non-recurring gain on the sale of land of \$36 was recorded in 2016 as a result of the sale of nonoperating property from a recent acquisition. No additional land sales are anticipated at this time.

Other income (expenses), net for 2017 reflects decreased expenses of \$160 as compared to 2016. Higher earnings on life insurance policies of approximately \$159 and lower retirement expenses of \$146 were the primary reasons for the decrease. Other expenses decreased by a net of \$8. The decreased expenses were partially offset by additional charitable contributions of \$153. For 2018, other income (expenses) will be largely determined by the change in

market returns and discount rates for retirement programs and related assets.

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Income taxes for 2017 decreased \$866, or 16.0%, compared to 2016 due primarily to a higher volume of asset improvements eligible for the tax benefit under the IRS TPR, including the replacement of company-owned lead service lines, partially offset by the effects of the 2017 Tax Act. (See the Income Taxes, Deferred Income Taxes and Uncertain Tax Positions section included herein for additional details.) The Company's effective tax rate was 25.9% for 2017 and 31.3% for 2016. The Company's effective tax rate for 2018 will largely be determined by the combination of the full implementation of the 2017 Tax Act and the level of eligible asset improvements expensed for tax purposes that would have been capitalized for tax purposes prior to the implementation of the TPR. The 2017 Tax Act should lower the effective tax rate, although the Company is awaiting direction from the PPUC on how to handle the benefit from lowering the federal statutory corporate tax rate. The Company expects the level of eligible asset improvements expensed for tax purposes to decrease in 2018 as a significant portion of the company-owned lead service lines have already been replaced.

2016 Compared with 2015

Net income for 2016 was \$11,846, a decrease of \$643, or 5.1%, from net income of \$12,489 for 2015. The primary contributing factor to the decrease in net income was higher income taxes.

Operating revenues for the year increased \$495, or 1.1%, from \$47,089 for 2015 to \$47,584 for 2016. The primary reasons for the increase in revenues were an increase in customers, and higher sewer billing and collection service revenue. The average number of customers served in 2016 increased as compared to 2015 by 974 customers, from 65,667 to 66,641 customers, due primarily to recent acquisitions. Lower per capita consumption due mainly to a prior year emergency interconnection partially offset the increase. Total per capita consumption for 2016 was 1.1% lower than 2015, but just 0.2% lower excluding the prior year benefit of the emergency interconnection.

Operating expenses for the year increased \$268, or 1.1%, from \$24,428 for 2015 to \$24,696 for 2016. The increase was primarily due to higher expenses of approximately \$271 for depreciation, \$118 for wages, \$60 for shareholder expenses and \$54 for maintenance. The increased expenses were partially offset by approximately \$149 for wages and benefits that were able to be capitalized, and reduced rate case expense of \$80. Other expenses decreased by a net of \$6.

Interest expense on debt for 2016 increased \$83, or 1.6%, from \$5,182 for 2015 to \$5,265 for 2016. The increase was due to an increase in long-term debt outstanding resulting from the bond issuance in July 2015.

Allowance for funds used during construction increased \$22, from \$206 in 2015 to \$228 in 2016, due to a higher volume of eligible construction.

A non-recurring gain on the sale of land of \$36 was recorded in 2016 as a result of the sale of nonoperating property from a recent acquisition.

Other income (expenses), net for 2016 reflects increased expenses of \$176 as compared to the same period of 2015. Higher retirement expenses of \$256 were the primary reason for the increase. The increased expenses were partially offset by higher earnings on life insurance policies of \$78. Other expenses decreased by a net of approximately \$2 as compared to the same period of 2015.

Income taxes for 2016 increased \$669, or 14.1%, compared to 2015 due to a lower volume of asset improvements eligible for the tax benefit of the IRS TPR. The Company's effective tax rate was 31.3% for 2016 and 27.5% for 2015.

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Rate Matters

See Note 8 to the Company's financial statements included herein for a discussion of its rate matters.

Effective January 1, 2018 the Company's tariff included a DSIC on revenues of 4.51%.

The benefit from the implementation of the IRS TPR impacts the rate matters of the Company. Earnings in excess of the regulatory benchmark delayed the collection of a DSIC until June 2017, when the Company began recognizing DSIC for bills rendered after July 1, 2017 that included June consumption. The benefit of the IRS TPR may also lengthen the amount of time between rate increase requests. When the Company does file for its next rate increase, which it expects to do in 2018, the PPUC will take into account the lower income taxes which resulted from the implementation of the IRS TPR, as well as the lower income taxes that will result from the 2017 Tax Act, effectively reducing the amount of revenue required in future years and lowering the Company's rate increase request.

Acquisitions and Growth

See Note 2 to the Company's financial statements included herein for a discussion of completed acquisitions included in financial results.

On October 8, 2013, the Company signed an agreement to purchase the wastewater assets of SYC WWTP, L.P. in Shrewsbury and Springfield Townships, York County, Pennsylvania. Completion of the acquisition is contingent upon receiving approval from all required regulatory authorities. Closing is expected in 2018, at which time the Company will add approximately 30 commercial and industrial wastewater customers.

This acquisition is expected to be immaterial to Company results. The Company is also pursuing other bulk water contracts and acquisitions in and around its service territory to help offset any further declines in per capita water consumption and to grow its business.

On May 10, 2017, the Company signed an emergency interconnect agreement with Dallastown-Yoe Water Authority. The effectiveness of this agreement is contingent upon receiving approval from all required regulatory authorities. Approval is expected to be granted in 2018 at which time the Company will construct a water main extension to a single point of interconnection and supply an agreed upon amount of water to the authority at current tariff rates.

Capital Expenditures

During 2017, the Company invested \$24,602 in construction expenditures for routine items and an additional untreated water pumping station and force main, as well as various replacements of infrastructure including company-owned lead service lines as discussed in Note 10 to the financial statements included herein. The Company replaced or relined approximately 42,500 feet of main in 2017. In addition, the Company invested \$472 in the acquisition of water and wastewater systems during 2017. The Company was able to fund construction expenditures and acquisitions using internally-generated funds, line of credit borrowings, proceeds from its stock purchase plans, and customer advances and contributions from developers, municipalities, customers or builders. See Notes 1, 4 and 5 to the Company's financial statements included herein.

The Company anticipates construction and acquisition expenditures for 2018 and 2019 of approximately \$22,564 and \$19,755, respectively, exclusive of any acquisitions not yet approved. In addition to routine transmission and distribution projects, a portion of the anticipated 2018 and 2019 expenditures will be for additional main extensions, spillway improvements and the armoring of one of the dams, replacing a water storage tank, expansion of a wastewater treatment plant, and various replacements of infrastructure. The Company intends to use primarily internally-generated funds for its anticipated 2018 and 2019 construction and fund the remainder through line of credit borrowings, proceeds from its stock purchase plans and customer advances and contributions (see Note 1 to the

Company's financial statements included herein). Customer advances and contributions are expected to account for between 5% and 10% of funding requirements in 2018 and 2019. Potential debt and equity offerings may be utilized if required. The Company believes it will have adequate credit facilities and access to the capital markets, if necessary, during 2018 and 2019, to fund anticipated construction and acquisition expenditures.

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Liquidity and Capital Resources

Cash

The Company manages its cash through a cash management account that is directly connected to a line of credit. Excess cash generated automatically pays down outstanding borrowings under the line of credit arrangement. If there are no outstanding borrowings, the cash is used as an earnings credit to reduce banking fees. Likewise, if additional funds are needed beyond what is generated internally for payroll, to pay suppliers, or for debt service, funds are automatically borrowed under the line of credit. The Company fully utilized its cash on hand in 2017 primarily as a result of higher capital expenditures and repurchase of common stock, incurring a cash overdraft on its cash management account of \$769 as of December 31, 2017. In addition, the Company borrowed \$6,389 under its lines of credit in 2017. The cash management facility and the other lines of credit are expected to provide the necessary liquidity and funding for the Company's operations, capital expenditures, acquisitions and potential buybacks of stock for the foreseeable future.

Accounts Receivable

The accounts receivable balance tends to follow the change in revenues but is also affected by the timeliness of payments by customers and the level of the reserve for doubtful accounts. In 2017, the accounts receivable balance increased due to an increase in revenue from increased customer counts and the DSIC and a slight decrease in percentage of prior months billings paid by customers in December 2017 as compared to December 2016. Prior to December, the Company experienced an improvement in the timeliness of payments by its customers. A reserve is maintained at a level considered adequate to provide for losses that can be reasonably anticipated based on inactive accounts with outstanding balances. Management periodically evaluates the adequacy of the reserve based on past experience, agings of the receivables, adverse situations that may affect a customer's ability to pay, current economic conditions, and other relevant factors. If the status of these factors deteriorates, the Company may incur additional expenses for uncollectible accounts and experience a reduction in its internally-generated funds.

Internally-generated Funds

The amount of internally-generated funds available for operations and construction depends on the Company's ability to obtain timely and adequate rate relief, changes in regulations, customers' water usage, weather conditions, customer growth and controlled expenses. In 2017, the Company generated \$20,110 internally as compared to \$19,365 in 2016 and \$20,710 in 2015. The increase from 2016 was primarily due to lower income taxes paid.

Credit Lines

Historically, the Company has borrowed \$15,000 to \$20,000 under its lines of credit before refinancing with long-term debt or equity capital. As of December 31, 2017, the Company maintained unsecured lines of credit aggregating \$41,500 with four banks at interest rates ranging from LIBOR plus 1.20% to LIBOR plus 1.25%. The Company had \$6,389 in outstanding borrowings under its lines of credit as of December 31, 2017. The weighted average interest rate on line of credit borrowings as of December 31, 2017 was 2.65%. The Company plans to renew a \$7,500 line of credit that expires in June 2018 and a \$10,000 line of credit that expires in September 2018 under similar terms and conditions.

The Company has taken steps to manage the risk of reduced credit availability. It has maintained committed lines of credit that cannot be called on demand and obtained a 2-year revolving maturity on its larger facilities. There is no guarantee that the Company will be able to obtain sufficient lines of credit with favorable terms in the future. If the Company is unable to obtain sufficient lines of credit or to refinance its line of credit borrowings with long-term debt or equity when necessary, it may have to eliminate or postpone capital expenditures. Management believes the Company will have adequate capacity under its current lines of credit to meet financing needs throughout 2018.

Long-term Debt

The Company's loan agreements contain various covenants and restrictions. Management believes it is currently in compliance with all of these restrictions. See Note 4 to the Company's financial statements included herein for

additional information regarding these restrictions.

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The Pennsylvania Economic Development Financing Authority Series 2014 bonds contain special redemption provisions. Under these provisions, representatives of deceased beneficial owners have the right to request redemption prior to the stated maturity of all or part of their holding in the bonds. The Company is not obligated to redeem any individual holding exceeding \$25, or aggregate holdings exceeding \$300 in any annual period. In 2017, no bonds were retired under these provisions. In 2016, the Company retired \$10 of the bonds under these provisions. Currently, no additional bonds that meet the special provisions have been tendered for redemption.

The York County Industrial Development Authority Series 2006 bonds are subject to optional redemption provisions that allow the Company to redeem all or a portion of the bonds on or after October 1, 2016. The Company may refinance these bonds prior to maturity in 2036 to take advantage of lower interest rates.

The Company's total long-term debt as a percentage of the total capitalization, defined as total common stockholders' equity plus total long-term debt, was 43.7% as of December 31, 2017, compared with 43.4% as of December 31, 2016. The Company began using its lines of credit in 2017 due primarily to increased capital expenditures which increased the debt to total capitalization ratio. The Company expects to allow the debt percentage to trend upward until it approaches fifty percent before considering additional equity. A debt to total capitalization ratio between forty-six and fifty percent has historically been acceptable to the PPUC in rate filings. Due to its recent ability to generate more cash internally, the Company has been able to keep its ratio below fifty percent. See Note 4 to the Company's financial statements included herein for the details of its long-term debt outstanding as of December 31, 2017.

Income Taxes, Deferred Income Taxes and Uncertain Tax Positions

The Company has a substantial deferred income tax asset primarily due to the excess accumulated deferred income taxes on accelerated depreciation from the 2017 Tax Act detailed below and the differences between the book and tax balances of the pension and deferred compensation plans. The Company does not believe a valuation allowance is required due to the expected generation of future taxable income during the periods in which those temporary differences become deductible.

The Company has seen an increase in its deferred income tax liability amounts primarily as a result of the accelerated and bonus depreciation deduction available for federal tax purposes which creates differences between book and tax depreciation expense. In 2017, the recent increase was offset by the remeasurement of the deferred income tax liabilities upon enactment of the 2017 Tax Act detailed below. The Company expects this trend to continue as it makes significant investments in capital expenditures subject to accelerated depreciation or TPR, but at a more modest rate due to the elimination of bonus depreciation on qualified water and wastewater property.

The 2017 Tax Act, among other things, reduces the federal statutory corporate tax rate for tax years beginning in 2018 from 34% to 21%, eliminates certain deductions, and eliminates bonus depreciation on qualified water and wastewater property. This resulted in the remeasurement of the federal portion of the Company's deferred taxes as of December 31, 2017 to the 21% rate. The effect was recognized in income for the year ended December 31, 2017 for all deferred tax assets and liabilities except accelerated depreciation. Under normalization rules applicable to public utility property included in the 2017 Tax Act, the excess accumulated deferred income taxes on accelerated depreciation is recorded as a regulatory liability. The regulatory liability is a temporary difference so a deferred tax asset is recorded including the gross-up of revenue necessary to return, in rates, the effect of the temporary difference.

The Company filed for a change in accounting method under the IRS TPR effective in 2014. Under the change in accounting method, the Company is permitted to deduct the costs of certain asset improvements that were previously being capitalized and depreciated for tax purposes as an expense on its income tax return. The Company was permitted to make this deduction for prior years (the "catch-up deduction") and each year going forward (the "ongoing deduction"). As a result of the catch-up deduction, income tax benefits of \$3,887 were deferred as a regulatory liability. The Company will seek approval from the PPUC in its next rate filing to amortize the catch-up deduction, recorded as a regulatory liability.

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As a result of the ongoing deduction, the net income tax benefits of \$1,796, \$962 and \$1,438 for the years ended December 31, 2017, 2016 and 2015, respectively, reduced income tax expense and flowed-through to net income. The ongoing deduction results in a reduction in the effective income tax rate, a net reduction in income tax expense, and a reduction in the amount of income taxes currently payable. Both the ongoing and catch-up deductions result in increases to deferred tax liabilities and regulatory assets representing the appropriate book and tax basis difference on capital additions. The Company expects to continue to expense these asset improvements in the future.

The Company's effective tax rate will largely be determined by the combination of the full implementation of the 2017 Tax Act and the level of eligible asset improvements expensed for tax purposes that would have been capitalized for tax purposes prior to the implementation of the TPR.

The Company has determined there are no uncertain tax positions that require recognition as of December 31, 2017. See Note 3 to the Company's financial statements included herein for additional details regarding income taxes.

Common Stock

Common stockholders' equity as a percent of the total capitalization was 56.3% as of December 31, 2017, compared with 56.6% as of December 31, 2016. The ratio decreased in 2017 due to share repurchases and higher debt primarily from increased capital expenditures. Similar transactions, among other things, could reduce this percentage in the future. It is the Company's intent to target a ratio between fifty and fifty-four percent.

Credit Rating

On April 21, 2017, Standard & Poor's affirmed the Company's credit rating at A-, with a stable outlook. The Company's ability to maintain its credit rating depends, among other things, on adequate and timely rate relief, which it has been successful in obtaining, its ability to fund capital expenditures in a balanced manner using both debt and equity and its ability to generate cash flow. In 2018, the Company's objectives are to continue to maximize its funds provided by operations and maintain a strong capital structure in order to be able to attract capital.

Environmental Matters

During its triennial testing completed in 2016, the Company determined it exceeded the action level for lead as established by the Lead and Copper Rule, or LCR, issued by the U.S. Environmental Protection Agency. The rule allows the Company to have five samples of the 50 high-risk homes tested exceed the action level of 15 parts per billion, or PPB. The testing found that six properties with lead service lines, all built before 1935, exceeded the action level, and the reported exceedance amount was 1 PPB. The Company determined that only 3% of the company-owned service lines in the system were lead. The Company is required, per the LCR, to engage in more frequent testing for lead, public education, and annually replace 7% of the remaining company-owned lead service lines in its distribution system. The Company completed two rounds of compliance testing at the customer's tap in 2017 and the water samples did not exceed the action level either time. As a result, the Company will reduce its monitoring from semi-annual to annual beginning in 2018.

The Company is performing in excess of the required actions under the LCR. Specifically, the Company is providing the affected customers with a free water test and a 200 gallon per month credit to flush their line in order to reduce any lead content until their lead service line has been replaced. The cost of the water tests and flushing credits was \$16 and \$9 for the years ended December 31, 2017 and 2016, respectively. Additional amounts for water tests and flushing credits are not expected to have a material impact on the financial position of the Company over the remaining three years.

In addition, the Company entered into a consent order agreement with the Pennsylvania Department of Environmental Protection in December 2016. Under the agreement, the Company committed to exceed the LCR replacement schedule by replacing all of the remaining known company-owned lead service lines within four years from the agreement. The cost for these service line replacements was approximately \$1,390 and \$75 for the years ended

December 31, 2017 and 2016, respectively, and is included in utility plant. Additional costs of approximately \$535 are expected until the replacements are complete, and will be integrated into the Company's annual capital budgets.

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Finally, the Company was granted approval by the PPUC to modify its tariff to include the cost of the replacement of lead customer-owned service lines that are discovered when the Company replaces its lead service lines over the remaining three years, and to include the cost of the annual replacement of up to 400 lead customer-owned service lines whenever they are discovered, regardless of the material used for the company-owned service line over nine years. The tariff modification allows the Company to replace customer-owned service lines at its own initial cost. The Company will record the costs as a regulatory asset to be recovered in future base rates to customers, over a reasonable period of at least four but not more than six years. The cost for the customer-owned lead service line replacements under the four-year tariff modification was approximately \$191 through December 31, 2017 and is included as a regulatory asset. Additional replacements are expected to be approximately \$75 under the four-year tariff modification, assuming the average percentage of customer-owned lead service lines that were replaced when company-owned lead service lines were replaced through December 31, 2017 remains consistent over the entire replacement period. The Company is unable to predict how many lead customer-owned service lines are in use, and, therefore, its current estimate of \$1,040 for replacements under the nine-year tariff modification is subject to adjustment as more facts become available.

Dividends

During 2017, the Company's dividend payout ratios relative to net income and net cash provided by operating activities were 64.1% and 40.9%, respectively. During 2016, the Company's dividend payout ratios relative to net income and net cash provided by operating activities were 68.0% and 41.1%, respectively. During the fourth quarter of 2017, the Board of Directors increased the dividend by 4.0% from \$0.1602 per share to \$0.1666 per share per quarter.

The Company's Board of Directors declared a dividend in the amount of \$0.1666 per share at its January 2018 meeting. The dividend is payable on April 16, 2018 to shareholders of record as of February 28, 2018. While the Company expects to maintain this dividend amount in 2018, future dividends will be dependent upon the Company's earnings, financial condition, capital demands and other factors and will be determined by the Company's Board of Directors. See Note 4 to the Company's financial statements included herein for restrictions on dividend payments.

Inflation

The Company is affected by inflation, most notably by the continually increasing costs incurred to maintain and expand its service capacity. The cumulative effect of inflation results in significantly higher facility replacement costs which must be recovered from future cash flows. The ability of the Company to recover this increased investment in facilities is dependent upon future rate increases, which are subject to approval by the PPUC. The Company can provide no assurances that its rate increases will be approved by the PPUC; and, if approved, the Company cannot guarantee that these rate increases will be granted in a timely or sufficient manner to cover the investments and expenses for which the rate increase was sought.

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Contractual Obligations

The following summarizes the Company's contractual obligations by period as of December 31, 2017:

| | Payments due by period | | | | |
|---------------------------------|------------------------|------------------------|------------------|------------------|-------------------------|
| | Total | Less than 1 Year | Years 2 and 3 | Years 4 and 5 | More than 5 Years |
| Long-term debt obligations (a) | \$92,833 | \$44 | \$34,919 | \$7,500 | \$50,370 |
| Interest on long-term debt (b) | 54,776 | 4,719 | 7,184 | 5,924 | 36,949 |
| Short-term Lines of Credit (c) | 1,000 | 1,000 | - | - | - |
| Purchase obligations (d) | 1,380 | 1,380 | - | - | - |
| Defined benefit obligations (e) | 2,300 | 2,300 | - | - | - |
| Deferred employee benefits (f) | 5,481 | 227 | 458 | 648 | 4,148 |
| Other deferred credits (g) | 2,532 | 257 | 450 | 437 | 1,388 |
| Total | \$160,302 | \$9,927 | \$43,011 | \$14,509 | \$92,855 |

(a) Represents debt maturities including current maturities. Included in the table is a potential payment of \$12,000 in Year 2 on the variable rate bonds which would only be due if the bonds were unable to be remarketed. There is currently no such indication of this happening. If the bonds are successfully remarketed, they will be due in 2029.

(b) Excludes interest on the \$12,000 variable rate debt as these payments cannot be reasonably estimated. The interest rate on this issue is reset weekly by the remarketing agent based on then current market conditions. The interest rate as of December 31, 2017 was 1.78%. Also excludes interest on the committed line of credit due to the variability of both the outstanding amount and the interest rate. The interest rate as of December 31, 2017 was 2.63%.

(c) Represents obligations under the Company's short-term lines of credit.

(d) Represents an approximation of open purchase orders at year end.

(e) Represents contributions expected to be made to qualified defined benefit plans. The contribution may increase if the minimum required contribution as calculated under Employee Retirement Income Security Act (ERISA) standards is higher than this amount. The contribution is also dependent upon the amount recovered in rates charged to customers. The amount of required contributions in year 2 and thereafter is not currently determinable.

(f) Represents the obligations under the Company's Supplemental Retirement and Deferred Compensation Plans for executives and management.

(g) Represents the estimated settlement payments to be made under the Company's interest rate swap contract.

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In addition to these obligations, the Company makes refunds on Customers' Advances for Construction over a specific period of time based on operating revenues related to developer-installed water mains or as new customers are connected to and take service from such mains. The refund amounts are not included in the above table because the timing cannot be accurately estimated. Portions of these refund amounts are payable annually through 2028 and amounts not paid by the contract expiration dates become non-refundable and are transferred to Contributions in Aid of Construction.

See Note 10 to the Company's financial statements included herein for a discussion of its commitments.

Critical Accounting Estimates

The methods, estimates and judgments the Company used in applying its accounting policies have a significant impact on the results reported in its financial statements. The Company's accounting policies require management to make subjective judgments because of the need to make estimates of matters that are inherently uncertain. The Company's most critical accounting estimates include: regulatory assets and liabilities, revenue recognition, accounting for its pension plans, and income taxes.

Regulatory Assets and Liabilities

Generally accepted accounting principles define accounting standards for companies whose rates are established by or are subject to approval by an independent third-party regulator. In accordance with the accounting standards, the Company defers costs and credits on its balance sheet as regulatory assets and liabilities when it is probable that these costs and credits will be recognized in the rate-making process in a period different from when the costs and credits were incurred. These deferred amounts are then recognized in the statement of income in the period in which they are reflected in customer rates. If the Company later finds that these assets and liabilities cannot be included in rate-making, they are adjusted appropriately. See Note 1 for additional details regarding regulatory assets and liabilities.

Revenue Recognition

Operating revenues include amounts billed to metered water and certain wastewater customers on a cycle basis and unbilled amounts based on both actual and estimated usage from the latest meter reading to the end of the accounting period. Estimates are based on average daily usage for those particular customers. The unbilled revenue amount is recorded as a current asset on the balance sheet. Actual results could differ from these estimates and would result in operating revenues being adjusted in the period in which the actual usage is known. Based on historical experience, the Company believes its estimate of unbilled revenues is reasonable.

The Company will comply with Accounting Standards Update No. 2014-09 beginning January 1, 2018. See Note 1 to the Company's financial statements included herein for details on the adoption of this standard.

Pension Accounting

Accounting for defined benefit pension plans requires estimates of future compensation increases, mortality, the discount rate, and expected return on plan assets as well as other variables. These variables are reviewed annually with the Company's pension actuary. The Company used compensation increases of 2.5% to 3.0% in 2016 and 2017.

The Company adopted a new mortality table in 2014, the RP-2014, using the white collar table for the administrative and general plan and the blue collar table for the union plan. Using the new mortality table increased the life expectancy of pension plan participants, resulting in a significant increase to the pension benefit obligation, and ultimately, a decline in the Company's funded status of the plans. In 2015, the Social Security Administration released new underlying data creating an Adjusted RP-2014 mortality table. A new mortality improvement scale was released in 2015, the MP-2015, again in 2016, the MP-2016, and again in 2017, the MP-2017. The Company adopted each of the improvement scales in the years they were released. These changes partially offset the increase in the pension benefit obligation realized in 2014.

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The Company selected its December 31, 2017 and 2016 discount rates based on the Citigroup Pension Liability Index. This index uses the Citigroup spot rates for durations out to 30 years and matches them to expected disbursements from the plan over the long term. The Company believes this index most appropriately matches its pension obligations. The present values of the Company's future pension obligations were determined using a discount rate of 3.50% at December 31, 2017 and 4.00% at December 31, 2016.

Adopting a new mortality table that represents a change in life expectancy and choosing a different discount rate normally changes the amount of pension expense and the corresponding liability. In the case of the Company, these items change its liability, but do not have an impact on its pension expense. The PPUC, in a previous rate settlement, agreed to grant recovery of the Company's contribution to the pension plans in customer rates. As a result, under the accounting standards regarding rate-regulated activities, expense in excess of the Company's pension plan contribution can be deferred as a regulatory asset and expensed as contributions are made to the plans and are recovered in customer rates. Therefore, these changes affect regulatory assets rather than pension expense.

The Company's estimate of the expected return on plan assets is primarily based on the historic returns and projected future returns of the asset classes represented in its plans. The target allocation of pension assets is 50% to 70% equity securities, 30% to 50% fixed income securities, and 0% to 10% cash reserves. The Company used 6.75% as its expected rate of return in 2016 and 2017. A decrease in the expected pension return would normally cause an increase in pension expense; however due to the aforementioned rate settlement, the Company's expense would continue to be equal to its contributions to the plans. The change would instead be recorded in regulatory assets.

Lower discount rates and underperformance of assets could cause future required contributions and expense to increase substantially. If this were to happen, the Company would have to consider changes to its pension plan benefits and possibly request additional recovery of expenses through increased rates charged to customers. See Note 7 to the Company's financial statements included herein for additional details regarding the pension plans.

Income Taxes

The Company estimates the amount of income tax payable or refundable for the current year and the deferred income tax liabilities and assets that results from estimating temporary differences resulting from the treatment of certain items, such as depreciation, for tax and financial statement reporting. Generally, these differences result in the recognition of a deferred tax asset or liability on the balance sheet and require the Company to make judgments regarding the probability of the ultimate tax impact of the various transactions entered into. Based on these judgments, it may require tax reserves or valuation allowances on deferred tax assets to reflect the expected realization of future tax benefits. The Company believes its determination of what qualifies as a repair expense tax deduction versus a capital cost as it relates to the IRS TPR ongoing and catch-up deductions is consistent with the regulations. The Company also believes it has appropriately applied the provisions of the 2017 Tax Act including properly applying the accounting standards related to the 2017 Tax Act such as remeasuring its deferred tax assets and liabilities to the newly enacted federal statutory corporate tax rate. Actual income taxes could vary from these estimates and changes in these estimates could increase income tax expense in the period that these changes in estimates occur.

Other critical accounting estimates are discussed in the Significant Accounting Policies Note to the Financial Statements.

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Off-Balance Sheet Transactions

The Company does not use off-balance sheet transactions, arrangements or obligations that may have a material current or future effect on financial condition, results of operations, liquidity, capital expenditures, capital resources or significant components of revenues or expenses. The Company does not use securitization of receivables or unconsolidated entities. For risk management purposes, the Company uses a derivative financial instrument, an interest rate swap agreement discussed in Note 4 to the financial statements included herein. The Company does not engage in trading or other risk management activities, does not use other derivative financial instruments for any purpose, has no material lease obligations, no guarantees and does not have material transactions involving related parties.

Impact of Recent Accounting Pronouncements

See Note 1 to the Company's financial statements included herein for a discussion on the effect of new accounting pronouncements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

The Company's operations are exposed to market risks primarily as a result of changes in interest rates under its lines of credit. As of February 2018, the Company has unsecured lines of credit with four banks having a combined maximum availability of \$41,500. The first line of credit, in the amount of \$13,000, is a committed line of credit with a revolving 2-year maturity (currently May 2019), and carries an interest rate of LIBOR plus 1.20%. The Company had \$5,389 outstanding under this line of credit as of December 31, 2017. The second line of credit, in the amount of \$11,000, is a committed line of credit, which matures in May 2019 and carries an interest rate of LIBOR plus 1.25%. The third line of credit, in the amount of \$7,500, is a committed line of credit, which matures in June 2018 and carries an interest rate of LIBOR plus 1.25%. The fourth line of credit, in the amount of \$10,000, is a committed line of credit, which matures in September 2018 and carries an interest rate of LIBOR plus 1.20%. The Company had \$1,000 outstanding under this line of credit as of December 31, 2017. Other than lines of credit, the Company has long-term fixed rate debt obligations that are not subject to interest rate risk as discussed in Note 4 to the financial statements included herein, and a variable rate PEDFA loan agreement, which is subject to minimal market risk, described below.

In May 2008, the PEDFA issued \$12,000 aggregate principal amount of PEDFA Exempt Facilities Revenue Bonds, Series A (the "Bonds"). The proceeds of this bond issue were used to refund the \$12,000 PEDFA Exempt Facilities Revenue Bonds, Series B of 2004 which were refunded due to bond insurer downgrading issues. The PEDFA then loaned the proceeds to the Company pursuant to a variable interest rate loan agreement with a maturity date of October 1, 2029. In connection with the loan agreement, the Company retained its interest rate swap agreement whereby the Company exchanged its floating rate obligation for a fixed rate obligation. The purpose of the interest rate swap is to manage the Company's exposure to fluctuations in the interest rate. If the interest rate swap agreement works as intended, the receive rate on the swap should approximate the variable rate the Company pays on the PEDFA Series A Bond Issue, thereby minimizing its risk. See Note 4 to the Company's financial statements included herein.

The table below provides information about the Company's financial instruments that are sensitive to changes in interest rates, including long-term debt obligations and the interest rate swap. For debt obligations, the table presents principal cash flows and related weighted average interest rates by expected maturity dates. For the interest rate swap, the table presents the undiscounted net payments and weighted average interest rates by expected maturity dates. Notional amounts are used to calculate the contractual payments to be exchanged under the contract. Weighted average variable rates are based on implied forward rates in the yield curve at the reporting date.

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| Liabilities | Expected Maturity Date | | | | | | | <u>Fair Value</u> |
|-----------------------|------------------------|-------------|-------------|-------------|-------------|-------------------|--------------|-----------------------|
| | <u>2018</u> | <u>2019</u> | <u>2020</u> | <u>2021</u> | <u>2022</u> | <u>Thereafter</u> | <u>Total</u> | |
| Long-term debt: | | | | | | | | |
| Fixed Rate | \$44 | \$11,030 | \$6,500 | \$0 | \$7,500 | \$50,370 | \$75,444 | \$91,000 |
| Average interest rate | 1.00% | 9.89% | 10.05% | 0% | 8.43% | 4.65% | 6.26% | |
| Variable Rate | - | \$17,389 | - | - | - | - | \$17,389 | \$17,000 |
| Interest rate | 2.04% | 2.04% | - | - | - | - | 2.04% | |

| Interest Rate Derivatives | Expected Maturity Date | | | | | | | <u>Fair Value</u> |
|---|------------------------|-------------|-------------|-------------|-------------|-------------------|--------------|-----------------------|
| | <u>2018</u> | <u>2019</u> | <u>2020</u> | <u>2021</u> | <u>2022</u> | <u>Thereafter</u> | <u>Total</u> | |
| Interest Rate Swap – Notional Value \$12,000 | | | | | | | | \$2,196 |
| Variable to Fixed * | \$257 | \$227 | \$223 | \$219 | \$218 | \$1,388 | \$2,532 | |
| Average pay rate | 3.16% | 3.16% | 3.16% | 3.16% | 3.16% | 3.16% | 3.16% | |
| Average receive rate | 1.03% | 1.26% | 1.30% | 1.33% | 1.34% | 1.47% | 1.38% | |

*Represents undiscounted net payments.

The variable rate portion of the liabilities section of the table includes the \$12,000 variable rate loan potentially due in 2019, as the underlying bonds could be tendered at any time. If all of the bonds were tendered and could not be remarketed, the earliest that the Company would have to buy them back would be fourteen months from the date of notification. As of the date of this report, there had been no such notification. If the bonds are able to be remarketed as intended for the term of the bonds, the loan will be due in October 2029. Interest on the \$12,000 variable rate loan is included at an assumed rate of 1.78%, which represents the rate paid to bondholders for the PEDFA Series A issue at December 31, 2017. The variable rate portion of the liabilities section also includes \$5,389 of outstanding borrowings under the Company's committed line of credit due in 2019. This line of credit is reviewed annually and could be extended for another year. The interest rate is variable but is included in the table at 2.63%, which is its December 31, 2017 rate. These rates are used for 2018 and 2019, but may not be indicative of the actual rates.

Other than the interest rate swap, the Company has no other derivative instruments used for any purpose, no additional financial instruments with significant credit risk, and no material exposure to currency or commodity risk.

Item 8. Financial Statements and Supplementary Data.

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Report of Independent Registered Public Accounting Firm

To the Stockholders and the Board of Directors of
The York Water Company

Opinions on the Financial Statements and Internal Control over Financial Reporting

We have audited the accompanying balance sheets of The York Water Company (the "Company") as of December 31, 2017 and 2016, the related statements of income, common stockholders' equity, and cash flows, for each of the three years in the period ended December 31, 2017, and the related notes and financial statement schedule listed in Item 15(a)2 (collectively referred to as the "financial statements"). We also have audited the Company's internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control – Integrated Framework: (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2017, in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control – Integrated Framework: (2013) issued by COSO.

Basis for Opinions

The Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's financial statements and an opinion on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the financial statements included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

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Definition and Limitations of Internal Control Over Financial Reporting

A company's 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 for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/Baker Tilly Virchow Krause, LLP

York, Pennsylvania

We have served as the Company's auditor since 2003.

March 6, 2018

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THE YORK WATER COMPANY

Balance Sheets

(In thousands of dollars, except per share amounts)

| | Dec. 31, 2017 | Dec. 31, 2016 |
|--|------------------|------------------|
| ASSETS | | |
| UTILITY PLANT, at original cost | \$365,767 | \$343,412 |
| Plant acquisition adjustments | (3,234) | (3,667) |
| Accumulated depreciation | (73,746) | (68,838) |
| Net utility plant | 288,787 | 270,907 |
| | | |
| OTHER PHYSICAL PROPERTY, net of accumulated depreciation of \$387 in 2017 and \$353 in 2016 | 737 | 745 |
| | | |
| CURRENT ASSETS: | | |
| Cash and cash equivalents | 2 | 4,209 |
| Accounts receivable, net of reserves of \$305 in 2017 and \$305 in 2016 | 4,547 | 4,296 |
| Unbilled revenues | 2,459 | 2,429 |
| Recoverable income taxes | - | 282 |
| Materials and supplies inventories, at cost | 906 | 746 |
| Prepaid expenses | 697 | 658 |
| Total current assets | 8,611 | 12,620 |
| | | |
| OTHER LONG-TERM ASSETS: | | |
| Notes receivable | 255 | 255 |
| Deferred regulatory assets | 30,331 | 33,027 |
| Other assets | 3,309 | 2,940 |
| Total other long-term assets | 33,895 | 36,222 |
| | | |
| Total Assets | \$332,030 | \$320,494 |

The accompanying notes are an integral part of these statements.

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THE YORK WATER COMPANY

Balance Sheets

(In thousands of dollars, except per share amounts)

| | Dec. 31, 2017 | Dec. 31, 2016 |
|---|------------------|------------------|
| STOCKHOLDERS' EQUITY AND LIABILITIES | | |
| COMMON STOCKHOLDERS' EQUITY: | | |
| Common stock, no par value, authorized 46,500,000 shares, shares issued 12,872,742 in 2017 and 12,852,295 in 2016, shares outstanding 12,872,742 in 2017 and 12,852,295 in 2016 | \$79,201 | \$78,513 |
| Retained earnings | 40,204 | 35,548 |
| Total common stockholders' equity | 119,405 | 114,061 |
| PREFERRED STOCK, authorized 500,000 shares, no shares issued | - | - |
| LONG-TERM DEBT, excluding current portion | 90,098 | 84,609 |
| COMMITMENTS | - | - |
| CURRENT LIABILITIES: | | |
| Short-term borrowings | 1,000 | - |
| Current portion of long-term debt | 44 | 44 |
| Accounts payable | 3,136 | 3,669 |
| Dividends payable | 1,892 | 1,803 |
| Accrued compensation and benefits | 1,134 | 1,233 |
| Accrued income taxes | 531 | - |
| Accrued interest | 989 | 921 |
| Other accrued expenses | 419 | 514 |
| Total current liabilities | 9,145 | 8,184 |
| DEFERRED CREDITS: | | |
| Customers' advances for construction | 6,324 | 7,102 |
| Deferred income taxes | 34,754 | 54,169 |
| Deferred employee benefits | 7,075 | 8,990 |
| Deferred regulatory liabilities | 24,372 | 4,433 |
| Other deferred credits | 2,196 | 2,292 |
| Total deferred credits | 74,721 | 76,986 |
| Contributions in aid of construction | 38,661 | 36,654 |
| Total Stockholders' Equity and Liabilities | \$332,030 | \$320,494 |

The accompanying notes are an integral part of these statements.

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THE YORK WATER COMPANY

Statements of Income

(In thousands of dollars, except per share amounts)

| | Year Ended December 31, | | |
|--|-------------------------|----------|----------|
| | 2017 | 2016 | 2015 |
| OPERATING REVENUES: | | | |
| Residential | \$31,184 | \$30,142 | \$29,682 |
| Commercial and industrial | 13,729 | 13,760 | 13,822 |
| Other | 3,676 | 3,682 | 3,585 |
| | 48,589 | 47,584 | 47,089 |
| OPERATING EXPENSES: | | | |
| Operation and maintenance | 8,891 | 8,031 | 8,066 |
| Administrative and general | 9,323 | 9,129 | 9,082 |
| Depreciation and amortization | 6,769 | 6,422 | 6,151 |
| Taxes other than income taxes | 1,133 | 1,114 | 1,129 |
| | 26,116 | 24,696 | 24,428 |
| Operating income | 22,473 | 22,888 | 22,661 |
| OTHER INCOME (EXPENSES): | | | |
| Interest on debt | (5,348) | (5,265) | (5,182) |
| Allowance for funds used during construction | 864 | 228 | 206 |
| Gain on sale of land | - | 36 | - |
| Other income (expenses), net | (472) | (632) | (456) |
| | (4,956) | (5,633) | (5,432) |
| Income before income taxes | 17,517 | 17,255 | 17,229 |
| Income taxes | 4,543 | 5,409 | 4,740 |
| Net Income | \$12,974 | \$11,846 | \$12,489 |
| Basic Earnings Per Share | \$1.01 | \$0.92 | \$0.97 |
| Diluted Earnings Per Share | \$1.01 | \$0.92 | \$0.97 |
| Cash Dividends Declared Per Share | \$0.6472 | \$0.6267 | \$0.6040 |

The accompanying notes are an integral part of these statements.

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THE YORK WATER COMPANY

Statements of Common Stockholders' Equity

(In thousands of dollars, except per share amounts)

For the Years Ended December 31, 2017, 2016 and 2015

| | Common Stock Shares | Common Stock Amount | Retained Earnings | Total |
|--|---------------------------|---------------------------|----------------------|------------|
| Balance, December 31, 2014 | 12,830,521 | \$ 77,556 | \$ 27,007 | \$ 104,563 |
| Net income | - | - | 12,489 | 12,489 |
| Dividends | - | - | (7,743) | (7,743) |
| Retirement of common stock | (121,012) | (2,546) | - | (2,546) |
| Issuance of common stock under dividend reinvestment, direct stock and employee stock purchase plans | 102,868 | 2,307 | - | 2,307 |
| Balance, December 31, 2015 | 12,812,377 | 77,317 | 31,753 | 109,070 |
| Net income | - | - | 11,846 | 11,846 |
| Dividends | - | - | (8,051) | (8,051) |
| Retirement of common stock | (46,771) | (1,339) | - | (1,339) |
| Issuance of common stock under dividend reinvestment, direct stock and employee stock purchase plans | 85,458 | 2,513 | - | 2,513 |
| Stock-based compensation | 1,231 | 22 | - | 22 |
| Balance, December 31, 2016 | 12,852,295 | 78,513 | 35,548 | 114,061 |
| Net income | - | - | 12,974 | 12,974 |
| Dividends | - | - | (8,318) | (8,318) |
| Retirement of common stock | (37,229) | (1,263) | - | (1,263) |
| Issuance of common stock under dividend reinvestment, direct stock and employee stock purchase plans | 56,171 | 1,905 | - | 1,905 |
| Stock-based compensation | 1,505 | 46 | - | 46 |
| Balance, December 31, 2017 | 12,872,742 | \$ 79,201 | \$ 40,204 | \$ 119,405 |

The accompanying notes are an integral part of these statements.

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THE YORK WATER COMPANY

Statements of Cash Flows

(In thousands of dollars, except per share amounts)

| | Year Ended December 31, | | |
|--|-------------------------|----------|----------|
| | 2017 | 2016 | 2015 |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | | |
| Net income | \$12,974 | \$11,846 | \$12,489 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Gain on sale of land | - | (36) | - |
| Depreciation and amortization | 6,769 | 6,422 | 6,151 |
| Stock-based compensation | 46 | 22 | - |
| Increase in deferred income taxes | 2,484 | 1,646 | 2,270 |
| Other | 54 | 331 | 317 |
| Changes in assets and liabilities: | | | |
| Increase in accounts receivable and unbilled revenues | (572) | (867) | (73) |
| (Increase) decrease in recoverable income taxes | 282 | 767 | (92) |
| Increase in materials and supplies, prepaid expenses, regulatory and other assets | (507) | (3,098) | (3,310) |
| Increase (decrease) in accounts payable, accrued compensation and benefits, accrued expenses, deferred employee benefits, regulatory liabilities, and other deferred credits | (2,018) | 2,387 | 3,009 |
| Increase (decrease) in accrued interest and taxes | 599 | (55) | (51) |
| Net cash provided by operating activities | 20,111 | 19,365 | 20,710 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | | |
| Utility plant additions, including debt portion of allowance for funds used during construction of \$483 in 2017, \$127 in 2016 and \$115 in 2015 | (24,602) | (13,158) | (13,844) |
| Acquisitions of water and wastewater systems | (472) | (50) | (352) |
| Proceeds from sale of land | - | 40 | - |
| Decrease in notes receivable | - | - | 11 |
| Cash received from surrender of life insurance policies | - | 642 | - |
| Net cash used in investing activities | (25,074) | (12,526) | (14,185) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | | |
| Customers' advances for construction and contributions in aid of construction | 1,642 | 1,769 | 1,117 |
| Repayments of customer advances | (413) | (443) | (447) |
| Proceeds of long-term debt issues | 22,878 | - | 14,301 |
| Debt issuance costs | - | - | (298) |
| Repayments of long-term debt | (17,533) | (53) | (11,886) |
| Borrowings under short-term line of credit agreements | 1,000 | - | - |
| Changes in cash overdraft position | 769 | - | - |
| Repurchase of common stock | (1,263) | (1,339) | (2,546) |
| Issuance of common stock | 1,905 | 2,513 | 2,307 |
| Dividends paid | (8,229) | (7,956) | (7,682) |
| Net cash provided by (used in) financing activities | 756 | (5,509) | (5,134) |
| Net change in cash and cash equivalents | (4,207) | 1,330 | 1,391 |
| Cash and cash equivalents at beginning of period | 4,209 | 2,879 | 1,488 |
| Cash and cash equivalents at end of period | \$2 | \$4,209 | \$2,879 |

Supplemental disclosures of cash flow information:

Cash paid during the period for:

| | | | |
|--------------------------------------|---------|---------|---------|
| Interest, net of amounts capitalized | \$4,652 | \$5,051 | \$4,985 |
| Income taxes | 758 | 2,509 | 2,155 |

Supplemental schedule of non-cash investing and financing activities:

Accounts payable includes \$1,498 in 2017, \$2,766 in 2016 and \$720 in 2015 for the construction of utility plant.

The accompanying notes are an integral part of these statements.

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Notes to Financial Statements

(In thousands of dollars, except per share amounts)

1. Significant Accounting Policies

The primary business of The York Water Company, or the Company, is to impound, purify and distribute water. The Company also operates three wastewater collection and treatment systems. The Company operates within its franchised territory located in York and Adams Counties, Pennsylvania, and is subject to regulation by the Pennsylvania Public Utility Commission, or PPUC.

The following summarizes the significant accounting policies employed by The York Water Company.

Utility Plant and Depreciation

The cost of additions includes contracted cost, direct labor and fringe benefits, materials, overhead and, for certain utility plant, allowance for funds used during construction. In accordance with regulatory accounting requirements, water and wastewater systems acquired are recorded at estimated original cost of utility plant when first devoted to utility service and the applicable depreciation is recorded to accumulated depreciation. The difference between the estimated original cost less applicable accumulated depreciation, and the purchase price and acquisition costs is recorded as an acquisition adjustment within utility plant as permitted by the PPUC. At December 31, 2017 and 2016, utility plant includes a net credit acquisition adjustment of \$3,234 and \$3,667, respectively. For those amounts approved by the PPUC, the net acquisition adjustment is being amortized over the remaining life of the respective assets. Certain amounts are still awaiting approval from the PPUC before amortization will commence. Amortization amounted to \$58 in each of the three years in the period ended December 31, 2017.

Upon normal retirement of depreciable property, the estimated or actual cost of the asset is credited to the utility plant account, and such amounts, together with the cost of removal less salvage value, are charged to the reserve for depreciation. To the extent the Company recovers cost of removal or other retirement costs through rates after the retirement costs are incurred, a regulatory asset is reported. Gains or losses from abnormal retirements are reflected in income currently.

The straight-line remaining life method is used to compute depreciation on utility plant cost, exclusive of land and land rights. Annual provisions for depreciation of transportation and mechanical equipment included in utility plant are computed on a straight-line basis over the estimated service lives. Such provisions are charged to clearing accounts and apportioned therefrom to operating expenses and other accounts in accordance with the Uniform System of Accounts as prescribed by the PPUC.

The Company charges to maintenance expense the cost of repairs and replacements and renewals of minor items of property. Maintenance of transportation equipment is charged to clearing accounts and apportioned therefrom in a manner similar to depreciation. The cost of replacements, renewals and betterments of units of property is capitalized to the utility plant accounts.

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The following remaining lives are used for financial reporting purposes:

| Utility Plant Asset Category | December 31, | | Approximate range of remaining lives |
|---|--------------|-----------|--------------------------------------|
| | 2017 | 2016 | |
| Mains and accessories | \$182,927 | \$176,068 | 10 – 83 years |
| Services, meters and hydrants | 71,183 | 68,510 | 19 – 54 years |
| Operations structures, reservoirs and water tanks | 53,610 | 46,494 | 11 – 37 years |
| Pumping and treatment equipment | 29,814 | 29,459 | 2 – 33 years |
| Office, transportation and operating equipment | 12,787 | 12,360 | 3 – 20 years |
| Land and other non-depreciable assets | 3,196 | 3,172 | - |
| Utility plant in service | 353,517 | 336,063 | |
| Construction work in progress | 12,250 | 7,349 | - |
| Total Utility Plant | \$365,767 | \$343,412 | |

The effective rate of depreciation was 2.26% in 2017, 2.25% in 2016, and 2.24% in 2015 on average utility plant, net of customers' advances and contributions. Larger depreciation provisions resulting from allowable accelerated methods are deducted for tax purposes.

Cash and Cash Equivalents

For the purposes of the statements of cash flows, the Company considers all highly liquid debt instruments purchased with an original maturity of three months or less to be cash equivalents except for those instruments earmarked to fund construction expenditures or repay long-term debt.

The Company periodically maintains cash balances in major financial institutions in excess of the federally insured limit by the Federal Deposit Insurance Corporation (FDIC). The Company has not experienced any losses and believes it is not exposed to any significant credit risk on cash and cash equivalents.

Accounts Receivable

Accounts receivable are stated at outstanding balances, less a reserve for doubtful accounts. The reserve for doubtful accounts is established through provisions charged against income. Accounts deemed to be uncollectible are charged against the reserve and subsequent recoveries, if any, are credited to the reserve. The reserve for doubtful accounts is maintained at a level considered adequate to provide for losses that can be reasonably anticipated. Management's periodic evaluation of the adequacy of the reserve is based on past experience, agings of the receivables, adverse situations that may affect a customer's ability to pay, current economic conditions, and other relevant factors. This evaluation is inherently subjective. Unpaid balances remaining after the stated payment terms are considered past due.

Revenue Recognition

Operating revenues include amounts billed to water customers on a cycle basis and unbilled amounts based on actual and estimated usage from the latest meter reading to the end of the accounting period. Operating revenues also include amounts billed to wastewater customers as either a flat monthly fee or a metered rate based on water consumption. The metered wastewater revenue includes actual and estimated usage from the latest meter reading to the end of the accounting period.

Materials and Supplies Inventories

Materials and supplies inventories are stated at cost. Costs are determined using the average cost method.

Notes Receivable

Notes receivable are recorded at cost and represent amounts due from various municipalities for construction of water mains in their particular municipality. Management, considering current information and events regarding the borrowers' ability to repay their obligations, considers a note to be impaired when it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the note agreement. When a note is considered to be impaired, the carrying value of the note is written down. The amount of the impairment is measured based on the present value of expected future cash flows discounted at the note's effective interest rate.

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Regulatory Assets and Liabilities

The Company is subject to the provisions of generally accepted accounting principles regarding rate-regulated entities. The accounting standards provide for the recognition of regulatory assets and liabilities as allowed by regulators for costs or credits that are reflected in current customer rates or are considered probable of being included in future rates. The regulatory assets or liabilities are then relieved as the cost or credit is reflected in rates.

Regulatory assets represent costs that are expected to be fully recovered from customers in future rates while regulatory liabilities represent amounts that are expected to be refunded to customers in future rates. These deferred costs have been excluded from the Company's rate base and, therefore, no return is being earned on the unamortized balances.

Regulatory assets and liabilities are comprised of the following:

| | December 31, | | Remaining |
|--|--------------|----------|------------------|
| | 2017 | 2016 | Recovery Periods |
| <u>Assets</u> | | | |
| Income taxes | \$18,564 | \$20,609 | Various |
| Postretirement benefits | 5,382 | 7,471 | 5 – 10 years |
| Unrealized swap losses | 2,172 | 2,264 | 1 – 12 years |
| Utility plant retirement costs | 3,994 | 2,679 | 5 years |
| Customer-owned lead service line replacements | 191 | - | Not yet known |
| Service life study expenses | 23 | 4 | 5 years |
| Rate case filing expenses | 5 | - | Not yet known |
| | \$30,331 | \$33,027 | |
| <u>Liabilities</u> | | | |
| Excess accumulated deferred income taxes on accelerated depreciation | \$14,348 | \$- | Not yet known |
| Income taxes | 6,260 | 753 | 1 – 50 years |
| IRS TPR catch-up deduction | 3,887 | 3,887 | Not yet known |
| | \$24,495 | \$4,640 | |

The regulatory asset for income taxes includes (a) deferred state income taxes related primarily to differences between book and tax depreciation expense, (b) deferred income taxes related to the differences that arise between specific asset improvement costs capitalized for book purposes and deducted as a repair expense for tax purposes, and (c) deferred income taxes associated with the gross-up of revenues related to the differences. These assets are recognized for ratemaking purposes on a cash or flow-through basis and will be recovered in rates as they reverse.

Postretirement benefits include the difference between contributions and deferred pension expense and the underfunded status of the pension plans. The underfunded status represents the difference between the projected benefit obligation and the fair market value of the assets. This asset is expected to be recovered in future years as additional contributions are made or markets continue to generate positive returns. The recovery period is dependent on contributions made to the plans, plan asset performance and the discount rate used to value the obligations. The period is estimated at between 5 and 10 years.

The Company uses regulatory accounting treatment to defer the mark-to-market unrealized gains and losses on its interest rate swap to reflect that the gain or loss is included in the ratemaking formula when the transaction actually settles. The value of the swap as of the balance sheet date is recorded as part of other deferred credits. Realized gains or losses on the swap will be recorded as interest expense in the statement of income over its remaining life of 12 years.

Utility plant retirement costs represents costs already incurred for the removal of assets, which are expected to be recovered over a five-year period in rates, through depreciation expense.

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The Company was granted approval by the PPUC to modify its tariff to replace lead customer-owned service lines that are discovered when the Company replaces its lead service lines over the remaining three years, and to include the cost of the annual replacement of up to 400 lead customer-owned service lines whenever they are discovered, regardless of the material used for the company-owned service line over nine years. The tariff modification allows the Company to replace customer-owned service lines at its own initial cost and record the costs as a regulatory asset to be recovered in future base rates to customers. The recovery period will be determined when the next rate case is filed, but will be over a reasonable period of at least four but not more than six years.

Service life study expenses are deferred and amortized over their remaining life of five years. Rate case filing expenses are deferred and amortized over their remaining life which will be determined when the next rate case is filed.

Under normalization rules applicable to public utility property included in the Tax Cuts and Jobs Act of 2017, or 2017 Tax Act, the excess accumulated deferred income taxes on accelerated depreciation from lowering of the enacted federal statutory corporate tax rate is recorded as a regulatory liability. The benefit will be given back to customers in rates over the remaining regulatory life of the property determined when the next rate case is filed.

The regulatory liability for income taxes includes deferred taxes related to excess accumulated deferred income taxes on accelerated depreciation, other postretirement benefits, and bad debts, as well as deferred investment tax credits. These liabilities will be given back to customers in rates, as tax deductions occur over the next 1 to 50 years.

The regulatory liability for the Internal Revenue Service, or IRS, tangible property regulations, or TPR, catch-up deduction represents the tax benefits realized on the Company's 2014 income tax return for qualifying capital expenditures made prior to 2014. The Company will seek approval from the PPUC in its next rate filing to amortize the catch-up deduction.

Regulatory liabilities are part of other accrued expenses and deferred regulatory liabilities on the balance sheets.

Other Assets

Other assets consist mainly of the cash value of life insurance policies held as an investment by the Company for reimbursement of costs and benefits associated with its supplemental retirement and deferred compensation programs.

Deferred Debt Expense

Deferred debt expense is amortized on a straight-line basis over the term of the related debt and is presented on the balance sheet as a direct reduction from long-term debt.

Customers' Advances for Construction

Customer advances are cash payments from developers, municipalities, customers or builders for construction of utility plant, and are refundable upon completion of construction, as operating revenues are earned. If the Company loans funds for construction to the customer, the refund amount is credited to the note receivable rather than paid out in cash. After all refunds to which the customer is entitled are made, any remaining balance is transferred to contributions in aid of construction. Pursuant to the 2017 Tax Act, effective December 22, 2017, customer advances are taxable income to the Company and additional funds are collected from customers to cover the taxes. These funds are recorded as a liability within Customer Advances for Construction and are amortized as deferred income over the tax life of the underlying assets.

Contributions in Aid of Construction

Contributions in Aid of Construction is composed of (i) direct, non-refundable contributions from developers, customers or builders for construction of water infrastructure and (ii) customer advances that have become non-refundable. Contributions in aid of construction are deducted from the Company's rate base, and therefore, no return is earned on property financed with contributions. The PPUC requires that contributions received remain on

the Company's balance sheets indefinitely as a long-term liability.

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Interest Rate Swap Agreement

The Company is exposed to certain risks relating to its ongoing business operations. The primary risk managed by using derivative instruments is interest rate risk. The Company utilizes an interest rate swap agreement to convert its variable-rate debt to a fixed rate. Interest rate swaps are contracts in which a series of interest rate cash flows are exchanged over a prescribed period. The notional amount on which the interest payments are based is not exchanged. The Company has designated the interest rate swap agreement as a cash flow hedge, classified as a financial derivative used for non-trading activities.

The accounting standards regarding accounting for derivatives and hedging activities require companies to recognize all derivative instruments as either assets or liabilities at fair value on the balance sheets. In accordance with the standards, the interest rate swap is recorded on the balance sheets in other deferred credits at fair value.

The Company uses regulatory accounting treatment rather than hedge accounting to defer the unrealized gains and losses on its interest rate swap. Instead of the effective portion being recorded as other comprehensive income and the ineffective portion being recognized in earnings, the entire unrealized swap value is recorded as a regulatory asset. Based on current ratemaking treatment, the Company expects the gains and losses to be recognized in rates and in interest expense as the swap settlements occur. Swap settlements are recorded in the income statement with the hedged item as interest expense. Swap settlements resulted in the reclassification from regulatory assets to interest expense of \$301 in 2017, \$345 in 2016, and \$366 in 2015. The overall swap result was a loss of \$209 in 2017, \$128 in 2016, and \$285 in 2015. During the twelve months ending December 31, 2018, the Company expects to reclassify \$252 (before tax) from regulatory assets to interest expense.

The interest rate swap will expire on October 1, 2029.

Stock-Based Compensation

The Company records compensation expense in the financial statements for stock-based awards based on the grant date fair value of those awards. Stock-based compensation expense is recognized over the requisite service periods of the awards on a straight-line basis, which is generally commensurate with the vesting term. Forfeitures are recognized as they occur.

Income Taxes

Certain income and expense items are accounted for in different time periods for financial reporting than for income tax reporting purposes.

Deferred income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. To the extent such income taxes increase or decrease future rates, an offsetting regulatory asset or liability has been recorded.

Investment tax credits have been deferred and are being amortized to income over the average estimated service lives of the related assets. As of December 31, 2017 and 2016, deferred investment tax credits amounted to \$618 and \$657, respectively.

The Company filed for a change in accounting method under the IRS TPR effective in 2014. Under the change in accounting method, the Company is permitted to deduct the costs of certain asset improvements that were previously being capitalized and depreciated for tax purposes as an expense on its income tax return. The Company is permitted to make this deduction for prior years (the "catch-up deduction") and each year going forward, beginning with 2014 (the "ongoing deduction"). The ongoing deduction results in a reduction in the effective income tax rate, a net

reduction in income tax expense, and a reduction in the amount of income taxes currently payable. The catch-up deduction resulted in a decrease in current income taxes payable and an increase to regulatory liabilities. The Company will seek approval from the PPUC in its next rate filing to amortize the remaining catch-up deduction recorded as a regulatory liability. Both the ongoing and catch-up deductions resulted in increases to deferred tax liabilities and regulatory assets representing the appropriate book and tax basis difference on capital additions.

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The 2017 Tax Act, among other things, reduces the federal statutory corporate tax rate for tax years beginning in 2018 from 34% to 21%, eliminates certain deductions, and eliminates bonus depreciation on qualified water and wastewater property. This resulted in the remeasurement of the federal portion of the Company's deferred taxes as of December 31, 2017 to the 21% rate. The effect was recognized in income for the year ended December 31, 2017 for all deferred tax assets and liabilities except accelerated depreciation. Under normalization rules applicable to public utility property included in the 2017 Tax Act, the excess accumulated deferred income taxes on accelerated depreciation is recorded as a regulatory liability. The regulatory liability is a temporary difference so a deferred tax asset is recorded including the gross-up of revenue necessary to return, in rates, the effect of the temporary difference.

Allowance for Funds Used During Construction

Allowance for funds used during construction (AFUDC) represents the estimated cost of funds used for construction purposes during the period of construction. These costs are reflected as non-cash income during the construction period and as an addition to the cost of plant constructed. AFUDC includes the net cost of borrowed funds and a rate of return on other funds. The PPUC approved rate of 10.04% was applied for 2017 and 2016. The Company applied a blended rate in 2015 due to its partial use of tax-exempt financing for 2015 construction projects. The tax-exempt borrowing rates of 4.00% - 4.50% were applied to those expenditures so financed, whereas the approved 10.04% rate was applied to the remainder of 2015 expenditures. AFUDC is recovered through water and wastewater rates as utility plant is depreciated.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain 2016 balance sheet amounts have been reclassified to conform to the 2017 presentation. Such reclassifications had no effect on net income, the statement of common stockholders' equity, or the statement of cash flow category reporting.

Impact of Recent Accounting Pronouncements

In May 2017, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2017-09, Compensation – Stock Compensation (Topic 718): Scope of Modification Accounting. This ASU clarifies when a change to the terms or conditions of a share-based payment award must be accounted for as a modification. The guidance requires modification accounting if the fair value, vesting condition or the classification of the award is not the same immediately before and after a change to the terms and conditions of the award. The ASU is effective for annual periods beginning after December 15, 2017, and interim periods within those fiscal years, with early adoption available. The Company will adopt the standard effective January 1, 2018. The adoption will not have a material impact on its financial position, results of operations and cash flows.

In March 2017, the FASB issued ASU No. 2017-07, Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Post-Retirement Benefit Cost. This ASU requires employers to report the service cost component in the same line item as other compensation costs arising from services rendered by employees during the reporting period. The other components of net benefit costs will be presented in the income statement separately from the service cost and outside of a subtotal of income from operations. In addition, only the service cost component may be eligible for capitalization where applicable. The Company will adopt the standard effective January 1, 2018. The adoption will not have a material impact on its financial position, results of operations and cash flows, but will result in a presentation change on the statements of income.

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In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 320): Classification of Certain Cash Receipts and Cash Payments. This ASU clarifies how certain cash receipts and payments should be presented in the statement of cash flows. The ASU is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years, with early adoption available. The Company will adopt the standard effective January 1, 2018. The adoption will not have a material impact on its financial position, results of operations and cash flows.

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In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842), which replaces the existing guidance in Accounting Standard Codification 840 – Leases. This ASU requires a dual approach for lessee accounting under which a lessee would account for leases as finance leases or operating leases. Both finance leases and operating leases will result in the lessee recognizing a right-of-use asset and a corresponding lease liability. For finance leases, the lessee would recognize interest expense and amortization of the right-of-use asset, and for operating leases, the lessee would recognize a straight-line total lease expense. This ASU is effective for fiscal years beginning after December 15, 2018, and for interim periods within those fiscal years. The Company is currently assessing the impact of the adoption of the standard, but it expects the adoption to have little or no effect on its financial position, results of operations and cash flows.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers. This ASU supersedes the revenue recognition requirements in Accounting Standards Codification 605—Revenue Recognition and most industry-specific guidance throughout the Codification. The standard requires that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the Company expects to be entitled in exchange for those goods or services. In August 2015, the FASB issued ASU 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date, deferring the effective date of this amendment for public companies by one year to fiscal years beginning after December 15, 2017. Early adoption is permitted for fiscal years beginning after December 15, 2016, the original effective date. The standard permits the use of either a retrospective or cumulative effect transition method. The Company will adopt the standard effective January 1, 2018 using the modified retrospective transition method. The Company completed its assessment of the standard and determined adoption will not have a material impact on its financial position, results of operations and cash flows. Under ASU 2014-09, revenue is recognized as control transfers to the customer. As such, revenue for the Company's water and wastewater contracts, which is a significant percentage of the Company's revenue, are generally from a single performance obligation that will be recognized consistent with the revenue recognition model the Company currently uses for its contracts. The Company will comply with the new disclosure requirements included in ASU 2014-09 which will have a significant impact on disclosures upon adoption.

2. Acquisitions

On April 9, 2015, the Company completed the acquisition of the water assets of The Meadows community in Adams County, Pennsylvania. The Company began operating the existing system as a satellite location on April 13, 2015. The acquisition resulted in the addition of approximately 90 new water customers with purchase price and acquisition costs of approximately \$63, which is less than the depreciated original cost of the assets. The Company recorded a negative acquisition adjustment of approximately \$159 and will seek approval from the PPUC to amortize the negative acquisition adjustment over the remaining life of the acquired assets.

On April 22, 2015, the Company completed the acquisition of the water assets of the Paradise Homes Community in York County, Pennsylvania. The Company began operating the existing system through an interconnection with its current distribution system on April 27, 2015. The acquisition resulted in the addition of approximately 90 new water customers with purchase price and acquisition costs of approximately \$36, which is less than the depreciated original cost of the assets. The Company recorded a negative acquisition adjustment of approximately \$28 and will seek approval from the PPUC to amortize the negative acquisition adjustment over the remaining life of the acquired assets.

On October 19, 2015, the Company completed the acquisition of the water assets of the Newberry Farms Mobile Home Park in York County, Pennsylvania. The Company began operating the existing system through an interconnection with its current distribution system on October 22, 2015. The acquisition resulted in the addition of approximately 160 new water customers with purchase price and acquisition costs of approximately \$129, of which \$13 was paid in 2016, which approximated the depreciated original cost of the assets. In 2016, the Company recorded an immaterial negative acquisition adjustment and will seek approval from the PPUC to expense the negative acquisition adjustment.

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On November 2, 2015, the Company completed the acquisition of the water assets of the Margareta Mobile Home Park in York County, Pennsylvania. The Company began operating the existing system through an interconnection with its current distribution system on November 3, 2015. The acquisition resulted in the addition of approximately 65 new water customers with purchase price and acquisition costs of approximately \$102 after a net transfer of \$31 to related construction projects in 2016, which is more than the depreciated original cost of the assets. In 2016, the Company recorded an acquisition adjustment of approximately \$56 and will seek approval from the PPUC to amortize the acquisition adjustment over the remaining life of the acquired assets.

On March 10, 2016, the Company completed the acquisition of the water assets of Crestview Mobile Home Park in York County, Pennsylvania. The Company began operating the existing system through an interconnection with its current distribution system on March 15, 2016. The acquisition resulted in the addition of approximately 120 new water customers with purchase price and acquisition costs of approximately \$47, which is more than the depreciated original cost of the assets. The Company recorded an acquisition adjustment of approximately \$19 and will seek approval from the PPUC to amortize the acquisition adjustment over the remaining life of the acquired assets. These customers were previously served by the Company through a single customer connection to the park.

On October 13, 2016, the Company completed the acquisition of the water assets of the Westwood Mobile Home Park in York County, Pennsylvania. The Company began operating the existing system through an interconnection with its current distribution system on October 17, 2016. The acquisition resulted in the addition of approximately 200 new water customers with purchase price and acquisition cost of approximately \$21, which is less than the depreciated original cost of the assets. The Company recorded a negative acquisition adjustment of approximately \$76 and will seek approval from the PPUC to amortize the acquisition adjustment over the remaining life of the acquired assets. These customers were previously served by the Company through a single customer connection to the park.

On January 6, 2017, the Company completed the acquisition of the water assets of Stockham's Village Mobile Home Park in Adams County, Pennsylvania. The Company began operating the existing system through an interconnection with its current distribution system on January 9, 2017. The acquisition resulted in the addition of approximately 80 new water customers with purchase price and acquisition costs of approximately \$24, which is more than the depreciated original cost of the assets. The Company recorded an acquisition adjustment of approximately \$17 and will seek approval from the PPUC, to amortize the acquisition adjustment over the remaining life of the acquired assets.

On February 23, 2017, the Company completed the acquisition of the wastewater collection assets of West York Borough in York County, Pennsylvania. The Company began operating the existing collection facilities on February 27, 2017. The acquisition resulted in the addition of approximately 1,700 wastewater customers, representing more than 2,200 units, with purchase price and acquisition costs of approximately \$448, which is more than the depreciated original cost of the assets. The Company recorded an acquisition adjustment of approximately \$358 and will seek approval from the PPUC to amortize the acquisition adjustment over the remaining life of the acquired assets.

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3. Income Taxes

The provisions for income taxes consist of:

| | 2017 | 2016 | 2015 |
|---|---------|---------|---------|
| Federal current | \$1,213 | \$2,681 | \$1,873 |
| State current | 846 | 1,082 | 597 |
| Federal deferred | 2,514 | 1,683 | 2,131 |
| State deferred | 9 | 2 | 177 |
| Federal investment tax credit, net of current utilization | (39) | (39) | (38) |
| Total income taxes | \$4,543 | \$5,409 | \$4,740 |

A reconciliation of the statutory Federal tax provision (34%) to the total provision follows:

| | 2017 | 2016 | 2015 |
|--|---------|---------|---------|
| Statutory Federal tax provision | \$5,956 | \$5,867 | \$5,858 |
| State income taxes, net of Federal benefit | 563 | 715 | 511 |
| IRS TPR ongoing deduction | (1,796) | (962) | (1,438) |
| Tax-exempt interest | (33) | (34) | (37) |
| Amortization of investment tax credit | (39) | (39) | (38) |
| Cash value of life insurance | (9) | 44 | 71 |
| Domestic production deduction | (177) | (194) | (190) |
| Change in enacted federal tax rate | 134 | - | - |
| Other, net | (56) | 12 | 3 |
| Total income taxes | \$4,543 | \$5,409 | \$4,740 |

The Company filed for a change in accounting method under the IRS TPR effective in 2014. Under the change in accounting method, the Company is permitted to deduct the costs of certain asset improvements that were previously being capitalized and depreciated for tax purposes as an expense on its income tax return. The Company was permitted to make this deduction for prior years (the "catch-up deduction") and for each year going forward (the "ongoing deduction"). As a result of the catch-up deduction, income tax benefits of \$3,887 were deferred as a regulatory liability. The Company will seek approval from the PPUC in its next rate filing to amortize the catch-up deduction recorded as a regulatory liability. As a result of the ongoing deduction, the net income tax benefits of \$1,796, \$962 and \$1,438 for the years ended December 31, 2017, 2016 and 2015, respectively, reduced income tax expense and flowed-through to net income. The ongoing deduction results in a reduction in the effective income tax rate, a net reduction in income tax expense, and a reduction in the amount of income taxes currently payable. Both the ongoing and catch-up deductions result in increases to deferred tax liabilities and regulatory assets representing the appropriate book and tax basis difference on capital additions.

The 2017 Tax Act, among other things, reduces the federal statutory corporate tax rate for tax years beginning in 2018 from 34% to 21%, eliminates certain deductions, and eliminates bonus depreciation on qualified water and wastewater property. This resulted in the remeasurement of the federal portion of the Company's deferred taxes as of December 31, 2017 to the 21% rate. The effect was recognized in income for the year ended December 31, 2017 for all deferred tax assets and liabilities except accelerated depreciation. Under normalization rules applicable to public utility property included in the 2017 Tax Act, the excess accumulated deferred income taxes on accelerated depreciation is recorded as a regulatory liability. The regulatory liability is a temporary difference so a deferred tax asset is recorded including the gross-up of revenue necessary to return, in rates, the effect of the temporary difference.

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The tax effects of temporary differences between book and tax balances that give rise to significant portions of the deferred tax assets and deferred tax liabilities as of December 31, 2017 and 2016 are summarized in the following table:

| | 2017 | 2016 |
|---|----------|----------|
| Deferred tax assets: | | |
| Reserve for doubtful accounts | \$88 | \$124 |
| Compensated absences | 147 | 212 |
| Deferred compensation | 1,150 | 1,581 |
| Excess accumulated deferred income taxes on accelerated depreciation | 4,145 | - |
| Deferred taxes associated with the gross-up of revenues necessary to return, in rates, the effect of temporary differences | 1,736 | 124 |
| Pensions | 924 | 2,146 |
| Other costs deducted for book, not for tax | 42 | 57 |
| Total deferred tax assets | 8,232 | 4,244 |
| Deferred tax liabilities: | | |
| Accelerated depreciation | 27,785 | 38,063 |
| Basis differences from IRS TPR | 7,579 | 8,339 |
| Investment tax credit | 439 | 390 |
| Deferred taxes associated with the gross-up of revenues necessary to recover, in rates, the effect of temporary differences | 5,291 | 8,183 |
| Tax effect of pension regulatory asset | 1,555 | 3,033 |
| Other costs deducted for tax, not for book | 337 | 405 |
| Total deferred tax liabilities | 42,986 | 58,413 |
| Net deferred tax liability | \$34,754 | \$54,169 |

In accordance with accounting standards, the net deferred tax liability is classified as a noncurrent deferred income tax liability on the balance sheets.

No valuation allowance was required for deferred tax assets as of December 31, 2017 and 2016. In assessing the value of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based upon expected future taxable income and the current regulatory environment, management believes it is more likely than not that the Company will realize the benefits of these deductible differences.

The Company determined that there were no uncertain tax positions meeting the recognition and measurement test of the accounting standards recorded in the years that remain open for review by taxing authorities, which are 2014 through 2016 for both federal and state income tax returns. The Company has not yet filed tax returns for 2017, but has not taken any new position in its 2017 income tax provision.

The Company's policy is to recognize interest and penalties related to income tax matters in other expenses. There were no interest or penalties for the years ended December 31, 2017, 2016, and 2015.

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4. Long-Term Debt and Short-Term Borrowings

Long-term debt as of December 31, 2017 and 2016 is summarized in the following table:

| | 2017 | 2016 |
|--|----------|----------|
| 10.17% Senior Notes, Series A, due 2019 | \$6,000 | \$6,000 |
| 9.60% Senior Notes, Series B, due 2019 | 5,000 | 5,000 |
| 1.00% Pennvest Note, due 2019 | 74 | 118 |
| 10.05% Senior Notes, Series C, due 2020 | 6,500 | 6,500 |
| 8.43% Senior Notes, Series D, due 2022 | 7,500 | 7,500 |
| Variable Rate Pennsylvania Economic Development Financing Authority Exempt Facilities Revenue Bonds, Series 2008A, due 2029 | 12,000 | 12,000 |
| 4.75% York County Industrial Development Authority Revenue Bonds, Series 2006, due 2036 | 10,500 | 10,500 |
| 4.50% Pennsylvania Economic Development Financing Authority Exempt Facilities Revenue Refunding Bonds, Series 2014, due 2038 | 14,870 | 14,870 |
| 5.00% Monthly Senior Notes, Series 2010A, due 2040 | 15,000 | 15,000 |
| 4.00% - 4.50% York County Industrial Development Authority Exempt Facilities Revenue Bonds, Series 2015, due 2029 - 2045 | 10,000 | 10,000 |
| Committed Line of Credit, due 2019 | 5,389 | — |
| Total long-term debt | 92,833 | 87,488 |
| Less discount on issuance of long-term debt | (215) | (226) |
| Less unamortized debt issuance costs | (2,476) | (2,609) |
| Less current maturities | (44) | (44) |
| Long-term portion | \$90,098 | \$84,609 |

Payments due by year as of December 31, 2017:

| 2018 | 2019 | 2020 | 2021 | 2022 |
|-------|----------|---------|------|---------|
| \$ 44 | \$28,419 | \$6,500 | \$ - | \$7,500 |

Payments due in 2019 include payback of the committed line of credit. The committed line of credit is reviewed annually, and upon favorable outcome, would likely be extended for another year. Payments due in 2019 also include potential payments of \$12,000 on the variable rate bonds (due 2029) which would only be payable if all bonds were tendered and could not be remarketed. There is currently no such indication of this happening.

Fixed Rate Long-Term Debt

The Pennsylvania Economic Development Financing Authority, or PEDFA, Series 2014 Bonds contain both optional and special redemption provisions. Under the optional provisions, the Company can redeem all or a portion of the bonds on or after May 1, 2019. Under the special provisions, representatives of deceased beneficial owners of the bonds have the right to request redemption prior to the stated maturity of all or part of their interest in the bonds beginning on or after May 1, 2014. The Company is not obligated to redeem any individual interest exceeding \$25, or aggregate interest exceeding \$300, in any annual period. In 2017, no bonds were retired under these provisions. In 2016, the Company retired \$10 of the bonds under these provisions. In 2015, no bonds were retired under these provisions. Currently, no additional bonds that meet the special provisions have been tendered for redemption.

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Variable Rate Long-Term Debt

On May 7, 2008, the PEDFA issued \$12,000 aggregate principal amount of PEDFA Exempt Facilities Revenue Refunding Bonds, Series A of 2008 (the "Series A Bonds") for the Company's benefit pursuant to the terms of a trust indenture, dated as of May 1, 2008, between the PEDFA and Manufacturers and Traders Trust Company, as trustee.

The PEDFA then loaned the proceeds of the offering of the Series A Bonds to the Company pursuant to a loan agreement, dated as of May 1, 2008, between the Company and the PEDFA. The loan agreement provides for a \$12,000 loan with a maturity date of October 1, 2029. Amounts outstanding under the loan agreement are the Company's direct general obligations. The proceeds of the loan were used to redeem the PEDFA Exempt Facilities Revenue Bonds, Series B of 2004 (the "2004 Series B Bonds"). The 2004 Series B Bonds were redeemed because the bonds were tendered and could not be remarketed due to the downgrade of the bond insurer's credit rating.

Borrowings under the loan agreement bear interest at a variable rate as determined by PNC Capital Markets, as remarketing agent, on a periodic basis elected by the Company, which has currently elected that the interest rate be determined on a weekly basis. The remarketing agent determines the interest rate based on the current market conditions in order to determine the lowest interest rate which would cause the Series A Bonds to have a market value equal to the principal amount thereof plus accrued interest thereon. The variable interest rate under the loan agreement averaged 0.88% in 2017, 0.47% in 2016, and 0.06% in 2015. As of December 31, 2017 and 2016, the interest rate was 1.78% and 0.80%, respectively.

The holders of the \$12,000 Series A Bonds may tender their bonds at any time. When the bonds are tendered, they are subject to an annual remarketing agreement, pursuant to which a remarketing agent attempts to remarket the tendered bonds according to the terms of the indenture. In order to keep variable interest rates down and to enhance the marketability of the Series A Bonds, the Company entered into a Reimbursement, Credit and Security Agreement with PNC Bank, National Association ("the Bank") dated as of May 1, 2008. This agreement provides for a direct pay letter of credit issued by the Bank to the trustee for the Series A Bonds. The Bank is responsible for providing the trustee with funds for the timely payment of the principal and interest on the Series A Bonds and for the purchase price of the Series A Bonds that have been tendered or deemed tendered for purchase and have not been remarketed. The Company's responsibility is to reimburse the Bank the same day as regular interest payments are made, and within fourteen months for the purchase price of tendered bonds that have not been remarketed. The reimbursement period for the principal is immediate at maturity, upon default by the Company, or if the Bank does not renew the Letter of Credit. The current expiration date of the Letter of Credit is June 30, 2019. It is reviewed annually for a potential extension of the expiration date.

The Company may elect to have the Series A Bonds redeemed, in whole or in part, on any date that interest is payable for a redemption price equal to the principal amount thereof plus accrued interest to the date of redemption. The Series A Bonds are also subject to mandatory redemption for the same redemption price in the event that the IRS determines that the interest payable on the Series A Bonds is includable in gross income of the holders of the bonds for federal tax purposes.

Interest Rate Swap Agreement

In connection with the issuance of the PEDFA 2004 Series B Bonds, the Company entered into an interest rate swap agreement with a counterparty, in the notional principal amount of \$12,000. The Company elected to retain the swap agreement for the 2008 Series A Bonds. Interest rate swap agreements derive their value from underlying interest rates. These transactions involve both credit and market risk. The notional amounts are amounts on which calculations, payments, and the value of the derivative are based. Notional amounts do not represent direct credit exposure. Direct credit exposure is limited to the net difference between the calculated amounts to be received and paid, if any. Such difference, which represents the fair value of the swap, is reflected on the Company's balance sheets. See Note 11 for additional information regarding the fair value of the swap.

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The interest rate swap will terminate on the maturity date of the 2008 Series A Bonds (which is the same date as the maturity date of the loan under the loan agreement), unless sooner terminated pursuant to its terms. In the event the interest rate swap terminates prior to the maturity date of the 2008 Series A Bonds, either the Company or the swap counterparty may be required to make a termination payment to the other based on market conditions at such time. The Company is exposed to credit-related losses in the event of nonperformance by the counterparty. The Company controls the credit risk of its financial contracts through credit approvals, limits and monitoring procedures, and does not expect the counterparty to default on its obligations. Notwithstanding the terms of the swap agreement, the Company is ultimately obligated for all amounts due and payable under the loan agreement.

The interest rate swap agreement contains provisions that require the Company to maintain a credit rating of at least BBB- with Standard & Poor's. On April 21, 2017 Standard & Poor's affirmed the Company's credit rating at A-, with a stable outlook and adequate liquidity. If the Company's rating were to fall below this rating, it would be in violation of these provisions, and the counterparty to the derivative could request immediate payment if the derivative was in a liability position. The Company's interest rate swap was in a liability position as of December 31, 2017. If a violation was triggered on December 31, 2017, the Company would have been required to pay the counterparty approximately \$2,239.

The Company's interest rate swap agreement provides that it pay the counterparty a fixed interest rate of 3.16% on the notional amount of \$12,000. In exchange, the counterparty pays the Company a floating interest rate (based on 59% of the U.S. Dollar one-month LIBOR rate) on the notional amount. The floating interest rate paid to the Company is intended, over the term of the swap, to approximate the variable interest rate on the loan agreement and the interest rate paid to bondholders, thereby managing its exposure to fluctuations in prevailing interest rates. The Company's net payment rate on the swap averaged 2.50% in 2017, 2.86% in 2016 and 3.06% in 2015.

As of December 31, 2017, there was a spread of 91 basis points between the variable rate paid to bondholders and the variable rate received from the swap counterparty, which equated to an overall effective rate of 4.07% (including variable interest and swap payments). As of December 31, 2016, there was a spread of 39 basis points which equated to an overall effective rate of 3.55% (including variable interest and swap payments).

Line of Credit Borrowings

As of December 31, 2017, the Company maintained unsecured lines of credit aggregating \$41,500 with four banks. The first line of credit, in the amount of \$13,000, is a committed line of credit with a revolving 2-year maturity (currently May 2019), and carries an interest rate of LIBOR plus 1.20%. The Company had 5,389 outstanding under this line of credit as of December 31, 2017. The second line of credit, in the amount of \$11,000, is a committed line of credit, which matures in May 2019 and carries an interest rate of LIBOR plus 1.25%. The third line of credit, in the amount of \$7,500, is a committed line of credit, which matures in June 2018 and carries an interest rate of LIBOR plus 1.25%. The fourth line of credit, in the amount of \$10,000, is a committed line of credit, which matures in September 2018 and carries an interest rate of LIBOR plus 1.20%. The Company had \$1,000 outstanding under this line of credit as of December 31, 2017. Average borrowings outstanding under the lines of credit were \$3,132 in 2017. The average cost of borrowings under the lines of credit during 2017 was 1.76%. The weighted average interest rate on the line of credit borrowings as of December 31, 2017 was 2.65%.

Debt Covenants and Restrictions

The terms of the debt agreements carry certain covenants and limit in some cases the Company's ability to borrow additional funds, to prepay its borrowings and include certain restrictions with respect to declaration and payment of cash dividends and the Company's acquisition of its stock. Under the terms of the most restrictive agreements, the Company cannot borrow in excess of 60% of its utility plant, and cumulative payments for dividends and acquisition of stock since December 31, 1982 may not exceed \$1,500 plus net income since that date. As of December 31, 2017, none of the earnings retained in the business are restricted under these provisions. The Company's Pennvest Loan is secured by \$800 of receivables. Other than this loan, the Company's debt is unsecured.

The Company's lines of credit require it to maintain a minimum equity to total capitalization ratio (defined as the sum of equity plus funded debt) and a minimum interest coverage ratio (defined as net income plus interest expense plus income tax expense divided by interest expense). As of December 31, 2017, the Company was in compliance with these covenants.

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5. Common Stock and Earnings Per Share

Net income of \$12,974, \$11,846 and \$12,489 for the years ended December 31, 2017, 2016 and 2015 respectively, is used to calculate both basic and diluted earnings per share. Basic net income per share is based on the weighted average number of common shares outstanding. Diluted net income per share is based on the weighted average number of common shares outstanding plus potentially dilutive shares. The dilutive effect of employee stock-based compensation is included in the computation of diluted net income per share. The dilutive effect of stock-based compensation is calculated using the treasury stock method and expected proceeds upon exercise or issuance of the stock-based compensation. The following table summarizes the shares used in computing basic and diluted net income per share:

| | 2017 | 2016 | 2015 |
|---|------------|------------|------------|
| Weighted average common shares, basic | 12,849,123 | 12,845,955 | 12,831,687 |
| Effect of dilutive securities: | | | |
| Employee stock-based compensation | 48 | 18 | - |
| Weighted average common shares, diluted | 12,849,171 | 12,845,973 | 12,831,687 |

Under the employee stock purchase plan, all full-time employees who have been employed at least ninety consecutive days may purchase shares of the Company's common stock limited to 10% of gross compensation. The purchase price is 95% of the fair market value (as defined). Shares issued during 2017, 2016 and 2015 were 4,770, 5,115 and 7,417, respectively. As of December 31, 2017, 70,826 authorized shares remain unissued under the plan.

The Company has a Dividend Reinvestment and Direct Stock Purchase and Sale Plan ("the Plan"), which is available to both current shareholders and the general public. On October 3, 2016, the Company filed a Registration Statement on Form S-3 with the Securities and Exchange Commission (SEC) to authorize an additional 331,000 shares and rollover the unissued 170,240 shares authorized under the 2013 Form S-3, for issuance under the new Prospectus for the Plan. In addition to providing more shares for the Plan, the new Prospectus identified a change in the Company's stock transfer agent. Under the optional dividend reinvestment portion of the Plan, holders of the Company's common stock may purchase additional shares instead of receiving cash dividends. The purchase price is 95% of the fair market value (as defined). Under the direct stock purchase portion of the Plan, purchases were made weekly at 100% of the stock's fair market value through October 19, 2016. Beginning in November 2016, purchases are made monthly at 100% of the stock's fair market value, as defined in the new Prospectus. Other provisions of the Plan were left substantially unchanged. The Registration Statement was declared effective by the SEC on November 16, 2016. Shares issued during 2017, 2016 and 2015 under both Prospectuses were 51,401, 80,343 and 95,451, respectively. As of December 31, 2017, 441,238 authorized shares remain unissued under the plan.

On March 11, 2013, the Board of Directors, or the Board, authorized a share repurchase program granting the Company authority to repurchase up to 1,200,000 shares of the Company's common stock from time to time. The stock repurchase program has no specific end date and the Company may repurchase shares in the open market or through privately negotiated transactions. The Company may suspend or discontinue the repurchase program at any time. During 2017, 2016 and 2015, the Company repurchased and retired 37,229, 46,771 and 121,012 shares, respectively. As of December 31, 2017, 618,004 shares remain available for repurchase.

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6. Stock Based Compensation

On May 2, 2016, the Company's stockholders approved The York Water Company Long-Term Incentive Plan, or LTIP. The LTIP was adopted to provide the incentive of long-term stock-based awards to officers, directors and key employees. The LTIP provides for the granting of nonqualified stock options, incentive stock options, stock appreciation rights, performance restricted stock grants and units, restricted stock grants and units, and unrestricted stock grants. A maximum of 100,000 shares of common stock may be issued under the LTIP over the ten-year life of the plan. The maximum number of shares of common stock subject to awards that may be granted to any participant in any one calendar year is 2,000. Shares of common stock issued under the LTIP may be treasury shares or authorized but unissued shares. The LTIP is administered by the Compensation Committee of the Board, or the full Board, provided that the full Board administers the LTIP as it relates to awards to non-employee directors of the Company. The Company filed a registration statement with the SEC on May 11, 2016 covering the offering of stock under the LTIP. The LTIP was effective on July 1, 2016.

On November 21, 2016, the Board awarded stock to non-employee directors effective November 28, 2016. This stock award vested immediately. On the same date, the Compensation Committee awarded restricted stock to officers and key employees effective November 28, 2016. This restricted stock award vests ratably over three years beginning November 28, 2016.

On April 26, 2017, the Board awarded stock to non-employee directors effective May 1, 2017. This stock award vested immediately. On April 26, 2017, the Compensation Committee awarded restricted stock to officers and key employees effective May 1, 2017. This restricted stock award vests ratably over three years beginning May 1, 2017. In addition, the Board of Directors accelerated the vesting period for restricted stock granted in 2016 to two retiring officers from three years to their 2017 retirement dates, both of which have been fully recognized as of December 31, 2017.

The restricted stock awards provide the grantee with the rights of a shareholder, including the right to receive dividends and to vote such shares, but not the right to sell or otherwise transfer the shares during the restriction period. As a result, the awards are included in common shares outstanding on the balance sheet. Restricted stock awards result in compensation expense valued at the fair market value of the stock on the date of the grant and are amortized ratably over the restriction period.

The following table summarizes the stock grant amounts and activity for the years ended December 31, 2016 and 2017.

| | Number of Shares | Grant Date Weighted Average Fair Value |
|---|------------------------|---|
| Nonvested at beginning of the year 2016 | - | - |
| Granted | 1,231 | \$ 37.20 |
| Vested | (571) | \$ 37.20 |
| Forfeited | - | - |
| Nonvested at end of the year 2016 | 660 | \$ 37.20 |
| Granted | 1,505 | \$ 38.00 |
| Vested | (1,038) | \$ 37.75 |
| Forfeited | - | - |
| Nonvested at end of the year 2017 | 1,127 | \$ 37.76 |

For the years ended December 31, 2017 and 2016, the statement of income includes \$46 and \$22 of stock based compensation and related recognized tax benefits of \$18 and \$9, respectively. The total fair value of the shares vested in the years ended December 31, 2017 and 2016 was \$39 and \$21, respectively. Total stock based compensation related to nonvested awards not yet recognized is \$35 at December 31, 2017 which will be recognized over the remaining three year vesting period.

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7. Employee Benefit Plans

Pensions

The Company maintains a general and administrative and a union-represented defined benefit pension plan covering all of its employees hired prior to May 1, 2010. Employees hired after May 1, 2010 are eligible for an enhanced 401(k) plan rather than a defined benefit plan. The benefits under the defined benefit plans are based upon years of service and compensation near retirement. The Company amended its defined benefit pension plans in 2014, generally limiting the years of eligible service under the plans to 30 years. The Company's funding policy is to contribute annually the amount permitted by the PPUC to be collected from customers in rates, but in no case less than the minimum Employee Retirement Income Security Act (ERISA) required contribution.

The following table sets forth the plans' funded status as of December 31, 2017 and 2016. The measurement of assets and obligations of the plans is as of December 31, 2017 and 2016.

| Obligations and Funded Status At December 31 | 2017 | 2016 |
|---|------------|------------|
| Change in Benefit Obligation | | |
| Pension benefit obligation beginning of year | \$40,754 | \$39,469 |
| Service cost | 1,080 | 1,018 |
| Interest cost | 1,592 | 1,599 |
| Actuarial (gain) loss | 2,645 | (43) |
| Benefit payments | (1,435) | (1,289) |
| Pension benefit obligation end of year | 44,636 | 40,754 |
| Change in Plan Assets | | |
| Fair value of plan assets beginning of year | 35,467 | 31,835 |
| Actual return on plan assets | 5,107 | 2,621 |
| Employer contributions | 2,300 | 2,300 |
| Benefits paid | (1,435) | (1,289) |
| Fair value of plan assets end of year | 41,439 | 35,467 |
| Funded Status of Plans at End of Year | \$(3,197) | \$(5,287) |

The accounting standards require that the funded status of defined benefit pension plans be fully recognized on the balance sheets. They also call for the unrecognized actuarial gain or loss, the unrecognized prior service cost and the unrecognized transition costs to be adjustments to shareholders' equity (accumulated other comprehensive income). Due to a rate order granted by the PPUC, the Company is permitted under the accounting standards to defer the charges otherwise recorded in accumulated other comprehensive income as a regulatory asset. Management believes these costs will be recovered in future rates charged to customers. The liability for the funded status of the Company's pension plans is recorded in "Deferred employee benefits" on its balance sheets.

In 2017, the plans recognized a significant actuarial loss. The Company adopted the new mortality improvement scale (MP-2017) and recognized a 50 basis point decrease in the discount rate. In 2016, the plans recognized a small actuarial gain. The Company adopted the new mortality improvement scale (MP-2016), but recognized a 20 basis point decrease in the discount rate and lowered the expected long-term return on plan assets from 7.00% to 6.75%. The Company uses the corridor method to amortize actuarial gains and losses. Gains and losses over 10% of the greater of pension benefit obligation or the market value of assets are amortized over the average future service of plan participants expected to receive benefits.

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Changes in plan assets and benefit obligations recognized in regulatory assets are as follows:

| | 2017 | 2016 |
|---|---------|---------|
| Net gain arising during the period | \$(66) | \$(432) |
| Recognized net actuarial loss | (493) | (561) |
| Recognized prior service credit | 13 | 13 |
| Total changes in regulatory asset during the year | \$(546) | \$(980) |

Amounts recognized in regulatory assets that have not yet been recognized as components of net periodic benefit cost consist of the following at December 31:

| | 2017 | 2016 |
|----------------------|---------|---------|
| Net loss | \$8,895 | \$9,454 |
| Prior service credit | (101) | (114) |
| Regulatory asset | \$8,794 | \$9,340 |

Components of net periodic benefit cost are as follows:

| | 2017 | 2016 | 2015 |
|--------------------------------------|---------|---------|---------|
| Service cost | \$1,080 | \$1,018 | \$1,166 |
| Interest cost | 1,592 | 1,599 | 1,515 |
| Expected return on plan assets | (2,395) | (2,233) | (2,229) |
| Amortization of loss | 493 | 561 | 705 |
| Amortization of prior service credit | (13) | (13) | (13) |
| Rate-regulated adjustment | 1,543 | 1,368 | 1,156 |
| Net periodic benefit cost | \$2,300 | \$2,300 | \$2,300 |

The rate-regulated adjustment set forth above is required in order to reflect pension expense for the Company in accordance with the method used in establishing water rates. The Company is permitted by rate order of the PPUC to expense pension costs to the extent of contributions and defer the remaining expense to regulatory assets to be collected in rates at a later date as additional contributions are made. During 2017, the deferral decreased by \$1,543.

The estimated costs for the defined benefit pension plans relating to the December 31, 2017 balance sheet that will be amortized from regulatory assets into net periodic benefit cost over the next fiscal year are as follows:

| | |
|--------------------------|-------|
| Net loss | \$453 |
| Net prior service credit | (13) |
| | 440 |

The Company plans to contribute \$2,300 to the plans in 2018.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid in each of the next five years and the subsequent five years in the aggregate:

| 2018 | 2019 | 2020 | 2021 | 2022 | 2023-2027 |
|---------|---------|---------|---------|---------|-----------|
| \$1,714 | \$1,852 | \$1,865 | \$1,928 | \$2,007 | \$11,717 |

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The following tables show the projected benefit obligation, the accumulated benefit obligation and the fair value of plan assets as of December 31:

| | 2017 | 2016 |
|------------------------------|----------|----------|
| Projected benefit obligation | \$44,636 | \$40,754 |
| Fair value of plan assets | 41,439 | 35,467 |

| | 2017 | 2016 |
|--------------------------------|----------|----------|
| Accumulated benefit obligation | \$41,390 | \$37,822 |
| Fair value of plan assets | 41,439 | 35,467 |

Weighted-average assumptions used to determine benefit obligations at December 31:

| | 2017 | 2016 |
|-------------------------------|---------------|---------------|
| Discount rate | 3.50% | 4.00% |
| Rate of compensation increase | 2.50% - 3.00% | 2.50% - 3.00% |

Weighted-average assumptions used to determine net periodic benefit cost for years ended December 31:

| | 2017 | 2016 | 2015 |
|--|---------------|---------------|-------|
| Discount rate | 4.00% | 4.20% | 3.80% |
| Expected long-term return on plan assets | 6.75% | 6.75% | 7.00% |
| Rate of compensation increase | 2.50% - 3.00% | 2.50% - 3.00% | 3.00% |

The selected long-term rate of return on plan assets was primarily based on the asset allocation of each of the plan's assets (approximately 50% to 70% equity securities and 30% to 50% fixed income securities). Analysis of the historic returns of these asset classes and projections of expected future returns were considered in setting the long-term rate of return.

The investment objective of the Company's defined benefit pension plans is that of Growth and Income. The weighted-average target asset allocations are 50% to 70% equity securities, 30% to 50% fixed income securities, and 0% to 10% reserves (cash and cash equivalents). Within the equity category, the Company's target allocation is approximately 60-95% large cap, 0-25% mid cap, 0-10% small cap, 0-25% International Developed Nations, and 0-10% International Emerging Nations. Within the fixed income category, its target allocation is approximately 15-55% U.S. Treasuries, 0-22% Federal Agency securities, 0-40% corporate bonds, 15-55% mortgage-backed securities, 0-20% international, and 0-20% high yield bonds. The Company's investment performance objectives over a three to five year period are to exceed the annual rate of inflation as measured by the Consumer Price Index by 3%, and to exceed the annualized total return of specified benchmarks applicable to the funds within the asset categories.

Further guidelines within equity securities include: (1) holdings in any one company cannot exceed 5% of the portfolio; (2) a minimum of 20 individual stocks must be included in the domestic stock portfolio; (3) a minimum of 30 individual stocks must be included in the international stock portfolio; (4) equity holdings in any one industry cannot exceed 20-25% of the portfolio; and (5) only U.S.-denominated currency securities are permitted.

Further guidelines for fixed income securities include: (1) fixed income holdings in a single issuer are limited to 5% of the portfolio; (2) acceptable investments include money market securities, U.S. Government and its agencies and sponsored entities' securities, mortgage-backed and asset-backed securities, corporate securities and mutual funds offering high yield bond portfolios; (3) purchases must be limited to investment grade or higher; (4) non-U.S. dollar denominated securities are not permissible; and (5) high risk derivatives are prohibited.

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The fair values of the Company's pension plan assets at December 31, 2017 and 2016 by asset category and fair value hierarchy level are as follows. The majority of the valuations are based on quoted prices on active markets (Level 1), with the remaining valuations based on broker/dealer quotes, active market makers, models, and yield curves (Level 2).

| <u>Asset Category</u> | Total Fair Value | | Quoted Prices in Active Markets for Identical Assets (Level 1) | | Significant Other Observable Inputs (Level 2) | |
|---------------------------------|------------------|----------|--|----------|---|---------|
| | 2017 | 2016 | 2017 | 2016 | 2017 | 2016 |
| Cash and Money Market Funds (a) | \$1,968 | \$635 | \$1,968 | \$635 | \$- | \$- |
| <u>Equity Securities:</u> | | | | | | |
| Common Equity Securities (b) | 2,606 | 2,969 | 2,606 | 2,969 | - | - |
| Equity Mutual Funds (c) | 23,416 | 21,107 | 23,416 | 21,107 | - | - |
| <u>Fixed Income Securities:</u> | | | | | | |
| U.S. Treasury Obligations | 1,106 | 853 | - | - | 1,106 | 853 |
| Corporate and Foreign Bonds (d) | 5,153 | 3,439 | - | - | 5,153 | 3,439 |
| Fixed Income Mutual Funds (e) | 7,190 | 6,464 | 7,190 | 6,464 | - | - |
| Total Plan Assets | \$41,439 | \$35,467 | \$35,180 | \$31,175 | \$6,259 | \$4,292 |

(a) The portfolios are designed to keep up to one year of distributions in immediately available funds. The Company was more heavily-weighted in cash as of December 31, 2017 due to the timing of employer contributions.

(b) This category includes investments in U.S. common stocks and foreign stocks trading in the U.S. widely distributed among consumer discretionary, consumer staples, healthcare, information technology, financial services, telecommunications, industrials, materials, and energy. The individual stocks are primarily large cap stocks which track with the S&P 500.

(c) This category currently includes a majority of investments in closed-end mutual funds as well as domestic equity mutual funds and international mutual funds which give the portfolio exposure to mid and large cap index funds as well as international diversified index funds.

(d) This category currently includes only U.S. corporate bonds and notes widely distributed among consumer discretionary, consumer staples, healthcare, information technology and financial services.

(e) This category includes fixed income investments in mutual funds which include government, corporate and mortgage securities of both the U.S. and other countries. The mortgage-backed securities and non-U.S. corporate and sovereign investments add further diversity to the fixed income portion of the portfolio.

Defined Contribution Plan

The Company has a savings plan pursuant to the provisions of section 401(k) of the Internal Revenue Code. For employees hired before May 1, 2010, this plan provides for elective employee contributions of up to 15% of compensation and Company matching contributions of 100% of the participant's contribution, up to a maximum annual Company contribution of \$2.8 for each employee.

Employees hired after May 1, 2010 are entitled to an enhanced feature of the plan. This feature provides for elective employee contributions of up to 15% of compensation and Company matching contributions of 100% of the participant's contribution, up to a maximum of 4% of the employee's compensation. In addition, the Company will make an annual contribution of \$1.2 to each employee's account whether or not they defer their own compensation. Employees eligible for this enhanced 401(k) plan feature are not eligible for the defined benefit plans. As of

December 31, 2017, thirty employees were participating in the enhanced feature of the plan. The Company's contributions to both portions of the plan amounted to \$266 in 2017, \$261 in 2016, and \$262 in 2015.

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Deferred Compensation

The Company has non-qualified deferred compensation and supplemental retirement agreements with certain members of management. The future commitments under these arrangements are offset by corporate-owned life insurance policies. At December 31, 2017 and 2016, the present value of the future obligations was approximately \$3,981 and \$3,894, respectively. The insurance policies included in other assets had a total cash value of approximately \$3,152 and \$2,830 at December 31, 2017 and 2016, respectively. The Company's net expenses under the plans amounted to \$252 in 2017, \$557 in 2016 and \$380 in 2015.

Other

The Company has a retiree life insurance program which pays the beneficiary of a retiree \$2 upon the retiree's death. At December 31, 2017 and 2016, the present value of the future obligations was approximately \$120 and \$103, respectively. There is no trust or insurance covering this future liability, instead the Company will pay these benefits out of its general assets. The Company's net (income) expenses under the plan amounted to \$19 in 2017, \$9 in 2016 and \$(4) in 2015.

8. Rate Matters

From time to time, the Company files applications for rate increases with the PPUC and is granted rate relief as a result of such requests. Most recently, the PPUC authorized an increase in rates effective February 28, 2014. The Company anticipates that it will file a rate increase request in 2018.

The PPUC permits water utilities to collect a distribution system improvement charge, or DSIC. The DSIC allows the Company to add a charge to customers' bills for qualified replacement costs of certain infrastructure without submitting a rate filing. This surcharge mechanism typically adjusts periodically based on additional qualified capital expenditures completed or anticipated in a future period. The DSIC is capped at 5% of base rates, and is reset to zero when new base rates that reflect the costs of those additions become effective or when a utility's earnings exceed a regulatory benchmark. The surcharge reset to zero when the new base rates took effect in February 28, 2014. The Company's earnings are currently below the regulatory benchmark, allowing the Company to collect DSIC. The DSIC provided revenues of \$899 in 2017, \$0 in 2016, and \$0 in 2015. The DSIC is subject to audit by the PPUC.

9. Notes Receivable and Customers' Advances for Construction

The Company entered into an agreement with a municipality to extend water service into a previously formed water district. The Company loaned funds to the municipality to cover the costs related to the project. The municipality concurrently advanced these funds back to the Company in the form of customers' advances for construction. The municipality is required by enacted ordinance to charge application fees and water revenue surcharges (fees) to customers connected to the system, which are remitted to the Company. The note principal and the related customer advance are reduced periodically as operating revenues are earned by the Company from customers connected to the system and refunds of the advance are made. There is no due date for the notes or expiration date for the advance.

The Company recorded interest income of \$98 in 2017, \$100 in 2016 and \$110 in 2015. The interest rate on the note outstanding at December 31, 2017 is 7.5%.

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Included in the accompanying balance sheets at December 31, 2017 and 2016 were the following amounts related to this project.

| | 2017 | 2016 |
|--------------------------------------|-------|-------|
| Notes receivable, including interest | \$255 | \$255 |
| Customers' advances for construction | 306 | 307 |

The Company has other customers' advances for construction totaling \$6,018 and \$6,795 at December 31, 2017 and 2016, respectively.

10. Commitments

Based on its capital budget, the Company anticipates construction and acquisition expenditures for 2018 and 2019 of approximately \$22,564 and \$19,755, respectively, exclusive of any acquisitions not yet approved. The Company plans to finance ongoing capital expenditures with internally-generated funds, borrowings against the Company's lines of credit, proceeds from the issuance of common stock under its dividend reinvestment and direct stock purchase and sale plan and ESPP, potential common stock or debt issues and customer advances and contributions.

The Company has committed a total of approximately \$6,126 for an additional untreated water pumping station, of which \$582 remains to be incurred as of December 31, 2017. The Company may make additional commitments for this project in 2018.

During its triennial testing completed in 2016, the Company determined it exceeded the action level for lead as established by the Lead and Copper Rule, or LCR, issued by the U.S. Environmental Protection Agency. The rule allows the Company to have five samples of the 50 high-risk homes tested exceed the action level of 15 parts per billion, or PPB. The testing found that six properties with lead service lines, all built before 1935, exceeded the action level, and the reported exceedance amount was 1 PPB. The Company determined that only 3% of the company-owned service lines in the system were lead. The Company is required, per the LCR, to engage in more frequent testing for lead, public education, and annually replace 7% of the remaining company-owned lead service lines in its distribution system. The Company completed two rounds of compliance testing at the customer's tap in 2017 and the water samples did not exceed the action level either time. As a result, the Company will reduce its monitoring from semi-annual to annual beginning in 2018.

The Company is performing in excess of the required actions under the LCR. Specifically, the Company is providing the affected customers with a free water test and a 200 gallon per month credit to flush their line in order to reduce any lead content until their lead service line has been replaced. The cost of the water tests and flushing credits was \$16 and \$9 for the years ended December 31, 2017 and 2016, respectively. Additional amounts for water tests and flushing credits are not expected to have a material impact on the financial position of the Company over the remaining three years.

In addition, the Company entered into a consent order agreement with the Pennsylvania Department of Environmental Protection in December 2016. Under the agreement, the Company committed to exceed the LCR replacement schedule by replacing all of the remaining known company-owned lead service lines within four years from the agreement. The cost for these service line replacements was approximately \$1,390 and \$75 for the years ended December 31, 2017 and 2016, respectively, and is included in utility plant. Additional costs of approximately \$535 are expected until the replacements are complete, and will be integrated into the Company's annual capital budgets.

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Finally, the Company was granted approval by the PPUC to modify its tariff to include the cost of the replacement of lead customer-owned service lines that are discovered when the Company replaces its lead service lines over the remaining three years, and to include the cost of the annual replacement of up to 400 lead customer-owned service lines whenever they are discovered, regardless of the material used for the company-owned service line over nine years. The tariff modification allows the Company to replace customer-owned service lines at its own initial cost. The Company will record the costs as a regulatory asset to be recovered in future base rates to customers, over a reasonable period of at least four but not more than six years. The cost for the customer-owned lead service line replacements under the four-year tariff modification was approximately \$191 through December 31, 2017 and is included as a regulatory asset. Additional replacements are expected to be approximately \$75 under the four-year tariff modification, assuming the average percentage of customer-owned lead service lines that were replaced when company-owned lead service lines were replaced through December 31, 2017 remains consistent over the entire replacement period.. The Company is unable to predict how many lead customer-owned service lines are in use, and, therefore, its current estimate of \$1,040 for replacements under the nine-year tariff modification is subject to adjustment as more facts become available.

As of December 31, 2017, approximately 34% of the Company's full time employees are under union contract. The current contract was ratified in December 2017 and expires on April 30, 2020.

The Company is involved in certain legal and administrative proceedings before various courts and governmental agencies concerning water service and other matters. The Company expects that the ultimate disposition of these proceedings will not have a material effect on the Company's financial position, results of operations and cash flows.

11. Fair Value of Financial Instruments

The accounting standards regarding fair value measurements establish a fair value hierarchy which indicates the extent to which inputs used in measuring fair value are observable in the market. Level 1 inputs include quoted prices for identical instruments and are the most observable. Level 2 inputs include quoted prices for similar assets and observable inputs such as interest rates, commodity rates and yield curves. Level 3 inputs are not observable in the market and include management's own judgments about the assumptions market participants would use in pricing the asset or liability.

The Company has recorded its interest rate swap liability at fair value in accordance with the standards. The liability is recorded under the caption "Other deferred credits" on the balance sheets. The table below illustrates the fair value of the interest rate swap as of the end of the reporting period.

| Description | December 31, 2017 | Fair Value Measurements at Reporting Date Using Significant Other Observable Inputs (Level 2) |
|--------------------|-------------------|--|
| Interest Rate Swap | \$2,196 | \$2,196 |

Fair values are measured as the present value of all expected future cash flows based on the LIBOR-based swap yield curve as of the date of the valuation. These inputs to this calculation are deemed to be Level 2 inputs. The balance sheet carrying value reflects the Company's credit quality as of December 31, 2017. The rate used in discounting all prospective cash flows anticipated to be made under this swap reflects a representation of the yield to maturity for 30-year debt on utilities rated A- as of December 31, 2017. The use of the Company's credit quality resulted in a reduction in the swap liability of \$43 as of December 31, 2017. The fair value of the swap reflecting the Company's credit quality as of December 31, 2016 is shown in the table below.

| Description | December 31, 2016 | Fair Value Measurements at Reporting Date Using |
|-------------|-------------------|--|
|-------------|-------------------|--|

| | |
|----------------------------|--|
| | Significant Other Observable Inputs (Level 2) |
| Interest Rate Swap \$2,292 | \$2,292 |

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The carrying amount of current assets and liabilities that are considered financial instruments approximates fair value as of the dates presented. The Company's total long-term debt, with a carrying value of \$92,833 at December 31, 2017, and \$87,488 at December 31, 2016, had an estimated fair value of approximately \$108,000 and \$99,000, respectively. The estimated fair value of debt was calculated using a discounted cash flow technique that incorporates a market interest yield curve with adjustments for duration and risk profile. These inputs to this calculation are deemed to be Level 2 inputs. The Company recognized its credit rating in determining the yield curve, and did not factor in third party credit enhancements including bond insurance on the 2006 York County Industrial Development Authority issue and the letter of credit on the 2008 PEDFA Series A issue.

Customers' advances for construction and notes receivable have carrying values at December 31, 2017 of \$6,324 and \$255, respectively. At December 31, 2016, customers' advances for construction and notes receivable had carrying values of \$7,102 and \$255, respectively. The relative fair values of these amounts cannot be accurately estimated since the timing of future payment streams is dependent upon several factors, including new customer connections, customer consumption levels and future rate increases.

12. Taxes Other than Income Taxes

The following table provides the components of taxes other than income taxes:

| | 2017 | 2016 | 2015 |
|-------------------------------------|---------|---------|---------|
| Regulatory Assessment | \$231 | \$243 | \$242 |
| Property | 344 | 339 | 334 |
| Payroll, net of amounts capitalized | 539 | 530 | 510 |
| Capital Stock | - | 1 | 42 |
| Other | 19 | 1 | 1 |
| Total taxes other than income taxes | \$1,133 | \$1,114 | \$1,129 |

13. Selected Quarterly Financial Data (Unaudited)

| | First | Second | Third | Fourth | Year |
|------------------------------|----------|----------|----------|----------|----------|
| <u>2017</u> | | | | | |
| Operating revenues | \$11,290 | \$12,254 | \$12,692 | \$12,353 | \$48,589 |
| Operating income | 4,857 | 5,529 | 6,147 | 5,940 | 22,473 |
| Net income | 2,581 | 2,935 | 3,931 | 3,527 | 12,974 |
| Basic earnings per share | 0.20 | 0.23 | 0.31 | 0.27 | 1.01 |
| Diluted earnings per share | 0.20 | 0.23 | 0.31 | 0.27 | 1.01 |
| Dividends declared per share | 0.1602 | 0.1602 | 0.1602 | 0.1666 | 0.6472 |
| <u>2016</u> | | | | | |
| Operating revenues | \$11,278 | \$11,820 | \$12,601 | \$11,885 | \$47,584 |
| Operating income | 5,214 | 5,695 | 6,414 | 5,565 | 22,888 |
| Net income | 2,486 | 2,847 | 3,571 | 2,942 | 11,846 |
| Basic earnings per share | 0.19 | 0.23 | 0.27 | 0.23 | 0.92 |
| Diluted earnings per share | 0.19 | 0.23 | 0.27 | 0.23 | 0.92 |
| Dividends declared per share | 0.1555 | 0.1555 | 0.1555 | 0.1602 | 0.6267 |

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None.

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Item 9A. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

The Company's management, with the participation of the Company's President and Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based upon this evaluation, the Company's President and Chief Executive Officer along with the Chief Financial Officer concluded that the Company's disclosure controls and procedures as of the end of the period covered by this report are effective such that the information required to be disclosed by the Company in reports filed under the Securities Exchange Act of 1934 is (i) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to the Company's management, including the President and Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding disclosure. A controls system cannot provide absolute assurance, however, that the objectives of the controls system are met, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

During the Company's most recent fiscal quarter, the Company made changes to its internal control with regards to revenue recognition and income taxes. With regards to revenue recognition, the Company added internal controls over the adoption of Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers. The focus is on adoption of the final evaluation of the applicability of this standard to the Company by management and the Audit Committee for proper disclosure in this Annual Report, including the impact on its financial position, results of operations and cash flows and transition method. It also includes the internal controls over disclosures that will be applicable in 2018 and the review of new revenue streams or changes to revenue streams under the new standard. With regards to income taxes, the Company added internal controls over the adoption of the 2017 Tax Act. The focus is on applying the provisions under the 2017 Tax Act including assessment of critical judgments and estimates and the proper disclosure in this Annual Report and future filings. Management determined that these changes in the Company's internal control were effective as of December 31, 2017.

Management's Report on Internal Control Over Financial Reporting

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rule 13a-15(f) under the Securities Exchange Act of 1934. 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 for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management evaluated the Company's internal control over financial reporting as of December 31, 2017. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework (2013 framework). As a result of this

assessment and based on the criteria in the COSO framework, management has concluded that, as of December 31, 2017, the Company's internal control over financial reporting was effective.

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Item 9B. Other Information.

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

Directors of the Registrant

The information set forth under the caption "Election of Directors" of the 2018 Proxy Statement is incorporated herein by reference.

Executive Officers of the Registrant

The information set forth under the caption "Executive Officers of the Company" of the 2018 Proxy Statement is incorporated herein by reference.

Compliance with Section 16(a) of the Exchange Act

The information set forth under the caption "Section 16(a) Beneficial Ownership Reporting Compliance" of the 2018 Proxy Statement is incorporated herein by reference.

Code of Ethics

The information set forth under the caption "Code of Ethics" of the 2018 Proxy Statement is incorporated herein by reference.

Audit Committee

The information set forth under the caption "Board Committees and Functions" of the 2018 Proxy Statement is incorporated herein by reference.

Item 11. Executive Compensation.

The information set forth under the caption "Compensation of Directors and Executive Officers" of the 2018 Proxy Statement is incorporated herein by reference.

Compensation Committee Interlocks and Insider Participation

The information set forth under the caption "Compensation Committee Interlocks and Insider Participation" of the 2018 Proxy Statement is incorporated herein by reference.

Compensation Committee Report

The information set forth under the caption "Compensation Committee Report" of the 2018 Proxy Statement is incorporated herein by reference.

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Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

Securities Authorized for Issuance under Equity Compensation Plans

The following table provides information for the equity compensation plan of the Company as of December 31, 2017:

| Plan Category | Number of securities to be issued upon exercise of outstanding options, warrants and rights (a) | Weighted-average exercise price of outstanding options, warrants and rights (b) | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c) |
|--|--|--|--|
| Equity compensation plans approved by security holders* | - | - | 97,264 |
| Equity compensation plans not approved by security holders | - | - | 0 |

*Amounts are subject to adjustment to reflect stock dividends, stock splits, or other relevant changes in capitalization.

In addition, the Company has an employee stock purchase plan that allows employees to purchase stock at a 5% discount up to a maximum of 10% of their gross compensation. Under this plan, 70,826 authorized shares remain unissued as of December 31, 2017.

The information set forth under the caption "Security Ownership of Certain Beneficial Owners and Management" of the 2018 Proxy Statement is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

The information set forth under the captions "Director Independence" and "Related Party Transactions" of the 2018 Proxy Statement is incorporated herein by reference.

Item 14. Principal Accounting Fees and Services.

The information set forth under the caption, "Principal Accountant's Fees and Services" of the 2018 Proxy Statement is incorporated herein by reference.

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PART IV

Item 15. Exhibits and Financial Statement Schedules.

(a) Certain documents filed as part of the Form 10-K.

1. The financial statements set forth under Item 8 of this Form 10-K.

Report of Independent Registered Public Accounting Firm
Balance Sheets as of December 31, 2017 and 2016
Statements of Income for Years Ended December 31, 2017, 2016 and 2015
Statements of Common Stockholders' Equity for Years Ended December 31, 2017, 2016 and 2015
Statements of Cash Flows for Years Ended December 31, 2017, 2016 and 2015
Notes to Financial Statements

2. Financial Statement schedules.

| <u>Schedule</u> | <u>Schedule</u> | <u>Page</u> |
|-----------------|---|---------------|
| <u>Number</u> | <u>Description</u> | <u>Number</u> |
| II | <u>Valuation and Qualifying Accounts</u> | 70 |
| - | <u>for the years ended December 31, 2017, 2016 and 2015</u> | - |

The report of the Company's independent registered public accounting firm with respect to the financial statement schedule appears on page 32.

All other financial statements and schedules not listed have been omitted since the required information is included in the financial statements or the notes thereto, or is not applicable or required.

3. Exhibits required by Item 601 of Regulation S-K.

| <u>Exhibit</u> | <u>Exhibit</u> | <u>Page Number of</u> |
|----------------|---|--|
| <u>Number</u> | <u>Description</u> | <u>Incorporation</u> |
| | | <u>By Reference</u> |
| 3 | <u>Amended and Restated</u> <u>Articles of Incorporation</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 3.1 to Form 8-K dated May 4, 2010.</u> |
| 3.1 | <u>Amended and Restated</u> <u>By-Laws</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 3.1 to Form 8-K dated January 26, 2012.</u> |

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| <u>Exhibit Number</u> | <u>Exhibit Description</u> | <u>Page Number of Incorporation By Reference</u> |
|-----------------------|--|---|
| 4.1 | <u>Dividend Reinvestment and Direct Stock Purchase and Sale Plan</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission on Form S-3 dated October 3, 2016 (File No. 333-213942).</u> |
| 4.2 | <u>Indenture, dated as of October 1, 2010, by and between The York Water Company and Manufacturers and Traders Trust Company, as trustee, relative to the \$15,000,000 5.0% Monthly Senior Notes</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 4.1 to the Company's October 8, 2010 Form 8-K.</u> |
| 4.3 | <u>First Supplemental Indenture, dated as of October 1, 2010, by and between The York Water Company and Manufacturers and Traders Trust Company, as trustee (which includes the form of Note)</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 4.2 to the Company's October 8, 2010 Form 8-K.</u> |
| 10.1 | Articles of Agreement Between The York Water Company and Springettsbury Township relative to Extension of Water Mains dated April 17, 1985 | Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.1 to the Company's 1989 Form 10-K. |
| 10.2 | Note Agreement relative to the \$6,000,000 10.17% Senior Notes, Series A and \$5,000,000 9.60% Senior Notes, Series B dated January 2, 1989 | Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 4.5 to the Company's 1989 Form 10-K. |
| 10.3 | Note Agreement relative to the \$6,500,000 10.05% Senior Notes, Series C dated August 15, 1990 | Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 4.6 to the Company's 1990 Form 10-K. |
| 10.4 | Note Agreement relative to the \$7,500,000 8.43% Senior Notes, Series D dated December 15, 1992 | Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 4.7 to the Company's 1992 Form 10-K. |
| 10.5 | Promissory Note between The York Water Company and the Pennsylvania Infrastructure Investment Authority for \$800,000 at 1.00% dated August 24, 1999 | Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 4.2 to the Company's 2000 Form 10-K. |

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| <u>Exhibit Number</u> | <u>Exhibit Description</u> | <u>Page Number of Incorporation By Reference</u> |
|-----------------------|--|---|
| 10.6 | <u>Loan Agreement between The York Water Company and York County Industrial Development Authority, dated as of October 1, 2006 relative to the \$10,500,000 4.75% Exempt Facilities Revenue Bonds</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.3 to the Company's September 15, 2009 Form 8-K.</u> |
| 10.7 | <u>Trust Indenture dated October 1, 2006 between the York County Industrial Development Authority and Manufacturers and Traders Trust Company, as trustee</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.4 to the Company's September 15, 2009 Form 8-K.</u> |
| 10.8 | <u>Variable Rate Loan Agreement between The York Water Company and Pennsylvania Economic Development Financing Authority, dated as of May 1, 2008 relative to the \$12,000,000 Exempt Facilities Revenue Bonds</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.1 to the Company's May 12, 2008 Form 8-K.</u> |
| 10.9 | <u>Trust Indenture dated as of May 1, 2008 between Pennsylvania Economic Development Financing Authority and Manufacturers and Traders Trust Company, as trustee</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.5 to the Company's September 15, 2009 Form 8-K.</u> |
| 10.10 | <u>Reimbursement, Credit and Security Agreement, dated as of May 1, 2008 between The York Water Company and PNC Bank, National Association</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.3 to the Company's May 12, 2008 Form 8-K.</u> |
| 10.11 | <u>Loan Agreement between The York Water Company and Pennsylvania Economic Development Financing Authority, entered into April 25, 2014 and dated as of April 1, 2014 relative to the \$14,880,000 4.50% Exempt Facilities Revenue Refunding Bonds</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.1 to the Company's April 28, 2014 Form 8-K.</u> |
| 10.12 | <u>Trust Indenture entered into April 25, 2014 and dated as of April 1, 2014 between Pennsylvania Economic Development Financing Authority and Manufacturers and Traders Trust Company, as trustee</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.2 to the Company's April 28, 2014 Form 8-K.</u> |
| 10.13 | <u>Loan Agreement between The York Water Company and York County Industrial Development Authority, entered into July 23, 2015 and dated as of July 1, 2015 relative to the \$10,000,000 4.00% - 4.50% Exempt Facilities Revenue Bonds.</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.1 to the Company's July 24, 2015 Form 8-K.</u> |

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| <u>Exhibit Number</u> | <u>Exhibit Description</u> | <u>Page Number of Incorporation By Reference</u> |
|-----------------------|---|---|
| <u>10.14</u> | <u>Trust Indenture entered into July 23, 2015 and dated as of July 1, 2015 between York County Industrial Development Authority and Manufacturers and Traders Trust Company, as trustee</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.2 to the Company's July 24, 2015 Form 8-K. Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.1 to the Company's January 28, 2005 Form 8-K.</u> |
| <u>10.15</u> | <u>Cash Incentive Plan</u> | |
| <u>10.16</u> | <u>Form of Amended and Restated Change in Control Agreement made as of November 5, 2008 between The York Water Company and each of the individuals listed on a schedule attached thereto, which plans are identical in all material respects except as indicated in the attached schedule</u> | <u>Filed herewith.</u> |
| <u>10.17</u> | <u>Form of Amended and Restated Supplemental Retirement Plan made as of January 1, 2009 between The York Water Company and each of the individuals listed on a schedule attached thereto, which plans are identical in all material respects except as indicated in the attached schedule</u> | <u>Filed herewith.</u> |
| <u>10.18</u> | <u>Form of Amended and Restated Deferred Compensation Plan made as of July 1, 2015 between The York Water Company and each of the individuals listed on Schedule 10.18 thereto, which plans are identical in all material respects except as indicated in Schedule 10.18</u> | <u>Filed herewith.</u> |
| <u>10.19</u> | <u>Form of Amended and Restated Deferred Compensation Plan made as of January 1, 2009 between The York Water Company and each of the individuals listed on a schedule attached thereto, which plans are identical in all material respects except as indicated in Schedule 10.19</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.19 to the Company's March 8, 2011 Form 10-K.</u> |
| <u>10.20</u> | <u>Long-Term Incentive Plan</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission on Form S-8 dated May 11, 2016 (File No. 333-211287).</u> |

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| <u>Exhibit Number</u> | <u>Exhibit Description</u> | <u>Page Number of Incorporation By Reference</u> |
|-----------------------|---|--|
| <u>10.21</u> | <u>Employee Stock Purchase Plan</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 10.21 to the Company's March 7, 2017 Form 10-K.</u> |
| <u>14</u> | <u>Company Code of Conduct</u> | <u>Incorporated herein by reference. Filed previously with the Securities and Exchange Commission as Exhibit 14 to the Company's August 6, 2014 Form 10-Q.</u> |
| <u>23</u> | <u>Consent of Baker Tilly Virchow Krause, LLP, Independent Registered Public Accounting Firm</u> | <u>Filed herewith.</u> |
| <u>31.1</u> | <u>Certification pursuant to Rule 13a-15(f) and 15d-15(f)</u> | <u>Filed herewith.</u> |
| <u>31.2</u> | <u>Certification pursuant to Rule 13a-15(f) and 15d-15(f)</u> | <u>Filed herewith.</u> |
| <u>32.1</u> | <u>Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u> | <u>Filed herewith.</u> |
| <u>32.2</u> | <u>Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</u> | <u>Filed herewith.</u> |
| 101.INS | XBRL Instance Document | Filed herewith. |
| 101.SCH | XBRL Taxonomy Extension Schema | Filed herewith. |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase | Filed herewith. |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase | Filed herewith. |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase | Filed herewith. |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase | Filed herewith. |

Item 16. Form 10-K Summary.

None.

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THE YORK WATER COMPANY
 SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS
 FOR THE THREE YEARS ENDED DECEMBER 31, 2017

| <u>Description</u> | <u>Balance at</u> <u>Beginning</u> <u>of Year</u> | <u>Additions</u> <u>Charged</u> <u>to</u> <u>Cost and</u> <u>Expenses</u> | <u>Recoveries</u> | <u>Deductions</u> | <u>Balance</u> <u>at</u> <u>End of</u> <u>Year</u> |
|---|---|---|-------------------|-------------------|---|
| FOR THE YEAR ENDED DECEMBER 31, 2017 | | | | | |
| Reserve for uncollectible accounts | \$ 305,000 | \$ 290,897 | \$ 25,900 | \$ 316,797 | \$ 305,000 |
| FOR THE YEAR ENDED DECEMBER 31, 2016 | | | | | |
| Reserve for uncollectible accounts | \$ 315,000 | \$ 291,108 | \$ 38,976 | \$ 340,084 | \$ 305,000 |
| FOR THE YEAR ENDED DECEMBER 31, 2015 | | | | | |
| Reserve for uncollectible accounts | \$ 325,000 | \$ 292,248 | \$ 40,681 | \$ 342,929 | \$ 315,000 |

The Deductions column above represents write-offs of accounts receivable during the applicable year.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE YORK WATER COMPANY
(Registrant)

Dated: March 5, 2018 By: /s/Jeffrey R. Hines
Jeffrey R. Hines
President and CEO

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| | |
|---|---|
| By: <u>/s/Jeffrey R. Hines</u> Jeffrey R. Hines (Principal Executive Officer and Director) | By: <u>/s/Matthew E. Poff</u> Matthew E. Poff (Principal Accounting Officer and Chief Financial Officer) |
|---|---|

| | |
|-----------------------------|-----------------------------|
| Dated: <u>March 5, 2018</u> | Dated: <u>March 5, 2018</u> |
|-----------------------------|-----------------------------|

| | |
|------------|-------|
| Directors: | Date: |
|------------|-------|

| | |
|--|----------------------|
| By: <u>/s/James H. Cawley</u> James H. Cawley | <u>March 5, 2018</u> |
|--|----------------------|

| | |
|--|----------------------|
| By: <u>/s/Michael W. Gang</u> Michael W. Gang | <u>March 5, 2018</u> |
|--|----------------------|

| | |
|--|----------------------|
| By: <u>/s/Jeffrey R. Hines</u> Jeffrey R. Hines | <u>March 5, 2018</u> |
|--|----------------------|

| | |
|--|----------------------|
| By: <u>/s/George W. Hodges</u> George W. Hodges | <u>March 5, 2018</u> |
|--|----------------------|

| | |
|--|----------------------|
| By: <u>/s/George Hay Kain, III</u> George Hay Kain, III | <u>March 5, 2018</u> |
|--|----------------------|

| | |
|--|----------------------|
| By: <u>/s/Jody L. Keller</u> Jody L. Keller | <u>March 5, 2018</u> |
|--|----------------------|

| | |
|--|----------------------|
| By: <u>/s/Erin C. McGlaughlin</u> Erin C. McGlaughlin | <u>March 5, 2018</u> |
|--|----------------------|

| | |
|--|----------------------|
| By: <u>/s/Robert P. Newcomer</u> Robert P. Newcomer | <u>March 5, 2018</u> |
|--|----------------------|

By: /s/Steven R. Rasmussen March 5, 2018
Steven R. Rasmussen

By: /s/Ernest J. Waters March 5, 2018
Ernest J. Waters
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