

AQUA AMERICA INC  
Form 10-Q  
May 06, 2015  
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON DC 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 or 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the quarterly period ended March 31, 2015

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 1-6659

AQUA AMERICA, INC.

(Exact name of registrant as specified in its charter)

Pennsylvania  
(State or other jurisdiction of  
incorporation or organization)

23-1702594  
(I.R.S. Employer  
Identification No.)

762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania  
(Address of principal executive offices)

19010 -3489  
(Zip Code)

(610) 527-8000  
(Registrant's telephone number, including area code)

(Former Name, former address and former fiscal year, if changed since last report.)

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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 whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12(b)-2 of the Exchange Act.:

Large accelerated filer Accelerated filer  
Non-accelerated filer (do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of

April 23, 2015: 177,069,727

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AQUA AMERICA, INC. AND SUBSIDIARIES

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## AQUA AMERICA, INC. AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

(In thousands of dollars, except per share amounts)

(UNAUDITED)

	March 31, 2015	December 31, 2014
Assets		
Property, plant and equipment, at cost	\$ 5,764,467	\$ 5,707,017
Less: accumulated depreciation	1,331,323	1,305,027
Net property, plant and equipment	4,433,144	4,401,990
Current assets:		
Cash and cash equivalents	9,274	4,138
Accounts receivable and unbilled revenues, net	95,405	96,999
Deferred income taxes	35,202	26,849
Inventory, materials and supplies	12,591	12,788
Prepayments and other current assets	11,753	11,748
Total current assets	164,225	152,522
Regulatory assets	748,911	725,591
Deferred charges and other assets, net	54,864	52,084
Investment in joint venture	42,619	43,334
Funds restricted for construction activity	15	47
Goodwill	33,954	31,184
Total assets	\$ 5,477,732	\$ 5,406,752
Liabilities and Equity		
Aqua America stockholders' equity:		
Common stock at \$.50 par value, authorized 300,000,000 shares, issued 179,041,925 and 178,591,254 as of March 31, 2015 and December 31, 2014	\$ 89,521	\$ 89,296
Capital in excess of par value	763,259	758,145
Retained earnings	869,203	849,952
Treasury stock, at cost, 1,978,968 and 1,837,984 shares as of March 31, 2015 and December 31, 2014	(46,592)	(42,838)
Accumulated other comprehensive income	863	788
Total Aqua America stockholders' equity	1,676,254	1,655,343
Noncontrolling interest	40	40
Total equity	1,676,294	1,655,383
Long-term debt, excluding current portion	1,594,980	1,560,655

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Commitments and contingencies (See Note 13)	-	-
Current liabilities:		
Current portion of long-term debt	47,042	58,615
Loans payable	33,062	18,398
Accounts payable	34,717	63,035
Accrued interest	20,477	12,437
Accrued taxes	31,653	31,462
Other accrued liabilities	38,168	41,388
Total current liabilities	205,119	225,335
Deferred credits and other liabilities:		
Deferred income taxes and investment tax credits	1,041,418	1,000,791
Customers' advances for construction	75,833	78,301
Regulatory liabilities	273,873	278,317
Other	106,279	109,692
Total deferred credits and other liabilities	1,497,403	1,467,101
Contributions in aid of construction	503,936	498,278
Total liabilities and equity	\$ 5,477,732	\$ 5,406,752

See notes to consolidated financial statements beginning on page 8 of this report.

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## AQUA AMERICA, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF NET INCOME

(In thousands, except per share amounts)

(UNAUDITED)

	Three Months Ended March 31,	
	2015	2014
Operating revenues	\$ 190,326	\$ 182,672
Operating expenses:		
Operations and maintenance	73,189	71,686
Depreciation	30,500	30,981
Amortization	849	1,133
Taxes other than income taxes	14,621	12,102
Total operating expenses	119,159	115,902
Operating income	71,167	66,770
Other expense (income):		
Interest expense, net	18,665	19,310
Allowance for funds used during construction	(1,182)	(1,167)
(Gain) loss on sale of other assets	(169)	348
Equity loss in joint venture	714	686
Income from continuing operations before income taxes	53,139	47,593
Provision for income taxes	4,594	5,192
Income from continuing operations	48,545	42,401
Discontinued operations:		
Income from discontinued operations before income taxes	-	772
Provision for income taxes	-	314
Income from discontinued operations	-	458
Net income attributable to common shareholders	\$ 48,545	\$ 42,859
Income from continuing operations per share:		
Basic	\$ 0.27	\$ 0.24
Diluted	\$ 0.27	\$ 0.24

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Income from discontinued operations per share:		
Basic	\$ -	\$ 0.00
Diluted	\$ -	\$ 0.00
Net income per common share:		
Basic	\$ 0.27	\$ 0.24
Diluted	\$ 0.27	\$ 0.24
Average common shares outstanding during the period:		
Basic	176,888	176,839
Diluted	177,792	177,810
Cash dividends declared per common share	\$ 0.165	\$ 0.152

See notes to consolidated financial statements beginning on page 8 of this report.



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## AQUA AMERICA, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands of dollars)

(UNAUDITED)

	Three Months Ended March 31,	
	2015	2014
Net income attributable to common shareholders	\$ 48,545	\$ 42,859
Other comprehensive income, net of tax:		
Unrealized holding gain on investments, net of tax expense of \$41 and \$38 for the three months ended March 31, 2015 and 2014, respectively	75	72
Reclassification adjustment for loss reported in net income, net of tax benefit of \$134 for the three months ended March 31, 2014 (1)	-	249
Comprehensive income	\$ 48,620	\$ 43,180

(1) Amount of pre-tax loss of \$383 reclassified from accumulated other comprehensive income to loss on sale of other assets on the consolidated statements of net income for the three months ended March 31, 2014.

See notes to consolidated financial statements beginning on page 8 of this report.

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## AQUA AMERICA, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CAPITALIZATION

(In thousands of dollars, except per share amounts)

(UNAUDITED)

	March 31, 2015	December 31, 2014
Aqua America stockholders' equity:		
Common stock, \$.50 par value	\$ 89,521	\$ 89,296
Capital in excess of par value	763,259	758,145
Retained earnings	869,203	849,952
Treasury stock, at cost	(46,592)	(42,838)
Accumulated other comprehensive income	863	788
Total Aqua America stockholders' equity	1,676,254	1,655,343
Noncontrolling interest	40	40
Total equity	1,676,294	1,655,383
Long-term debt of subsidiaries (substantially secured by utility plant):		
Interest Rate Range	Maturity Date Range	
0.00% to 0.99%	2023 to 2033	5,587
1.00% to 1.99%	2016 to 2035	25,681
2.00% to 2.99%	2024 to 2031	15,641
3.00% to 3.99%	2016 to 2047	190,271
4.00% to 4.99%	2020 to 2054	484,084
5.00% to 5.99%	2015 to 2043	241,991
6.00% to 6.99%	2015 to 2036	64,949
7.00% to 7.99%	2022 to 2027	34,261
8.00% to 8.99%	2021 to 2025	18,809
9.00% to 9.99%	2018 to 2026	27,800
10.00% to 10.99%	2018	6,000
		1,115,074
Notes payable to bank under revolving credit agreement, variable rate, due 2017	113,000	72,000

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Unsecured notes payable:		
Bank note at 1.921% due 2017	50,000	50,000
Notes at 3.57% due 2027	50,000	50,000
Notes ranging from 4.62% to 4.87%, due 2016 through 2024	144,400	144,400
Notes ranging from 5.20% to 5.95%, due 2016 through 2037	169,548	187,548
Total long-term debt	1,642,022	1,619,270
Current portion of long-term debt	47,042	58,615
Long-term debt, excluding current portion	1,594,980	1,560,655
Total capitalization	\$ 3,271,274	\$ 3,216,038

See notes to consolidated financial statements beginning on page 8 of this report.

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## AQUA AMERICA, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENT OF EQUITY

(In thousands of dollars)

(UNAUDITED)

	Common Stock	Capital in Excess of Par Value	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income	Noncontrolling Interest	Total
Balance at December 31, 2014	\$ 89,296	\$ 758,145	\$ 849,952	\$ (42,838)	\$ 788	\$ 40	\$ 1,655,383
Net income	-	-	48,545	-	-	-	48,545
Other comprehensive income, net of income tax of \$41	-	-	-	-	75	-	75
Dividends	-	-	(29,176)	-	-	-	(29,176)
Repurchase of stock (140,984 shares)	-	-	-	(3,754)	-	-	(3,754)
Equity compensation plan (280,401 shares)	140	(140)	-	-	-	-	-
Exercise of stock options (170,270 shares)	85	2,767	-	-	-	-	2,852
Stock-based compensation	-	1,341	(118)	-	-	-	1,223
Employee stock plan tax benefits	-	1,409	-	-	-	-	1,409
Other	-	(263)	-	-	-	-	(263)
Balance at March 31, 2015	\$ 89,521	\$ 763,259	\$ 869,203	\$ (46,592)	\$ 863	\$ 40	\$ 1,676,294

See notes to consolidated financial statements beginning on page 8 of this report.



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## AQUA AMERICA, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOW

(In thousands of dollars)

(UNAUDITED)

	Three Months Ended March 31,	
	2015	2014
Cash flows from operating activities:		
Net income	\$ 48,545	\$ 42,859
Income from discontinued operations	-	458
Income from continuing operations	48,545	42,401
Adjustments to reconcile income from continuing operations to net cash flows from operating activities:		
Depreciation and amortization	31,349	32,114
Deferred income taxes	2,688	3,692
Provision for doubtful accounts	936	1,508
Stock-based compensation	1,341	1,331
(Gain) loss on sale of other assets	(169)	348
Net change in receivables, inventory and prepayments	191	3,644
Net change in payables, accrued interest, accrued taxes and other accrued liabilities	11,460	13,269
Other	(6,321)	(7,833)
Operating cash flows from continuing operations	90,020	90,474
Operating cash flows used in discontinued operations, net	-	(545)
Net cash flows from operating activities	90,020	89,929
Cash flows from investing activities:		
Property, plant and equipment additions, including the debt component of allowance for funds used during construction of \$296 and \$367	(70,284)	(59,819)
Acquisitions of utility systems and other, net	(788)	(4,045)
Release of funds previously restricted for construction activity	32	-
Net proceeds from the sale of utility system and other assets	232	133
Other	(1,180)	(91)
Investing cash flows used in continuing operations	(71,988)	(63,822)
Investing cash flows from discontinued operations, net	-	39
Net cash flows used in investing activities	(71,988)	(63,783)
Cash flows from financing activities:		
Customers' advances and contributions in aid of construction	1,193	1,142
Repayments of customers' advances	(1,040)	(234)
Net proceeds (repayments) of short-term debt	14,664	(8,827)
Proceeds from long-term debt	52,629	73,192

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Repayments of long-term debt	(29,800)	(31,874)
Change in cash overdraft position	(21,431)	(21,753)
Proceeds from exercised stock options	2,852	2,757
Stock-based compensation windfall tax benefits	1,230	964
Repurchase of common stock	(3,754)	(1,973)
Dividends paid on common stock	(29,176)	(26,873)
Other	(263)	(181)
Financing cash flows used in continuing operations	(12,896)	(13,660)
Financing cash flows used in discontinued operations, net	-	(36)
Net cash flows used in financing activities	(12,896)	(13,696)
Net change in cash and cash equivalents	5,136	12,450
Cash and cash equivalents at beginning of period	4,138	5,058
Cash and cash equivalents at end of period	\$ 9,274	\$ 17,508
Non-cash investing activity:		
Property, plant and equipment additions purchased at the period end, but not yet paid for	\$ 20,158	\$ 18,550

See notes to consolidated financial statements beginning on page 8 of this report.

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## AQUA AMERICA, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(In thousands of dollars, except per share amounts)

(UNAUDITED)

## Note 1 – Basis of Presentation

The accompanying consolidated balance sheets and statements of capitalization of Aqua America, Inc. and subsidiaries (the “Company”) at March 31, 2015, the consolidated statements of net income and comprehensive income for the three months ended March 31, 2015 and 2014, the consolidated statements of cash flow for the three months ended March 31, 2015 and 2014, and the consolidated statement of equity for the three months ended March 31, 2015 are unaudited, but reflect all adjustments, consisting of only normal recurring accruals, which are, in the opinion of management, necessary to present fairly the consolidated financial position, the consolidated changes in equity, the consolidated results of operations, and the consolidated cash flow for the periods presented. Because they cover interim periods, the statements and related notes to the financial statements do not include all disclosures and notes normally provided in annual financial statements and, therefore, should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2014. The results of operations for interim periods may not be indicative of the results that may be expected for the entire year. The December 31, 2014 consolidated balance sheet data presented herein was derived from the Company’s December 31, 2014 audited consolidated financial statements, but does not include all disclosures and notes normally provided in annual financial statements.

## Note 2 – Goodwill

The following table summarizes the changes in the Company’s goodwill, by business segment:

	Regulated Segment	Other	Consolidated
Balance at December 31, 2014	\$ 24,564	\$ 6,620	\$ 31,184
Goodwill acquired	-	12	12
Reclassifications (to) from utility plant acquisition adjustment, net	2,758	-	2,758
Balance at March 31, 2015	\$ 27,322	\$ 6,632	\$ 33,954





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AQUA AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

(UNAUDITED)

The reclassification of goodwill to utility plant acquisition adjustment in the table above results from a mechanism approved by the applicable public utility commission. The mechanism provides for the transfer over time, and the recovery through customer rates, of goodwill associated with certain acquisitions upon achieving certain objectives.

Note 3 – Acquisitions

In December 2014, the Company acquired the water utility system assets of Lake Mohawk and Lake Tomahawk utilities located in Northeastern Ohio serving approximately 1,250 customers. The total purchase price consisted of \$1,770 in cash.

In December 2014, the Company acquired a non-regulated business that specializes in providing water distribution system services to prevent the contamination of potable water, including training to waterworks operators. The total purchase price consisted of \$1,800, of which \$700 was paid in the first quarter of 2015.

In September 2014, the Company acquired the water and wastewater utility system assets of Texas H2O, Inc. located in Mansfield, Texas serving approximately 1,100 customers. The total purchase price consisted of \$2,796 in cash.

In September 2014, the Company acquired the water utility system assets of Lake Caroline Water Co. located in Caroline County, Virginia serving approximately 1,040 customers. The total purchase price consisted of \$1,377 in cash.

In August 2014, the Company acquired a non-regulated business that specializes in the inspection, cleaning and repair of storm and sanitary sewer lines. The total purchase price consisted of \$3,010, of which a total of \$810 is contingent upon satisfying certain annual performance targets over a three-year period.

In May 2014, the Company entered into an asset purchase agreement for the acquisition of the water and wastewater utility system assets of North Maine Utilities owned by the Village of Glenview, Illinois serving approximately 7,200 customers, for cash at closing of \$22,000. On April 1, 2015, the Illinois Commerce Commission approved this transaction, and on April 30, 2015, we completed this acquisition. As of the date of issuance of the financial statements, the initial accounting of the purchase price allocation for this acquisition is incomplete.

In March 2014, the Company acquired the wastewater utility system assets of Penn Township located in Chester County, Pennsylvania serving approximately 800 customers. The total purchase price consisted of \$3,668 in cash.

#### Note 4 – Discontinued Operations

In December 2014, we completed the sale of our water utility system in southwest Allen County, Indiana to the City of Fort Wayne, Indiana. The completion of this sale settled the dispute concerning the City of Fort Wayne's valuation of the northern portion of our water and wastewater utility systems, which were

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AQUA AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

(UNAUDITED)

acquired by the City of Fort Wayne in February 2008, by eminent domain. In addition, as a result of this transaction, Aqua Indiana will expand its sewer customer base by accepting new wastewater flows from the City of Fort Wayne.

In March 2014, we completed the sale of our wastewater treatment facility in Georgia.

The operating results and cash flows of the Company's operations named above, during the periods owned, have been presented in the Company's consolidated statements of net income and consolidated statements of cash flow as discontinued operations. These operations were included in the Company's "Regulated" segment.

A summary of discontinued operations presented in the consolidated statements of net income include the following:

	Three Months Ended March 31, 2014
Operating revenues	\$ 1,579
Total operating expenses	673
Operating income	906
Other expense:	
Loss on sale	134
Income from discontinued operations before income taxes	772
Provision for income taxes	314
Income from discontinued operations	\$ 458

As of March 31, 2015 and December 31, 2014, there were no assets or liabilities associated with the Company's discontinued operations.

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AQUA AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

(UNAUDITED)

Note 5 – Capitalization

In February 2015, the Company renewed its universal shelf registration, which had expired in February 2015, through a filing with the Securities and Exchange Commission (“SEC”) to allow for the potential future sale by the Company, from time to time, in one or more public offerings, of an indeterminate amount of our common stock, preferred stock, debt securities and other securities specified therein at indeterminate prices.

In February 2015, the Company filed a registration statement with the SEC to update an existing filing which permits the offering, from time to time, of an aggregate of \$500,000 in shares of common stock and shares of preferred stock in connection with acquisitions. The form and terms of any securities issued under these shelf registration statements will be determined at the time of issuance.

Note 6 – Fair Value of Financial Instruments

The Company follows the Financial Accounting Standards Board’s (“FASB”) accounting guidance for fair value measurements and disclosures, which defines fair value and establishes a framework for using fair value to measure assets and liabilities. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1: unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access;
- Level 2: inputs other than Level 1 that are observable, either directly or indirectly, such as quoted market prices in active markets for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in non-active markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; or

- Level 3: inputs that are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs. There have been no changes in the valuation techniques used to measure fair value or asset or liability transfers between the levels of the fair value hierarchy for the quarter ended March 31, 2015.

Financial instruments are recorded at carrying value in the financial statements and approximate fair value as of the dates presented. The fair value of these instruments is disclosed below in accordance with current accounting guidance related to financial instruments.

The fair value of funds restricted for construction activity and loans payable are determined based on their carrying amount and utilizing Level 1 methods and assumptions. As of March 31, 2015 and December 31,

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## AQUA AMERICA, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

(UNAUDITED)

2014, the carrying amount of the Company's funds restricted for construction activity was \$15 and \$47, respectively, which equates to their estimated fair value. As of March 31, 2015 and December 31, 2014, the carrying amount of the Company's loans payable was \$33,062 and \$18,398, respectively, which equates to their estimated fair value. The fair value of cash and cash equivalents, which is comprised of a money market fund, is determined based on the net asset value per unit utilizing Level 2 methods and assumptions. As of March 31, 2015 and December 31, 2014, the carrying amounts of the Company's cash and cash equivalents was \$9,274 and \$4,138, respectively, which equates to their fair value.

The carrying amounts and estimated fair values of the Company's long-term debt is as follows:

	March 31, 2015	December 31, 2014
Carrying Amount	\$ 1,642,022	\$ 1,619,270
Estimated Fair Value	1,682,623	1,694,424

The fair value of long-term debt has been determined by discounting the future cash flows using current market interest rates for similar financial instruments of the same duration utilizing Level 2 methods and assumptions. The Company's customers' advances for construction have a carrying value of \$75,833 as of March 31, 2015, and \$78,301 as of December 31, 2014. Their relative fair values cannot be accurately estimated because future refund payments depend on several variables, including new customer connections, customer consumption levels, and future rate increases. Portions of these non-interest bearing instruments are payable annually through 2025 and amounts not paid by the respective contract expiration dates become non-refundable. The fair value of these amounts would, however, be less than their carrying value due to the non-interest bearing feature.



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## AQUA AMERICA, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

(UNAUDITED)

## Note 7 – Net Income per Common Share

Basic net income per common share is based on the weighted average number of common shares outstanding. Diluted net income per common share is based on the weighted average number of common shares outstanding and potentially dilutive shares. The dilutive effect of employee stock-based compensation is included in the computation of diluted net income per common 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 treasury stock method assumes that the proceeds from the exercise of stock options are used to purchase the Company's common stock at the average market price during the period. The following table summarizes the shares, in thousands, used in computing basic and diluted net income per common share:

	Three Months Ended March 31,	
	2015	2014
Average common shares outstanding during the period for basic computation	176,888	176,839
Dilutive effect of employee stock-based compensation	904	971
Average common shares outstanding during the period for diluted computation	177,792	177,810

For the three months ended March 31, 2015 and 2014, all of the Company's employee stock options were included in the calculations of diluted net income per share as the calculated cost to exercise the stock options was less than the average market price of the Company's common stock during these periods.

Note 8 – Stock-based Compensation

Under the Company's 2009 Omnibus Equity Compensation Plan, as amended as of February 27, 2014, (the "2009 Plan"), as approved by the Company's shareholders to replace the 2004 Equity Compensation Plan (the "2004 Plan"), stock options, stock units, stock awards, stock appreciation rights, dividend equivalents, and other stock-based awards may be granted to employees, non-employee directors, and consultants and advisors. The 2009 Plan authorizes 6,250,000 shares for issuance under the plan. A maximum of 3,125,000 shares under the 2009 Plan may be issued pursuant to stock awards, stock units and other stock-based awards, subject to adjustment as provided in the 2009 Plan. During any calendar year, no individual may be granted (i) stock options and stock appreciation rights under the 2009 Plan for more than 500,000 shares of Company stock in the aggregate or (ii) stock awards, stock units or other stock-based awards under the 2009 Plan for more than 500,000 shares of Company stock in the aggregate, subject to adjustment as provided in the 2009 Plan. Awards under the 2009 Plan are made by a committee of the Board of Directors of the Company, or in the case of awards to non-employee directors, by the Board of Directors of the Company. At March 31, 2015, 4,252,788 shares underlying stock-based compensation awards were still available for grants under the 2009 Plan. No further grants may be made under the 2004 Plan.

Performance Share Units – A performance share unit ("PSU") represents the right to receive a share of the Company's common stock if specified performance goals are met over the three year performance period

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## AQUA AMERICA, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

(UNAUDITED)

specified in the grant, subject to exceptions through the respective vesting period, generally three years. Each grantee is granted a target award of PSUs, and may earn between 0% and 200% of the target amount depending on the Company's performance against the performance goals. The following table provides compensation costs for stock-based compensation related to PSUs:

	Three Months Ended March 31,	
	2015	2014
Stock-based compensation within operations and maintenance expenses	\$ 1,078	\$ 1,002
Income tax benefit	439	410

The following table summarizes nonvested PSU transactions for the three months ended March 31, 2015:

	Number of Share Units	Weighted Average Fair Value
Nonvested share units at beginning of period	582,644	\$ 22.98
Granted	123,820	26.54
Performance criteria adjustment	5,114	25.59
Forfeited	(3,713)	25.69
Share units vested	(34,500)	26.88
Share units issued	(217,014)	18.49
Nonvested share units at end of period	456,351	\$ 25.79

A portion of the fair value of PSUs was estimated at the grant date based on the probability of satisfying the market-based conditions associated with the PSUs using the Monte Carlo valuation method, which assesses probabilities of various outcomes of market conditions. The other portion of the fair value of the PSUs is based on the fair market value of the Company's stock at the grant date, regardless of whether the market-based condition is satisfied. The per unit weighted-average fair value at the date of grant for PSUs granted during the three months ended March 31, 2015 and 2014 was \$26.54 and \$25.31, respectively. The fair value of each PSU grant is amortized monthly into compensation expense on a straight-line basis over their respective vesting periods, generally 36 months. The accrual of compensation costs is based on our estimate of the final expected value of the award, and is adjusted as required for the portion based on the performance-based condition. The Company assumes that forfeitures will be minimal, and recognizes forfeitures as they occur, which results in a reduction in compensation expense. As the payout of the PSUs includes dividend equivalents, no separate dividend yield assumption is required in calculating the fair value of the PSUs. The recording of compensation expense for PSUs has no impact on net cash flows.

Restricted Stock Units – A restricted stock unit (“RSU”) represents the right to receive a share of the Company's common stock. RSUs are eligible to be earned at the end of a specified restricted period, generally three years, beginning on the date of grant. In some cases the right to receive the shares is subject to certain performance goals established at the time the grant is made. The Company assumes that forfeitures

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## AQUA AMERICA, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

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will be minimal, and recognizes forfeitures as they occur, which results in a reduction in compensation expense. As the payout of the RSUs includes dividend equivalents, no separate dividend yield assumption is required in calculating the fair value of the RSUs. The following table provides compensation costs for stock-based compensation related to RSUs:

	Three Months Ended March 31,	
	2015	2014
Stock-based compensation within operations and maintenance expenses	\$ 263	\$ 236
Income tax benefit	109	98

The following table summarizes nonvested RSU transactions for the three months ended March 31, 2015:

	Number of Stock Units	Weighted Average Fair Value
Nonvested stock units at beginning of period	122,565	\$ 22.29
Granted	37,650	26.26
Stock units vested but not paid	11,500	17.99
Stock units vested and paid	(63,387)	19.44
Forfeited	-	-
Nonvested stock units at end of period	108,328	\$ 24.88

The per unit weighted-average fair value at the date of grant for RSUs granted during the three months ended March 31, 2015 and 2014 was \$26.26 and \$24.80, respectively.



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## AQUA AMERICA, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

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Stock Options – The following table provides the income tax benefit for stock-based compensation related to stock options granted in prior periods:

	Three Months Ended March 31,	
	2015	2014
Income tax benefit	\$ 104	\$ 73

For the three months ended March 31, 2015 and 2014, there were no compensation costs for stock-based compensation related to stock options, as stock options were fully amortized in 2013. Additionally, there were no stock options granted during the three months ended March 31, 2015 or 2014.

The following table summarizes stock option transactions for the three months ended March 31, 2015:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Life (years)	Aggregate Intrinsic Value
Outstanding at beginning of period	1,084,992	\$ 17.06		
Forfeited	-	-		
Expired	-	-		
Exercised	(170,270)	16.75		
Outstanding and exercisable at end of period	914,722	\$ 17.12	3.1	\$ 8,443

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AQUA AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

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Restricted Stock – The following table provides compensation costs for stock-based compensation related to restricted stock:

	Three Months Ended March 31, 2015 2014	
Stock-based compensation within operations and maintenance expenses	\$ -	\$ 92
Income tax benefit	-	38

For the three months ended March 31, 2015, there were no compensation costs for stock-based compensation related to restricted stock, as restricted stock was fully amortized in 2014. Additionally, there was no restricted stock granted during the three months ended March 31, 2015 or 2014.

The following table summarizes nonvested restricted stock transactions for the three months ended March 31, 2015:

	Number of Shares	Weighted Average Fair Value
Nonvested shares at beginning of period	31,250	\$ 17.70
Granted	-	-
Vested	(31,250)	17.70
Forfeited	-	-
Nonvested shares at end of period	-	\$ -





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## AQUA AMERICA, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

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## Note 9 – Pension Plans and Other Postretirement Benefits

The Company maintains a qualified defined benefit pension plan (the “Pension Plan”), a nonqualified pension plan and other postretirement benefit plans for certain of its employees. The net periodic benefit cost is based on estimated values and an extensive use of assumptions about the discount rate, expected return on plan assets, the rate of future compensation increases received by the Company’s employees, mortality, turnover, and medical costs. The following tables provide the components of net periodic benefit cost:

	Pension Benefits Three Months Ended March 31,	
	2015	2014
Service cost	\$ 925	\$ 1,143
Interest cost	3,222	3,512
Expected return on plan assets	(4,674)	(4,305)
Amortization of prior service cost	43	69
Amortization of actuarial loss	1,532	500
Net periodic benefit cost	\$ 1,048	\$ 919
	Other Postretirement Benefits Three Months Ended March 31,	
	2015	2014
Service cost	\$ 406	\$ 312
Interest cost	758	737
Expected return on plan assets	(730)	(683)
Amortization of prior service cost	(54)	(74)
Amortization of actuarial loss	354	82

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Net periodic benefit cost	\$ 734	\$ 374
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The Company made cash contributions of \$6,878 to its Pension Plan during the first three months of 2015, and intends to make cash contributions of \$6,878 to the Pension Plan during the remainder of 2015.

Note 10 – Water and Wastewater Rates

During the first three months of 2015, the Company's operating divisions in Illinois, Ohio, and Texas were granted base rate increases designed to increase total operating revenues on an annual basis by \$3,347. Further, during the first three months of 2015, the Company's operating divisions in Illinois and North Carolina received approval to bill infrastructure rehabilitation surcharges designed to increase total operating revenues on an annual basis by \$345.

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AQUA AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

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Note 11 – Taxes Other than Income Taxes

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

	Three Months Ended March 31,	
	2015	2014
Property	\$ 6,825	\$ 4,824
Capital stock	540	501
Gross receipts, excise and franchise	2,442	2,779
Payroll	3,278	2,654
Regulatory assessments	653	594
Other	883	750
Total taxes other than income	\$ 14,621	\$ 12,102

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## AQUA AMERICA, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

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## Note 12 – Segment Information

The Company has identified ten operating segments and has one reportable segment named the “Regulated” segment. The reportable segment is comprised of eight operating segments for the Company’s water and wastewater regulated utility companies which are organized by the states where we provide these services. In addition, two segments are not quantitatively significant to be reportable and are comprised of the Company’s non-regulated subsidiaries: Aqua Resources, Inc. and Aqua Infrastructure, LLC. Aqua Resources, Inc. provides liquid waste hauling and disposal; water and wastewater service through operating and maintenance contracts with municipal authorities and other parties in close proximity to our utility companies’ service territories; offers, through a third party, water and wastewater line repair service and protection solutions to households; inspects, cleans and repairs storm and sanitary wastewater lines; installs and tests devices that prevent the contamination of potable water; designs and builds water and wastewater systems; and provides other non-regulated water and wastewater services. Aqua Infrastructure, LLC provides non-utility raw water supply services for firms in the natural gas drilling industry. These two segments are included as a component of “Other” in the tables below. Also included in “Other” are corporate costs that have not been allocated to the Regulated segment and intersegment eliminations. Corporate costs include general and administrative expense, and interest expense.

The following table presents information about the Company’s reportable segment:

	Three Months Ended March 31, 2015			Three Months Ended March 31, 2014		
	Regulated	Other	Consolidated	Regulated	Other	Consolidated
Operating revenues	\$ 180,564	\$ 9,762	\$ 190,326	\$ 178,199	\$ 4,473	\$ 182,672
Operations and maintenance expense	67,018	6,171	73,189	68,456	3,230	71,686
Depreciation	30,438	62	30,500	30,881	100	30,981
Operating income	68,624	2,543	71,167	66,419	351	66,770
Interest expense, net of allowance for funds used during construction	16,720	763	17,483			