AMERICAN WATER WORKS AND ELECTRIC COMPANY

INCORPORATED

ANNUAL REPORT
1942

FOR THE FISCAL YEAR ENDED DECEMBER 31, 1942

AMERICAN WATER WORKS AND ELECTRIC COMPANY

INCORPORATED

Annual Report

1942

FOR THE FISCAL YEAR ENDED DECEMBER 31, 1942

BOARD OF DIRECTORS

George A. Benington
George W. Biggs, Jr.
Thomas H. Blodgett
Harold F. Butler
Randolph Catlin
James A. Hill
Thomas H. McInnerney
H. Hobart Porter
Philip L. Ross
George M. Schurman
Earle S. Thompson

EXECUTIVE COMMITTEE

George A. Benington
Thomas H. Blodgett
James A. Hill
H. Hobart Porter
Earle S. Thompson

OFFICERS

H. Hobart Porter, *Chairman of the Board*
Earle S. Thompson, *President*

Philip L. Ross, *Vice-President*
Harold F. Butler, *Vice-President*
Gilbert W. Chapman, *Treasurer*
Hugh D. McDowell, *Secretary*
Raymond P. Kaesshaefer, *Comptroller*
Lorenzo Semple, Jr., *Assistant Vice-President*
Howard H. Briggs, *Assistant Secretary*
John Young, *Assistant Comptroller*
Lewis E. Sharpe, *Assistant Comptroller*
John P. Eaton, *Assistant Comptroller*

George W. Biggs, Jr., *Chief Engineer, Water Properties*

GENERAL COUNSEL

Sullivan & Cromwell, 48 Wall Street, New York City

TRANSFER AND DIVIDEND AGENTS

Agents of the Corporation, 50 Broad Street, New York City

REGISTRAR OF TRANSFERS

Guaranty Trust Company of New York, 140 Broadway, New York City

GENERAL OFFICES

50 Broad Street, New York City

American Water Works and Electric Company

INCORPORATED

March 19, 1943.

To the Stockholders:

The business of the system was conducted during the past year under changed conditions resulting from the war and under severe restrictions adopted by the Government in furtherance of the nation's determination to bring the war promptly to a successful conclusion.

It was a difficult year in many respects, and it presented many new problems. Considering the difficulties, however, we consider the year 1942 a constructive one for the Company and its subsidiaries.

In accordance with our established policy, we cooperated in every way that we could in the prosecution of the war. We regard that as the paramount duty of all business and of all citizens in the present crisis. We are confident that our security-holders concur without reservation in such policy.

We met all demands made upon us for the various forms of utility service furnished by our system; we prepared to meet further demands; we kept together an effective organization despite the loss of a large number of employees to the armed services of the nation; we maintained our properties in good working order and condition; and we made substantial reductions in our bank debts.

The normal growth of the electric and water properties has been seriously interrupted, since extensions and additions are now limited to those qualifying under restrictions applicable to the use of materials deemed essential for war purposes. This trend will doubtless continue during the war, and the restrictions upon the use of critical materials may become more severe.

A larger percentage than usual of the gross revenues in the electric and water works divisions, and particularly in the electric division, is now represented by sales to industrial customers.

The number of water and electric customers increased in 1942. However, the greater part of the increase occurred in the first part of the year, and the rate of growth for the year was substantially less than it has been in recent years.

Downward trends in the use of electricity became apparent in the latter part of the year in the commercial and residential classifications of service. This is probably the result of many factors, including restrictions on line extensions, reductions in sales of electric appliances and fixtures which contribute to load growth, curtailment of businesses dependent upon the use of automobiles, use of War Time instead of Standard Time, blackout tests, dim-outs, and a developing tendency among customers in these two groups to economize in the use of electricity under present conditions.

If these trends continue, it is possible that the year 1943 will show a decline in the number of electric customers in the residential group and in the present average rate of annual use of electricity by such customers.

Rationing of electricity has not been necessary. We believe that our integrated electric system will continue to be able to meet the demands made upon it by all classes of customers in the territory served. However, it appears from the press that plans for the rationing of electricity are being discussed by governmental authorities for various reasons, including fuel conservation. The scope and severity of any rationing program which may be finally adopted cannot presently be predicted. Substantial curtailment in the use of electricity by commercial and residential customers under a rationing program would adversely affect the revenues and earnings of the electric companies in the system.

There was a marked increase during the year in the revenues derived from bus and electric railway transportation services furnished by system companies, as a result of tire and gasoline rationing and restrictions upon the use of private automobiles.

The volume of business of the system as a whole was exceptionally good in 1942. Gross operating revenues of the system were larger than at any previous time in its history.

In normal times, such an increase in gross revenues would have resulted in a substantial improvement in net earnings. This was not the case in 1942, however, and the reason is obvious. Unavoidable increases in items of expense, such as wages, costs of fuel, materials and supplies, and taxes, particularly Federal taxes on income, absorbed the profit that ordinarily would have been expected to result from the increased volume of business. Considering the size of the additional burdens that had to be assumed, we feel that a creditable showing has been made toward offsetting the additional expenses and taxes without receiving any material relief in the way of rate increases.

As the owner of public utility properties, our system finds itself in an anomalous position. The properties are being operated generally upon the basis of rates and charges for services which were fixed under conditions prevailing in the pre-war period and which, for the most part, represent the lowest rates and charges reached after years of successive rate reductions.

These rates and charges cannot be increased without the approval of governmental regulatory bodies. Rate increases are presently opposed by public authorities upon the theory that such increases would be inflationary in character, that they would add to the cost of the war, that utilities should bear their share of the burdens of the war, that utilities should not be permitted to pass on to their customers the abnormal taxes that have been imposed to finance the war and that, under the present high tax rates, little relief would be obtained from rate increases because, as a practical matter, a substantial part of the benefit derived therefrom would have to be paid over to the Government in the form of taxes on the additional income.

Whatever the merits of such theories may be, it is a fact that the Company's utility system, unlike many other industries, is being required to bear, with no increase in the price it may charge for its own product, the greatly enhanced wage levels and the higher costs of fuel, materials and supplies which have resulted from increases made before the existing Federal stabilization measures were adopted. In some cases, these costs continue to rise with the sanction of the stabilization authorities.

It seems reasonable that some consideration and relief should be provided in these circumstances—relief either in the form of increased rates or reductions in the present tax burden, Federal, state and local, which, in the aggregate, took in 1942 an amount equal to approximately 25¢ out of each dollar of operating revenue taken in by the system during the year.

Relief also should be granted during the war from existing oppressive regulatory measures, particularly those dealing with such matters as the retroactive reclassification of accounts to conform to recently prescribed accounting procedures and similar matters. Many of these regulatory measures were promulgated as reforms and designed to be applied during peacetime conditions and not in a period of war and worldwide financial and economic upheaval. The postponement of such matters until after the war would not be serious from any standpoint and it seems to us that their deferment is the fair thing to do under present conditions. Such a course would afford relief to companies already burdened with expense. Further, and much more important in these days when the conservation of manpower for war needs is imperative, it would release executive, accounting, engineering and other personnel from activities not essential to the war and enable them to devote more of their time to matters which will contribute directly to the all-important purpose of winning the war at the earliest possible moment.

There are indications that the advocates of public ownership have not relaxed their efforts even in war time and that serious efforts continue to be made to have the "fair value" rule, which has been the law of the land for almost fifty years in connection with the determination of fair and reasonable rates, superseded by what the advocates of change choose to call the "original cost" or the "prudent investment" rate base theory. Utility companies are now being required to make studies of ancient records and documents with a view to restating their accounts so as to reflect the "original cost" of their properties. The term "original cost" is a defined term. It does not mean the cost of the property to the present owner and it does not necessarily have any relation whatever to present value. "Original cost" generally is defined to mean the cost of the property to the person first devoting it to public service. Aside from the time and expense involved in making the necessary studies, we do not object to the determination of the actual cost of the properties and the segregation and identification of such cost so that it will be available for such use, if any, as may properly be made of it. The use of "original cost," however, as the sole test of value for rate-making purposes, or capitalization or other phases of utility regulation is grossly unfair and inequitable. The adoption of such a standard would ignore present values and the costs actually incurred by present owners and would represent a violent departure from the long established "fair value" rule laid down by the Supreme Court which has been relied upon for years by regulatory bodies in fixing rates and authorizing the issue of securities and by owners of utility properties and their security-holders in making their investments. Its adoption would be retroactive action of exceedingly serious import. The change cannot be made without substantial losses to present owners and investors. It should not be made in any case merely by administrative rulings or by court decision. Such a momentous change in the long prevailing law of the land, if made at all, should be effected only through express legislative action within constitutional limitations and with full protection of existing rights.

These matters affect all security-holders in varying degree. They should be of deep concern to you, and especially to the common stockholders, because they affect the value and dividend prospects of equity securities.

There follow a few specific comments with respect to the financial statements submitted herewith and to certain other matters concerning the operations of the system during the year 1942.

EARNINGS

The net income of the Company alone in 1942, after preferred dividends, was $301,750, equivalent to 13 cents per share on the Common Stock of the Company, as against 47 cents per share reported for the year 1941.

The consolidated net income of the Company for the year 1942, before the special reduction in taxes mentioned below, and after preferred dividends, was $1,683,997, equivalent to 72 cents per share on the Common Stock of the Company.

The present Federal Revenue Act in substance permits the amortization for tax purposes, over a five-year period, of expenditures made for facilities certified by the Secretary of War or the Secretary of the Navy as being deemed necessary for war purposes. Under "Necessity Certificates" obtained by subsidiary companies, amortization in respect of certain facilities is to be claimed as a deduction for tax purposes for the year 1942. The reduction in taxes expected to result therefrom has been computed at approximately $808,200 and the accruals made for Federal taxes on income in the consolidated accounts for 1942 reflect such special reduction in taxes.

The consolidated net income of the Company in 1942, after the special reduction in taxes mentioned above, and after preferred dividends, was $2,492,197.

As reported last year, the consolidated net income of the Company in 1941, after preferred dividends, was equivalent to $1.11 per share on the Common Stock of the Company.

ELECTRIC PROPERTIES

The total consolidated electric revenues in 1942 reached the highest point in the system's history and amounted to $47,023,000, an increase of $3,366,000 over the year 1941. Of this increase, $2,771,000 was from industrial customers, $626,000 was from residential customers, and $254,000 was from miscellaneous groups. The revenue from commercial customers declined by $285,000 during the year.

As a result of the great industrial activity in the territories served, the total power output in 1942 amounted to 3,782,000,000 kilowatt-hours, an increase of 13% over the previous year's record output.

At the end of 1942, there were 451,194 electric customers of all classes, representing an increase of only 4,773 during that year as against an increase of about 22,000 in the previous year.

The average annual use of electricity by residential customers was 1,002 kilowatt-hours per customer during 1942, which represents only a moderate increase over the preceding year.

WATER WORKS PROPERTIES

The consolidated operating revenues of the water works properties of the Company (exclusive of those in the Community Water Service Company system) amounted to $15,300,000 for the year 1942 which compares with $14,602,000 for the year 1941, an increase of $698,000; the total number of their customers on December 31, 1942, was 493,168, an increase of 8,165 during the year as against an increase of 18,807 customers in 1941. The increase in water customers in 1942 took place in the early part of the year; 2,039 customers were lost during the last quarter of the year.

The combined operating revenues of the water works subsidiaries in the Community Water Service Company system amounted to $6,304,000 for the year 1942, as against $6,256,000 for the year 1941, an increase of $48,000; the total number of their customers on December 31, 1942, was 195,302, an increase of 1,298 for the year as against an increase of 5,241 customers in 1941 over the preceding year. The increase in water customers in 1942 took place in the early part of the year; 2,472 customers were lost during the last quarter of the year. Such data regarding customers have been adjusted to give effect to the sale of two properties during 1942. In the interest of economy, the separate consolidated financial statements of Community Water Service Company and its subsidiaries are not reproduced in this report. A copy of that company's annual report to its stockholders will be furnished upon request.

TRANSPORTATION PROPERTIES

The operating revenues of the bus and electric railway properties of the system increased by $1,949,000 during 1942 principally as a result of tire and gasoline rationing and restrictions upon the use of private automobiles. The bus revenues amounted to $3,609,000, and the electric railway revenues amounted to $1,887,000 during the year.

TAXES

Accruals for taxes in the consolidated accounts for 1942 increased by $3,833,900 over the year 1941 and amounted in the aggregate to $17,065,400, classified as follows:

State, local and miscellaneous taxes	$ 6,653,900
Federal taxes on income	10,411,500
Total	$17,065,400

Such tax accruals for 1942 were equivalent to 24.8% of the gross operating revenues of the consolidated system for the year, and the increase in such accruals in 1942 was equivalent to 64.2% of the increase in gross operating revenues in 1942 over those of the preceding year.

The importance of the steadily increasing tax burden of the consolidated system in the past five years, and the relation of taxes in that period to the gross operating revenues of the consolidated system and to the common stock of the Company, are shown by the following tabulation:

	Amount of Taxes	Percentage of Operating Revenues	Taxes Per Share of Common Stock
1938	$ 6,600,000	13.2%	$2.82
1939	7,775,500	14.5%	3.32
1940	10,277,900	17.8%	4.39
1941	13,231,500	21.0%	5.65
1942	17,065,400	24.8%	7.28

REDUCTION IN BANK LOANS

The Company reduced its bank loan by $1,024,000 in 1942, through two regular semi-annual payments aggregating $320,000 and an extra payment of $704,000. This loan, which matures May 1, 1944, amounted to $6,176,000 at the end of the year. The loan has been further reduced by an extra payment of $617,600 made in the early part of 1943.

West Penn Power Company in 1942 paid in full its bank loan amounting to $1,600,000.

Monongahela West Penn Public Service Company reduced its bank loan by $400,000 in 1942, with the result that the amount owing thereon amounted to $500,000 at the end of the year. It has been further reduced by a payment of $300,000 made in the early part of 1943.

The Potomac Edison Company reduced its bank loan by $600,000 in 1942, and paid off the remaining balance of $150,000 early in 1943.

The bank loans of the Company and its consolidated subsidiaries were reduced in the net amount of $3,485,000 during 1942.

CASH AND GOVERNMENT SECURITIES

At the end of the year 1942, the Company had $4,222,000 of cash resources and $2,355,000 of short-term securities of the Federal Government, or cash resources and short-term Government securities in the aggregate amount of $6,577,000, as against cash resources of $6,660,000 at the end of the previous year.

The consolidated subsidiaries of the Company, at the end of the year 1942, had cash resources in the aggregate amount of $9,893,000 and Treasury Tax Savings Notes and other securities of the Government in the aggregate amount of $5,380,000.

PROPERTY, MAINTENANCE AND RESERVES

During the year, the consolidated subsidiaries of the Company expended approximately $4,410,000 for maintenance of their physical properties and reserved approximately $6,180,000 for depreciation, retirements and depletion making a total of about $10,590,000 so expended or reserved. In addition, a total of approximately $432,000 was set aside during the year by certain subsidiary companies for the amortization of certain property adjustment and other accounts.

Net additions made during the year to plant and property account amounted to approximately $3,850,000 in the case of electric company subsidiaries and to about $1,650,000 in the case of the consolidated water company subsidiaries.

DIVIDENDS

Four quarterly dividends of \$1.50 per share each were paid during the year on the \$6 Series, First Preferred Stock of the Company. No dividends were paid on the Common Stock.

CALIFORNIA PROPERTIES

James Mills Orchards Corporation and Esperanza Land Corporation, which are land, orchards and farming subsidiary companies acquired in 1914 in connection with the reorganization of a predecessor company, had a net profit from operations of \$112,811.09 for the year 1942, against a profit from operations of \$29,446.58 for the year 1941, before losses in connection with tree removal.

It has been the policy of these companies where certain types of orchards have proved unsatisfactory, to clear the land for general farming purposes. In this connection, the Orchards Corporation removed trees having a book value of \$28,545.08 in 1942 compared with \$35,804.77 in 1941.

Substantially all of the net profit from operations in 1942, after deducting losses of \$28,545.08 for tree removal, was accrued as interest payable to this Company. Such interest has not been included in the Company's income account but is to be applied in reduction of the carrying values of the Company's investments and advances in respect of such subsidiaries.

MANAGEMENT OF WATER WORKS PROPERTIES

The water works properties have been operated as a group for many years. The necessary services in connection therewith, including management, accounting, engineering, sanitary engineering, purchasing and other services, have been furnished in recent years on the basis of cost in part by this Company and in part by subsidiaries. Since the close of the year 1942, and as a result of discussions with the staff of the Securities and Exchange Commission, the Company has decided to set up a new subsidiary service company to render the required services. In general, it is planned that the new subsidiary service company will comply with the standards which the Securities and Exchange Commission has prescribed with respect to services rendered under its jurisdiction to gas and electric companies and that the new arrangements, when worked out, will be submitted for approval to the Securities and Exchange Commission and to such state regulatory bodies as may have jurisdiction.

The Securities and Exchange Commission instituted proceedings with respect to this matter under date of January 28, 1943. A scheduled hearing was held on February 18, 1943 and was adjourned until April 22, 1943 in order to enable the Company to work out the details of the proposed plan with the staff of the Commission.

PERSONNEL

As of December 31, 1942, the various companies in the system had a total of 9,093 regular employees, as against 10,556 at the end of 1941. This decrease of 1,463 regular employees throughout the year resulted principally from the loss of employees to the armed services, curtailment of construction and sales promotion work and some switching of employees to other industries.

Approximately 825 former employees of the system were reported in the armed services at the end of 1942. Further losses are expected as the Selective Service System calls up men from the group having dependents. Our companies have cooperated with the local Selective Service Boards in every reasonable way, releasing manpower wherever practicable. The local boards have had a difficult and thankless duty to perform. In our experience, they have performed their delicate tasks wisely and well.

Unquestionably this system, in common with other business enterprises, will be further handicapped by the lack of personnel, as the war progresses. This problem is being faced realistically. Steps are being initiated with a view to employing women in many job categories which heretofore have been regarded as requiring male employees. Additional duties and responsibilities are being assumed by existing employees and other measures will be taken as conditions warrant to assure a continuance of the vital utility services of our system, upon which our customers rely.

The responsibility of management in the administration of employee relations has been greater in recent years than ever before. Our system has had its share of personnel problems. Fortunately, however, they have been disposed of in a spirit of mutual understanding and confidence, and without their becoming so acute as to result either in the interruption of the various forms of utility service furnished to the public by our system or in strained relations between employees and management.

Throughout the year the personnel of the system has carried an ever increasing burden of work. They have carried on loyally and faithfully. This spirit and the fine morale that exists among the personnel throughout the system are due in no small measure to the older and more experienced employees with many years of service. These older men and women have stuck to their jobs. They have broken in new and less experienced employees and maintained the fine spirit of service which has always characterized the organization. The management knows that it can count on the entire employee group to carry on through these tragic days of war and the reconstruction period that will follow.

CHANGES IN OFFICERS AND DIRECTORS

Mr. George M. Schurman, President and Director of National Bag Corporation, was elected as a Director of the Company in the early part of 1943.

Mr. M. B. Rogers, an Assistant Treasurer of the Company, and also an officer and director of various subsidiary companies, resigned in 1942 to accept a commission in the armed forces of the nation, and is now serving abroad.

H. HOBART PORTER,
Chairman,

EARLE S. THOMPSON,
President.

Proxies for the annual meeting of stockholders, to be held April 20, 1943, will be requested later and the proxy statement will be mailed to stockholders on or about March 23, 1943. This annual report is not sent to you in connection with the solicitation of proxies for such annual meeting and is not part of the proxy statement or proxy soliciting material with respect to the meeting.

PRICE, WATERHOUSE & CO.

56 PINE STREET

NEW YORK, March 15, 1943.

TO THE BOARD OF DIRECTORS OF
AMERICAN WATER WORKS AND ELECTRIC COMPANY, INCORPORATED:

We have examined the balance sheet of American Water Works and Electric Company, Incorporated, the parent company, and of American Water Works and Electric Company, Incorporated, and consolidated subsidiary companies, as of December 31, 1942, and the related statements of income and surplus for the year then ended. Our examination was made in accordance with generally accepted auditing standards applicable in the circumstances, and included such tests of the accounting records and other supporting evidence and such other procedures as we considered necessary.

As stated in the notes to the consolidated financial statements, the companies operate under the regulatory authority of various State and Federal Commissions. The extent to which the accounts of the companies may be affected by regulatory action on the matters referred to in Notes A and F to the consolidated financial statements is not determinable at present.

In our opinion, subject to the reservation in the preceding paragraph, the accompanying balance sheets and related statements of income and surplus present fairly the position of American Water Works and Electric Company, Incorporated, and of that company and its consolidated subsidiary companies at December 31, 1942, and the results of their operations for the year, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

PRICE, WATERHOUSE & CO.

American Water Works and Electric Company, Incorporated

(A DELAWARE CORPORATION)

BALANCE SHEET AS OF DECEMBER 31, 1942

Assets and Deferred Charges

Investments and advances:		
Securities and notes of subsidiary companies, including those pledged under a Collateral Security Agreement with banks securing the promissory notes held by such banks		$55,874,651.22
Open account advances to subsidiary companies		6,419,291.33
Other security investments		2.00
Total investments and advances		$62,293,944.55
Current assets:		
Cash in banks and on hand	$4,222,058.26	
United States Government short-term securities—at cost	2,355,000.00	
Cash in banks for payment of matured interest payable (contra)	146,307.00	
Special cash deposit	2,267.50	
Accounts receivable from subsidiary companies	355,071.04	
Accrued interest and dividends receivable from subsidiary companies	105,107.00	
Other current assets	10,623.85	
Total current assets		7,196,434.65
Deferred charges:		
Unamortized debt discount and expense (see Note A)	$1,463,859.33	
Other deferred charges	29,534.58	
Total deferred charges		1,493,393.91
Total assets and deferred charges		$70,983,773.11

American Water Works and Electric Company, Incorporated

(A DELAWARE CORPORATION)

BALANCE SHEET AS OF DECEMBER 31, 1942

Liabilities, Capital and Surplus

Long-term debt (see Note B):		
Six Per Cent. Gold Debentures, Series A, due November 1, 1975		$ 8,000,000.00
Five Per Cent. Gold Debentures, Series B, due December 1, 1975		3,000,000.00
Promissory notes payable to banks, 3%, due May 1, 1944		5,856,000.00
Total long-term debt		$16,856,000.00
Current liabilities:		
Note installments payable to banks in 1943	$ 320,000.00	
Accounts payable	39,489.77	
Matured interest payable (contra)	146,307.00	
Taxes accrued	248,536.42	
Interest accrued	122,865.33	
Dividend declared on preferred stock payable January 2, 1943	300,000.00	
Other current liabilities	35,509.99	
Total current liabilities		1,212,708.51
Capital stock:		
First Preferred Stock (see Note B):		
Authorized 500,000 shares—no par value		
Outstanding 200,000 shares—$6 Series (cumulative)	$20,000,000.00	
Common Stock:		
Authorized 2,500,000 shares—no par value		
Outstanding 2,352,950 shares	23,529,500.00	
Total capital stock		43,529,500.00
Surplus:		
Capital surplus	$ 560,894.48	
Earned surplus of American Water Works and Electric Company, Incorporated (of Virginia), predecessor company	1,969,101.20	
Earned surplus of American Water Works and Electric Company, Incorporated (of Delaware)	6,855,568.92	
Total surplus		9,385,564.60
Total liabilities, capital and surplus		$70,983,773.11

See Notes on page 19.

American Water Works and Electric Company, Incorporated

COMPARATIVE INCOME ACCOUNT

	For Year Ended Dec. 31, 1942	For Year Ended Dec. 31, 1941	Increase or Decrease*
Earnings:			
Dividends from subsidiary companies.....	$2,657,051.30	$3,476,448.27	$819,396.97*
Other dividend income.................	1,955.40	3,910.80	1,955.40*
Interest on bonds of subsidiary companies..	16,700.00	21,848.61	5,148.61*
Interest on notes and accounts of subsidiary companies	285,054.44	311,116.70	26,062.26*
Management and service charges to subsidiary companies	723,202.62	871,174.37	147,971.75*
Other income	13,379.61	11,810.48	1,569.13
Total earnings	$3,697,343.37	$4,696,309.23	$998,965.86*
Expenses:			
Salaries, rents and other expenses.........	$1,192,975.60	$1,331,899.54	$138,923.94*
Federal income taxes..................	100,000.00	106,200.00	6,200.00*
General taxes	35,097.32	51,686.60	16,589.28*
	$1,328,072.92	$1,489,786.14	$161,713.22*
Less: Amount of salaries, rents, other expenses and general taxes chargeable to American Water Works Construction Company (a subsidiary)............	52,313.23	60,839.36	8,526.13*
Net expenses	$1,275,759.69	$1,428,946.78	$153,187.09*
Net earnings	$2,421,583.68	$3,267,362.45	$845,778.77*
Deductions:			
Interest on debentures..................	$ 630,000.00	$ 630,000.00	$ —
Interest on other long-term debt.........	201,525.33	221,626.67	20,101.34*
Amortization of debt discount and expense.	71,853.47	90,192.26	18,338.79*
Miscellaneous	16,454.03	17,122.81	668.78*
Total deductions	$ 919,832.83	$ 958,941.74	$ 39,108.91*
Net income	$1,501,750.85	$2,308,420.71	$806,669.86*

American Water Works and Electric Company, Incorporated

SURPLUS ACCOUNT

YEAR ENDED DECEMBER 31, 1942

Balance at January 1, 1942		$ 9,068,125.25
Add:		
Net income for year ended December 31, 1942	$1,501,750.85	
Amount received in respect of investment previously written off	15,688.50	1,517,439.35
		$10,585,564.60
Deduct:		
Dividends on $6 Series, First Preferred Stock		1,200,000.00
Balance at December 31, 1942		$ 9,385,564.60

NOTE: There were no changes in the capital surplus account of the Company during 1942.

NOTES TO FINANCIAL STATEMENTS OF AMERICAN WATER WORKS AND ELECTRIC COMPANY, INCORPORATED

Note A: Included in unamortized debt discount and expense are (a) unamortized debt discount and expense on a debenture issue of the Company, (b) the balance of unamortized debt discount and expense on a debenture issue of the predecessor company, American Water Works and Electric Company, Incorporated (of Virginia), (c) the unamortized portion of the difference between the amount paid by the Company to certain subsidiary companies for securities issued by them and the amount realized by the Company on the sale of such securities, and (d) the unamortized portion of similar items taken over from the books of the said predecessor company at the time of the transfer of its property and assets to the Company; the aggregate of items (c) and (d) approximates $516,000.

The method used in amortizing debt discount and expense is explained in Note C to the consolidated financial statements.

Note B: The Debentures and the $6 Series, First Preferred Stock are redeemable at the option of the Company. The preferred stock is redeemable on 30 days' notice at $110 per share and accrued dividends.

Note C: The Company is the guarantor of the payment of principal and interest on bonds of a subsidiary water company in the principal amount of $726,000.

Note D: The financial statements of American Water Works and Electric Company, Incorporated, should be read in conjunction with the consolidated financial statements of the Company and its subsidiary companies and the notes appended thereto (pages 20 to 27, inclusive) to which reference is made.

American Water Works and Electric Company, Incorporated

AND SUBSIDIARY COMPANIES

CONSOLIDATED BALANCE SHEET AS OF DECEMBER 31, 1942

Assets and Deferred Charges

Property, plant and equipment (see Note A)			$380,551,130.93
Emergency plant facilities under contract with United States Government—at cost (see Note B)		$ 775,796.29	
Reimbursements to date	$ 90,509.51		
Reimbursements receivable, discounted with bank	685,286.78	775,796.29	—
Investments and other assets:			
Investments in securities of Community Water Service Company, a non-consolidated subsidiary, including those pledged by a subsidiary to secure a bank loan		$ 1,767,869.91	
Investment in and advances to associated and other non-consolidated subsidiary companies, and miscellaneous investments, less reserves		3,648,456.59	
Post war tax refunds receivable		419,921.00	
Loans to superannuated employees secured by life insurance policies		218,994.00	6,055,241.50
Current and working assets:			
Cash in banks and on hand		$14,115,657.99	
United States Treasury tax notes and other Government securities—at cost		7,735,655.91	
Cash in banks for payment of matured interest payable (contra)		624,292.00	
Special deposits with trustees and others		1,022,040.76	
Accounts receivable from non-consolidated subsidiaries		147,537.57	
Customers accounts receivable (includes $658,813.95 for appliances—principally installment accounts)	$5,734,090.63		
Miscellaneous accounts receivable	360,407.37		
	$6,094,498.00		
Less reserves for doubtful accounts receivable	481,547.10	5,612,950.90	
Operating and construction materials and supplies and appliance merchandise—at cost or less		3,342,731.73	
Prepaid insurance, taxes, etc.		432,679.89	33,033,546.75
Deferred charges:			
Prepaid royalties on coal properties		$ 492,301.24	
Unamortized debt discount, premium (net) and expense (see Note C)		11,465,881.48	
Unamortized commission, redemption premium and expense on capital stock issues (see Note D)		1,107,548.20	
Other deferred charges		700,081.56	13,765,812.48
Total assets and deferred charges			$433,405,731.66

American Water Works and Electric Company, Incorporated

AND SUBSIDIARY COMPANIES

CONSOLIDATED BALANCE SHEET AS OF DECEMBER 31, 1942

Liabilities, Capital and Surplus

Long-term debt of subsidiaries (see Note E)			$178,416,500.00
Preferred capital stocks of subsidiaries (see Note E)			90,188,550.00
Long-term debt of American Water Works and Electric Company, Inc.:			
Six Per Cent. Gold Debentures, Series A, due November 1, 1975		$ 8,000,000.00	
Five Per Cent. Gold Debentures, Series B, due December 1, 1975		3,000,000.00	
Promissory notes payable to banks, 3%, due May 1, 1944		5,856,000.00	16,856,000.00
Current and accrued liabilities:			
Notes payable to banks		$ 1,686,000.00	
Accounts payable to non-consolidated subsidiaries		290,166.37	
Accounts payable to others, including payrolls of $308,013.65		1,522,840.98	
Taxes accrued		14,427,406.26	
Interest accrued		1,963,605.51	
Matured interest payable (principally due Jan. 1, 1943—contra)		624,292.00	
Preferred dividends accrued		98,158.41	
Dividends declared on preferred stocks, payable after Dec. 31, 1942		1,309,502.09	
Customers' deposits		1,318,357.60	
Long-term debt of subsidiaries due in 1943		16,000.00	
Other current and accrued liabilities		288,533.53	23,544,862.75
Customers' advances for construction			1,178,206.51
Deferred credits			288,761.45
Reserves:			
For depreciation, retirements and depletion (see Note F)		$51,132,192.03	
For claims, contingencies and other purposes		1,548,324.70	52,680,516.73
Contributions in aid of construction			1,944,204.23
Premium on preferred capital stock			462,938.71
Minority interest in common stocks and surplus of subsidiaries			2,157,649.29
Capital stock of American Water Works and Electric Company, Incorporated:			
First Preferred Stock:			
Authorized 500,000 shares—no par value Outstanding 200,000 shares—$6 Series (cumulative)		$20,000,000.00	
Common Stock:			
Authorized 2,500,000 shares—no par value Issued 2,352,950 shares	$23,529,500.00		
Less 9,845 shares held in system	98,450.00	23,431,050.00	43,431,050.00
Capital surplus (no change during year)		$ 1,318,067.97	
Earned surplus, including earned surplus of predecessor company, American Water Works and Electric Company, Incorporated (of Virginia), and subsidiaries		20,938,424.02	22,256,491.99
Total liabilities, capital and surplus			$433,405,731.66

See Notes on pages 24 to 27.

American Water Works and Electric Company, Incorporated

AND SUBSIDIARY COMPANIES

COMPARATIVE CONSOLIDATED INCOME ACCOUNT

	For Year Ended Dec. 31, 1942	Dec. 31, 1941	Increase or Decrease*
Operating revenues:			
Electric	$47,023,501.86	$43,657,077.60	$3,366,424.26
Water	15,300,219.41	14,602,002.18	698,217.23
Gas	982,780.42	1,028,871.68	46,091.26*
Railway	1,887,589.95	1,336,290.65	551,299.30
Bus	3,608,990.20	2,211,111.31	1,397,878.89
Other	29,069.27	31,126.73	2,057.46*
Total operating revenues	$68,832,151.11	$62,866,480.15	$5,965,670.96
Expenses:			
Operating expenses	$22,496,302.87	$21,242,975.26	$1,253,327.61
Maintenance	4,410,030.69	4,363,719.91	46,310.78
Federal taxes on income (see Note G)	10,411,550.00	6,808,147.84	3,603,402.16
Other taxes	6,653,906.27	6,423,406.26	230,500.01
Provision for depreciation, retirements and depletion (see Note F)	6,180,801.64	5,335,533.04	845,268.60
Amortization of property account adjustments (see Note H)	432,519.36	831,190.72	398,671.36*
Total expenses	$50,585,110.83	$45,004,973.03	$5,580,137.80
Operating income	$18,247,040.28	$17,861,507.12	$ 385,533.16
Non-operating income	521,910.78	827,273.45	305,362.67*
Gross income	$18,768,951.06	$18,688,780.57	$ 80,170.49
Deductions—Subsidiaries:			
Interest	$ 7,545,332.47	$ 7,585,306.43	$ 39,973.96*
Interest charged to construction—credit	*101,215.16*	*223,299.24*	122,084.08
Amortization of debt discount, premium (net) and expense (see Note C)	967,036.29	849,164.93	117,871.36
Preferred dividends	5,267,519.42	5,264,139.08	3,380.34
Minority interests	280,789.32	276,041.00	4,748.32
Miscellaneous	197,457.93	169,823.12	27,634.81
	$14,156,920.27	$13,921,175.32	$ 235,744.95
Balance	$ 4,612,030.79	$ 4,767,605.25	$ 155,574.46*
Deductions—American Water Works and Electric Company, Incorporated:			
Interest	$ 831,525.33	$ 851,626.67	$ 20,101.34*
Amortization of debt discount and expense	71,853,47	90,192.26	18,338.79*
Miscellaneous	16,454.03	17,122.81	668.78*
	$ 919,832.83	$ 958,941.74	$ 39,108.91*
Net income, including special tax adjustment in 1942—see below	$ 3,692,197.96	$ 3,808,663.51	$ 116,465.55*
Net income before special tax adjustment	$ 2,883,997.96‡		
Tax adjustment†	808,200.00		
Net income transferred to Earned Surplus	$ 3,692,197.96		

‡Equivalent to 72¢ per share on the common stock after preferred dividends.
†Reduction in Federal taxes on income due to amortization of certain facilities under Necessity Certificates issued by the War Department.

American Water Works and Electric Company, Incorporated
AND SUBSIDIARY COMPANIES

CONSOLIDATED EARNED SURPLUS ACCOUNT
YEAR ENDED DECEMBER 31, 1942

Balance at January 1, 1942		$18,881,439.16
Add:		
Net income for year ended December 31, 1942		3,692,197.96
		$22,573,637.12
Deduct:		
Dividends on $6 Series, First Preferred Stock of American Water Works and Electric Company, Incorporated		$ 1,200,000.00
Amortization of commission, redemption premium and expense on capital stock issues	$485,257.63	
Sundry adjustments (net credit)	*25,165.27*	
	$460,092.36	
Less:		
Proportion of surplus adjustments applicable to common stocks of subsidiaries held by public	24,879.26	
		435,213.10
		$ 1,635,213.10
Balance at December 31, 1942		$20,938,424.02

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS OF AMERICAN WATER WORKS AND ELECTRIC COMPANY, INCORPORATED, AND SUBSIDIARIES

The consolidated accounts include all subsidiary companies over 50% of whose voting stock is owned, directly or indirectly, by the Company, with the exception of two minor subsidiaries and Community Water Service Company and its subsidiaries. At December 31, 1942, the equity applicable to the investments of the Company and a consolidated subsidiary in the net assets of Community Water Service Company and its subsidiary companies, based on the consolidated accounts of that group, amounted to $4,261,032.88. The equity of the Company and a consolidated subsidiary in the consolidated net income of Community Water Service Company and its subsidiaries was $357,209.22 for 1942 and $377,421.06 for 1941.

The preferred stocks of certain subsidiaries in the hands of the public have equal voting rights with the common stocks and comprise a substantial percentage of the total voting stock in such instances; however, such subsidiaries are included in the consolidation since the Company owns at least 94% of the common stock in each case.

* * * * * *

Note A: Property, plant and equipment comprises electric generating stations, electric and gas transmission and distribution systems, electric railways, buses, water pumping stations, reservoirs, water distribution systems, real estate, intangibles, etc., and includes $15,460,227.92 representing the excess of carrying values of the investments of the Company and of its subsidiaries, in securities of their respective subsidiaries over the underlying book equity of the subsidiaries at the respective dates of acquisition, as subsequently adjusted.

The uniform systems of accounts prescribed by the Federal and State commissions having jurisdiction over the electric, gas and certain of the water subsidiaries provide for a reclassification of the companies' utility plant accounts to set forth, among other things, the "original cost" of such plant (generally defined as "the cost of such property to the person first devoting it to public service"), and for the segregation of the differences between book cost and "original cost" in separate plant adjustment accounts to be depreciated, amortized, or otherwise disposed of as the commissions may approve or direct. The status of the subsidiaries under the foregoing requirements is generally as follows:

SUBSIDIARY WATER COMPANIES

Uniform systems of accounts, which are applicable to ten of the subsidiary water companies, require the determination of "original cost." Nine companies with combined property accounts of $45,658,635 have completed their studies (one company with property of $1,370,175 has not completed its study) and filed the results thereof with the respective State commissions. After giving effect to subsequent adjustments on the companies' books, the studies so filed reflected amounts aggregating $5,523,920 in Account 100.5—Utility Plant Acquisition Adjustments, and amounts aggregating $1,963,609 in Account 107—Utility Plant Adjustments. These studies are subject to review and possible revision.

WEST PENN POWER COMPANY AND ITS CONSOLIDATED SUBSIDIARIES

During 1939, the companies filed with the commissions, where required, reports with respect to the "original cost" of their properties as of December 31, 1936, based on studies made by or on behalf of the companies. Such reports have not been approved by the respective commissions. Important controversial questions exist as to the method of determining "original cost" and related matters, and further studies are being made for the purpose of developing additional data desired by the regulatory bodies. Accordingly, the amount and nature of the adjustments which will be necessary in the accounts to reflect "original cost" and related matters cannot be determined until the pending studies are completed and until the controversial questions are settled. In the reports which were filed with the commissions in 1939, and which have not been approved by the commissions, the excess of book cost over "original cost" of the properties at December 31, 1936, was reported at $9,191,457 which figure is reduced to $7,793,247 as a result of a subsequent adjustment of the books of a subsidiary company. This amount was classified in the filed reports as follows: Account 100.5—Utility Plant Acquisition Adjustments $12,189,467, Account 107—Utility Plant Adjustments (credit) $4,396,220. If the controversies in question are finally resolved against the company such excess will probably be substantially greater than $7,793,247 and the classification of the excess as between Accounts 100.5 and 107 will be substantially different from that shown above.

MONONGAHELA WEST PENN PUBLIC SERVICE COMPANY AND SUBSIDIARIES

Electric, gas and water properties have, with minor exceptions, been reclassified on the basis of the "original cost" of the properties under requirements of State and Federal commissions having jurisdiction over the companies. In addition to "original cost," the property accounts include amounts of $1,749,570.68 classified as Account 100.5 Electric Plant Acquisition Adjustments and $900,750.06 of gas and water plant acquisition adjustments (Account 100.5) which represent the differences between "original cost" and cost to the company of such properties. An additional amount of $2,169,035.28, classified as Account 107—Utility Plant Adjustments, represents amounts claimed as cost by the company but set aside in this account by authority or order of appropriate commissions and in respect of which a reserve of a like amount has been deducted pending determination of the final disposition of this adjustment account. Certain relatively small subsidiary gas and electric companies have completed their "original cost" studies and filed the results of such studies with the respective regulatory commissions but no entries have been recorded on the books pending receipt of proper commission authorization. The plant adjustment accounts shown by the latter studies total approximately $50,000.

THE POTOMAC EDISON COMPANY AND SUBSIDIARIES

In respect of these companies, the property, plant and equipment account includes, in addition to "original cost," Account 100.5—Electric Plant Acquisition Adjustments of approximately $1,230,000 representing the excess of the cost to the companies of electric plant over "original cost." In this connection the regulatory authorities have reserved the right to examine the companies' records and to order such adjusting entries as may be appropriate.

Note B: The Emergency Plant Facilities Contract between the United States Government and Monongahela West Penn Public Service Company, a subsidiary, under which these facilities were constructed, provides, among other things, that the title to the facilities will be in the subsidiary but also provides for reimbursement by the Government for the cost of such facilities over a five-year period commencing after completion. The contract also provides that the subsidiary may retain certain or all of these facilities at a price or prices specified in the contract or to be agreed upon when the emergency is terminated, or shall transfer the same to the Government.

Note C: The balance of unamortized debt discount, premium (net) and expense is being amortized over the lives of the various bond issues on a straight line basis, it being the general practice of the companies, where bonds are refunded in advance of their maturity dates, to continue the amortization of debt discount and expense applicable to such issues to the original maturity dates thereof and to amortize call premiums and interest, incurred in connection with the refundings, over the life of the new bonds.

However, under an order by the Federal Power Commission dated February 3, 1942, $1,104,855 of unamortized expense, redemption premium and interest applicable to certain refunded issues is being amortized over a five-year period from December 31, 1941. As a result, the amount of amortization charged to income in 1942 was increased by $128,480.

Note D: To and including the year ended December 31, 1930, commission and expense on issues of capital stock were written off to surplus over a ten-year period from the original date of the issue of the stock. Beginning with the year 1931, this basis was changed to a thirty-year period from the original date of issue of stock, based upon the balance remaining on the books at January 1, 1931, for each individual issue. Exceptions exist in the case of two subsidiaries which under orders of regulatory commissions are amortizing, by charges to earned surplus over five-year periods, the amounts of cash premiums paid and cash adjustments made on the exchange and redemption of preferred stocks, and commissions and expenses paid on the issuance of new preferred stocks. For the year 1942, the aggregate amount charged to earned surplus in respect of amortization on the five-year basis was approximately $460,000.

Note E: Long-term debt of subsidiaries includes $136,000 due within five years. At December 31, 1942, there were no arrears in dividends on preferred capital stocks of consolidated subsidiaries held by the public.

Note F: The companies' provisions for depreciation, retirements and depletion are presently determined for the various classes of operating companies in accordance with the following general principles:

1. In the case of the water works properties, provisions for depreciation and retirements are based upon the application of fixed rates to depreciable property. For certain of the companies, the rates used are determined by officers and engineers of the companies while for others the rates are prescribed by or agreed upon with State regulatory commissions or other public agencies. Certain of the companies have bond indentures under which they are required to provide for depreciation and retirements amounts not less than the difference between a percentage of operating revenue, ranging from 9% to 12½%, and the amounts expended for maintenance.

2. In the case of electric and gas subsidiaries, the uniform systems of accounts prescribed by Federal and State commissions having jurisdiction require generally that each utility shall record as of the end of each month the estimated amount of depreciation accrued during that month on depreciable utility plant. Such subsidiaries are providing reserves for depreciation by charges to income determined from time to time by officers and engineers of the companies. The extent to which regulatory action in connection with depreciation, "original cost" studies (see Note A) and other related matters will affect the companies' accounts cannot at present be ascertained.

3. In the case of bus properties, provisions for depreciation are based upon the estimated service life of the equipment as determined by the companies.

4. In the case of electric railway properties, specific amounts are provided for retirements by West Penn Railways Company, the principal electric railway subsidiary, based on the requirements estimated to be necessary to provide for the retirements of equipment and rolling stock. In 1942 an additional amount of approximately $142,000 was provided from income which represented the approximate net income from that subsidiary's railway operations for the year. Electric subsidiaries which have railway properties, provide for depreciation of all their properties without segregating the provisions as between the various classes of property. Abandonments of railway properties are generally not charged to reserves provided from income, but, in the case of Monongahela West Penn Public Service Company, are charged on the books of the subsidiaries to reserves provided in prior years from the reduction of the par value of common stock and in the case of West Penn Railways Company to capital surplus or reserves result-

ing from unrealized appreciation in investments in a system company. In 1942 $399,073.83 of railway abandonments were charged to such reserves by West Penn Railways Company. In the consolidated accounts such treatment by West Penn Railways Company results in (1) a decrease in property, plant and equipment and (2) a corresponding increase in "Excess of carrying values of the investments of the Company and of its subsidiaries in securities of their respective subsidiaries over the underlying book equity of the subsidiaries at the respective dates of acquisition, as subsequently adjusted," which is included under property, plant and equipment in the consolidated balance sheet. The approximate carrying value of electric railway properties on the books of subsidiaries at December 31, 1942 was $19,600,000 after deducting specific reserves of $3,700,000 for abandonment of railway properties.

5. One subsidiary company owns certain gas wells and provides a reserve for depletion based on the requirements of the mortgage covering the subsidiary's property.

The companies' provisions for depreciation, retirements and depletion have been less than the amounts claimed or to be claimed as deductions in their Federal income tax returns, which are determined in accordance with understandings reached with the Bureau of Internal Revenue. Approximately $1,250,000 is to be claimed in the Federal income tax returns of certain of the companies for 1942 in respect of amortization of facilities on a five-year basis under Necessity Certificates issued by the War Department. In the consolidated income account, depreciation on these facilities has been provided in accordance with the usual practice of the companies. The aggregate amounts claimed or to be claimed by the companies as depreciation deductions in their Federal income tax returns for the years 1941 and 1942, exclusive of claims in 1942 for amortization of facilities referred to above, were $7,657,632 and approximately $7,700,000, respectively.

Note G: The provision for "Federal taxes on income" shown in the consolidated income account for 1942 consists of the following:

Excess profits tax		$ 6,131,142
Less—Post war credit	$419,921	
Credit for debt retirement	193,170	613,091
		$ 5,518,051
Normal income tax and surtax		4,893,499
Total Federal taxes on income		$10,411,550

The foregoing Federal taxes on income are $808,200 less than they would have been if the companies had not claimed as deductions in their Federal tax returns amortization of certain facilities over a five-year period under Necessity Certificates issued by the War Department. Also non-recurring deductions for income tax purposes which were allowable as a result of bond issues refunded by various water company subsidiaries during 1941 had the effect of reducing Federal taxes on income below what they otherwise would have been by amounts estimated at $425,000 in 1941 and $125,000 in 1942.

Note H: "Amortization of property account adjustments" includes amounts charged to income by an electric subsidiary for amortization of a portion of the excess of carrying values of its investments in securities of its subsidiaries over the cost of such investments, and also includes in 1941 amounts provided by certain electric subsidiaries for amortization of amounts carried in "Electric plant adjustments in process of amortization" which account on the books of the subsidiaries in question, was completely written off in that year. In addition, "Amortization of property account adjustments" includes amounts provided by certain subsidiary water companies for amortization of Account 100.5—Utility Plant Acquisition Adjustments.

COMPARATIVE STATISTICAL SUMMARY

Electric Power and Light Properties

	As of December 31, 1942	1941
Generating Stations—Kilowatt:§		
Steam Stations	623,870	623,870
Hydro Stations	57,330	57,390
Oil and Gas Stations	2,239	2,239
Total	683,439	683,499
Net Kilowatt-Hour Output*	3,782,149,134	3,343,692,757
Number of Electric Customers	451,194	446,421
Transmission Lines—Pole Miles:		
132,000 Volts	473	473
66,000 Volts	336	334
Less than 66,000 Volts	2,742	2,725
Total	3,551	3,532

Transportation Properties

	1942	1941
Electric Railways:		
Miles of Track	285	291
Number of Cars	179	183
Bus Lines Operated:		
Miles of Route	1,633	1,658
Number of Buses	213	203

Water Works Properties

—Excluding subsidiaries of Community Water Service Company—

	1942	1941
Pumping Stations—Gallons Per Day:		
Distributive Service	789,379,300	785,059,300
Low Service	674,563,000	677,800,600
Relay Service	334,501,840	300,229,000
Transmission and Distribution Mains—Miles	6,411	6,347
Gallons of Water Sold*	71,206,768,000	66,520,001,000
Number of Water Customers	493,168	485,003

—Subsidiaries of Community Water Service Company—
(Data adjusted for properties sold in 1942)

	1942	1941
Pumping Stations—Gallons per Day:		
Distributive Service	228,035,000	226,309,800
Low Service	183,001,800	163,035,800
Relay Service	66,690,900	85,101,000
Transmission and Distribution Mains—Miles	2,491	2,478
Gallons of Water Sold*	20,831,467,000	20,090,978,000
Number of Water Customers	195,302	194,004

§Based on name-plate ratings.
*Twelve months ended December 31.