

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

FORM 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2004

Commission File
Number 1-6659

AQUA AMERICA, INC. (formerly Philadelphia Suburban Corporation)

(Exact name of registrant as specified in its charter)

Pennsylvania

23-1702594

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer Identification No.)

762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania

19010-3489

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including
area code:

(610) 527-8000

Securities registered pursuant to Section
12(b) of the Act:

Title of each class

Name of each exchange on
which registered

Common stock, par value \$.50 per share

New York Stock Exchange, Inc.
Philadelphia Stock Exchange Inc.

Securities registered pursuant to Section
12(g) of the Act: None

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 filing requirements for the past 90 days.

Yes No
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Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendments to this Form 10-K. []

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12(b)-2).

Yes No
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The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant as of June 30, 2004. \$1,851,041,022

For purposes of determining this amount only, registrant has defined affiliates as including (a) the executive officers named in Part I of this 10-K report, (b) all directors of registrant, and (c) each shareholder that has informed registrant by June 30, 2004, that it has sole or shared voting power of 5% or more of the outstanding common stock of registrant.

The number of shares outstanding of each of the registrant's classes of common stock as of February 18, 2005. 95,475,161

Documents incorporated by reference

(1) Portions of registrant's 2004 Annual Report to Shareholders have

been incorporated by reference into Parts I and II of this Form 10-K Report.

(2) Portions of the Proxy Statement, relative to the May 19, 2005 annual meeting of shareholders of registrant, to be filed within 120 days after the end of the fiscal year covered by this Form 10-K Report, have been incorporated by reference into Part III of this Form 10-K Report.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain statements in this Annual Report on Form 10-K ("10-K"), or incorporated by reference into this 10-K, are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 that are made based upon, among other things, our current assumptions, expectations and beliefs concerning future developments and their potential effect on us. These forward-looking statements involve risks, uncertainties and other factors, many of which are outside our control, that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. In some cases you can identify forward-looking statements where statements are preceded by, followed by or include the words "believes," "expects," "anticipates," "plans," "future," "potential" or the negative of such terms or similar expressions. Forward-looking statements in this 10-K, or incorporated by reference into this 10-K, include, but are not limited to, statements regarding:

- o projected capital expenditures and related funding requirements;
- o developments, trends and consolidation in the water and wastewater utility industries;
- o dividend payment projections;
- o opportunities for future acquisitions, the success of pending acquisitions and the impact of future acquisitions;
- o the capacity of our water supplies, water facilities and wastewater facilities;
- o the impact of geographic diversity on our exposure to unusual weather;
- o our capability to pursue timely rate increase requests;
- o our authority to carry on our business without unduly burdensome restrictions;
- o our ability to obtain fair market value for condemned assets;
- o the impact of fines and penalties;
- o the development of new services and technologies by us or our competitors;
- o the availability of qualified personnel;
- o the condition of our assets;
- o the impact of legal proceedings;
- o general economic conditions;
- o acquisition-related costs and synergies; and
- o the forward-looking statements contained under the heading "Forward-Looking Statements" in the section entitled "Management's Discussion and Analysis" from the portion of our 2004 Annual Report to Shareholders incorporated by reference herein and made a part hereof.

Because forward-looking statements involve risks and uncertainties, there are important factors that could cause actual results to differ materially

from those expressed or implied by these forward-looking statements, including but not limited to:

- o changes in general economic, business and financial market conditions;
- o changes in government regulations and policies, including environmental and public utility regulations and policies;

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- o changes in environmental conditions, including those that result in water use restrictions;
- o abnormal weather conditions;
- o changes in capital requirements;
- o changes in our credit rating;
- o our ability to integrate businesses, technologies or services which we may acquire;
- o our ability to manage the expansion of our business;
- o the extent to which we are able to develop and market new and improved services;
- o the effect of the loss of major customers;
- o our ability to retain the services of key personnel and to hire qualified personnel as we expand;
- o unanticipated capital requirements;
- o increasing difficulties in obtaining insurance and increased cost of insurance;
- o cost overruns relating to improvements or the expansion of our operations; and
- o civil disturbance or terroristic threats or acts.

Given these uncertainties, you should not place undue reliance on these forward-looking statements. You should read this 10-K and the documents that we incorporate by reference into this 10-K completely and with the understanding that our actual future results may be materially different from what we expect. These forward-looking statements represent our estimates and assumptions only as of the date of this 10-K. Except for our ongoing obligations to disclose material information under the federal securities laws, we are not obligated to update these forward-looking statements, even though our situation may change in the future. We qualify all of our forward-looking statements by these cautionary statements.

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PART I

Item 1. Business

Name Change

On January 16, 2004, Philadelphia Suburban Corporation changed its corporate name to Aqua America, Inc. In addition, we changed our ticker symbol from PSC to WTR on the New York Stock Exchange and Philadelphia Stock Exchange effective as of the opening of trading on January 20, 2004.

The Company

Aqua America, Inc. (referred to as "Aqua America", "we" or "us") is the holding company for regulated utilities providing water or wastewater services to what we estimate to be more than 2.5 million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Florida, Indiana, Virginia, Maine, Missouri, New York and South Carolina. Our largest operating subsidiary, Aqua Pennsylvania, Inc. - formerly Pennsylvania Suburban Water Company - accounts for approximately 55% of our operating revenues and provides water or wastewater services to approximately 1.3 million residents in the suburban areas north and west of the City of Philadelphia and in 21 other counties in Pennsylvania. Our other subsidiaries provide similar services in 12 other states. In addition, we provide water and wastewater service through operating and maintenance contracts with municipal authorities and other parties close to our operating companies' service territories. We are the largest U.S.-based publicly-traded water utility based on number of people served.

The following table reports our operating revenues by principal state for the year ended December 31, 2004:

	Operating Revenues (000's)

Pennsylvania	\$ 254,034
Ohio	37,679
Illinois	32,134
Texas	30,334
New Jersey	20,908
North Carolina	17,846
Indiana	15,344
Florida	12,672
Maine	9,403
Virginia	7,882
Other states	3,803

	\$ 442,039
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The following table indicates by customer class our operating revenues for the year ended December 31, 2004:

Customer class	Operating Revenues (000's)	Percent
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Residential water	\$264,910	60%
Commercial water	65,605	15%
Fire protection	20,771	5%
Industrial water	17,377	4%
Other water	23,822	5%
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Water	392,485	89%
Wastewater	35,931	8%
Water and wastewater operating contracts and other	13,623	3%
	-----	-----
	\$442,039	100%
	=====	=====

Our customer base is diversified among residential, commercial, industrial, other water, wastewater customers and operating contracts and other customers. Residential customers make up the largest component of our customer base, with these customers representing 60% of our total water revenues. Substantially all of our water customers are metered, which allows us to measure and bill for our customers' water consumption. Water consumption per customer is affected by local weather conditions during the year, especially during the late spring and early summer in our northern U.S. service territories. In general, during these seasons, an extended period of dry weather increases consumption, while above average rainfall decreases water consumption. Also, an increase in the average temperature generally causes an increase in water consumption. On occasion, abnormally dry weather in our service areas can result in governmental

authorities declaring drought warnings and water use restrictions in the affected areas, which could reduce water consumption. See "Water Supplies, Water Facilities and Wastewater Facilities" for a discussion of water use restrictions that may impact water consumption during abnormally dry weather. The geographic diversity of our customer base reduces our exposure to extreme or unusual weather conditions in any one area of our service territory.

The growth in revenues over the past three years is a result of increases in the customer base and in water rates. The majority of the increase in customer base is due to customers added through acquisitions. During the three-year period of 2000 through 2002, our customer base increased at an annual compound rate of 3.3%. The customer growth rate in 2003 was 23.8%, and reflects the additional customers obtained in the AquaSource acquisition on July 31, 2003. In 2004, the customer growth rate was 11.5% and reflects the additional customers added through the Heater and Florida Water Services acquisitions. Overall, for the five-year period of 2000 through 2004, our customer base increased at annual compound rate of 8.8%.

Available Information

We file annual, quarterly and current reports, proxy statements and other information with the Securities and Exchange Commission ("SEC"). You may read and copy any document we file at the SEC's public reference room at 450 Fifth Street, N.W., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. You may also obtain our SEC filings from the SEC's Web site at www.sec.gov.

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Our Internet Web site address is <http://www.aquaamerica.com>. We make available free of charge through our internet website's Investor Relations page all of our filings with the SEC, including our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and other information. These reports and information are available as soon as reasonably practicable after such material is electronically filed or furnished to the SEC.

Our Board of Directors has various committees including an audit committee, an executive compensation and employee benefits committee and a corporate governance committee. Each of the three committees named above has a formal charter. We also have Corporate Governance Guidelines and a Code of Ethical Business Conduct. Copies of these charters, guidelines and codes, and any waivers or amendments to such codes which are applicable to our executive officers, senior financial officers or directors, can be obtained free of charge from our Web site, www.aquaamerica.com.

In addition, you may request a copy of the foregoing filings, charters, guidelines and codes, and any waivers or amendments to such codes which are applicable to our executive officers, senior financial officers or directors, at no cost by writing or telephoning us at the following address or telephone number:

Investor Relations Department
Aqua America, Inc.
762 W. Lancaster Avenue
Bryn Mawr, PA 19010-3489
Telephone: 610-527-8000

Acquisitions and Water Sale Agreements

With more than 50,000 community water systems in the U.S. (84% of which serve less than 3,300 customers), the water industry is the most fragmented of the major utility industries (telephone, natural gas, electric, water and wastewater). The nation's water systems range in size from large municipally-owned systems, such as the New York City water system that serves approximately 9 million people, to small systems, where a few customers share a common well. In the states where we operate, we believe there are over 22,000 public water systems of widely varying size, with the majority of the population being served by government-owned water systems.

Although not as fragmented as the water industry, the wastewater industry in the U.S. also presents opportunities for consolidation. According to the U.S Environmental Protection Agency's ("EPA") most recent survey of

publicly-owned wastewater treatment facilities in 2000, there are approximately 16,000 such facilities in the nation serving approximately 72% of the U.S. population. The remaining population represents individual homeowners with their own treatment facilities; for example, community on-lot disposal systems and septic tank systems. The vast majority of wastewater facilities are government-owned rather than privately-owned. The EPA survey also indicated that there are approximately 6,600 wastewater facilities in operation or planned in the 13 states where we operate.

Because of the fragmented nature of the water and wastewater utility industries, we believe that there are many potential water and wastewater system acquisition candidates throughout the United States. We believe the factors driving consolidation of these systems are:

- o the benefits of economies of scale;
- o increasingly stringent environmental regulations;
- o the need for capital investment; and
- o the need for technological and managerial expertise.

We are actively exploring opportunities to expand our utility operations through acquisitions or other growth ventures. As of December 31, 2004, we had completed 111 acquisitions or other growth ventures during the past five years.

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We believe that acquisitions will continue to be an important source of growth for us. We intend to continue to pursue acquisitions of municipally-owned and investor-owned water and wastewater systems of all sizes that provide services in areas adjacent to our existing service territories or in new service areas. We engage in continuing activities with respect to potential acquisitions, including calling on perspective sellers, performing analyses and investigations of acquisition candidates, making preliminary acquisition proposals and negotiating the terms of potential acquisitions.

Water Supplies, Water Facilities and Wastewater Facilities

Our water utility operations obtain their water supplies from surface water sources such as reservoirs, lakes, ponds, rivers and streams, in addition to obtaining water from wells and purchasing water from other water suppliers. Less than 10% of our water sales are purchased from other suppliers. It is our policy to obtain and maintain the permits necessary to obtain the water we distribute.

Our supplies by principal service area are as follows:

- o Suburban Philadelphia - The principal supply of water is surface water from eight rural streams, two rivers (Schuylkill River and Delaware River), and the Upper Merion Reservoir, a former quarry now impounding groundwater. Wells and interconnections with adjacent municipal authorities supplement these surface supplies.
- o Pennsylvania (other than suburban Philadelphia) - The Roaring Creek Division draws its water from a man-made lake within a 12,000 acre watershed and two wells also located in the watershed. The Susquehanna Division obtains its water supply from wells. The Shenango Division draws its water from the Shenango River. The Waymart and Whitehaven Divisions' water supply is obtained from wells.
- o Ohio - Water supply is obtained for customers in Lake County from Lake Erie. Customers in Mahoning County obtain their water from man-made lakes and the Ashtabula division is supplied by purchased water. Water supply is obtained for customers in Stark and Summit Counties from wells. In Trumbull County, customers are served through an interconnection from our Pennsylvania division.
- o North Carolina - Water supply in 669 divisions is obtained principally from wells, with several divisions purchasing water from neighboring municipalities.
- o Illinois - Water supply is obtained for customers in Kankakee County from the Kankakee River and satellite wells, while customers in Vermilion County are supplied from Lake Vermilion. In Will, Lee, Boone, Lake and Knox counties, our customers are served from wells.
- o Texas - Water supply in 295 non-contiguous water systems is obtained principally from wells, supplemented in some cases by purchased water from adjacent surface water systems.
- o Florida - Water supply in the majority of the 70 water systems is obtained principally from wells, supplemented in some cases by purchased water from

- adjacent surface water systems.
- o New Jersey - Water supply in our three non-contiguous divisions is obtained principally from wells and is supplemented with purchased water in two divisions.
 - o Indiana - Water supply in three water systems is obtained principally from wells.
 - o Virginia - Water supply in 124 non-contiguous divisions is obtained from wells, one division's supply is from surface water, and four divisions supplement their supply with purchased water from a nearby water system.
 - o Maine - Eleven non-contiguous water systems obtain their water supply as follows: five systems use groundwater, five systems use surface water and one system purchases water from a neighboring municipal district.

Generally we believe that the capacities of our sources of supply, and our water treatment, pumping and distribution facilities are generally sufficient to meet the present requirements of our customers under normal conditions. We plan system improvements and additions to capacity in response to changing regulatory standards, changing patterns of consumption and increased demand from a growing number of customers. The various state public utility commissions have generally recognized the operating and capital costs associated with these improvements in setting water rates.

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On occasion, drought warnings and water use restrictions are issued by governmental authorities for portions of our service territories in response to extended periods of dry weather conditions. The timing and duration of the warnings and restrictions can have an impact on our water revenues and net income. In general, water consumption in the summer months is affected by drought warnings and restrictions to a higher degree because nonessential and recreational use of water is at its highest during the summer months. At other times of the year, warnings and restrictions generally have less of an effect on water consumption.

We have not had a drought warning or drought emergency since 2002. A drought warning calls for a 10 to 15 percent voluntary reduction of water use, particularly non-essential uses of water. A drought emergency imposes a ban on nonessential water use.

We believe that our wastewater treatment facilities are generally adequate to meet the present requirements of our customers. In addition, we own several sewer collection systems where the wastewater is treated at a municipally-owned facility. Capital funds are budgeted to address inflow and infiltration in the collection systems, and wet weather flows at our lift stations and treatment plants, and other conditions and requirements can affect compliance. Changes in regulatory requirements may be reflected in revised permit limits and conditions when NPDES permits are renewed, typically on a five-year cycle. Capital improvements are planned and budgeted to meet anticipated changes in regulations and needs for increased capacity related to projected growth. The various state public utility commissions have generally recognized the operating and capital costs associated with these improvements in setting wastewater rates for current customers and capacity charges for new customers.

Economic Regulation

Most of our water and wastewater utility operations are subject to regulation by their respective state regulatory commissions, which have broad administrative power and authority to regulate rates and charges, determine franchise areas and conditions of service and authorize the issuance of securities. The regulatory commissions also establish uniform systems of accounts and approve the terms of contracts with affiliates and customers, business combinations with other utility systems, loans and other financings, and the franchise areas that we serve. Some of our operations are subject to rate regulation by county or city governments. The profitability of our utility operations is influenced to a great extent by the timeliness and adequacy of rate allowances in the various states in which we operate. Accordingly, we maintain a rate case management capability to provide that the tariffs of our utility operations reflect, to the extent practicable, the timely recovery of increases in costs of operations, capital, taxes, energy, materials and compliance with environmental regulations. In the states in which we operate, we are subject to regulation by the following state regulatory commissions:

State

Regulatory Commission

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Pennsylvania	Pennsylvania Public Utility Commission
Ohio	The Public Utilities Commission of Ohio
North Carolina	North Carolina Utilities Commission
Illinois	Illinois Commerce Commission
Texas	Texas Commission on Environmental Quality
New Jersey	New Jersey Board of Public Utilities
Florida	Florida Public Service Commission
Indiana	Indiana Utility Regulatory Commission
Virginia	Virginia State Corporation Commission
Maine	Maine Public Utilities Commission
Missouri	Missouri Public Service Commission
New York	New York Public Service Commission
South Carolina	South Carolina Public Service Commission

Four states in which we operate permit water utilities, and in some states wastewater utilities, to add a surcharge to their water or wastewater bills to offset the additional depreciation and capital costs associated with certain capital expenditures related to replacing and rehabilitating infrastructure systems. Prior to these mechanisms being approved, water and wastewater utilities absorbed all of the depreciation and capital costs of these projects between base rate increases without the benefit of additional revenues. The gap between the time that a capital project is completed and the recovery of its costs in rates is known as regulatory lag. The infrastructure rehabilitation surcharge mechanism is intended to substantially reduce regulatory lag which often acted as a disincentive to water and wastewater utilities to rehabilitate their infrastructure. In addition, our subsidiaries in certain states use a surcharge or credit on their bill to reflect changes in certain costs, such as changes in state tax rates, until such time as the costs are incorporated into base rates.

Currently, Pennsylvania, Illinois, Ohio and Indiana allow for the use of infrastructure rehabilitation surcharges. These mechanisms typically adjust periodically based on additional qualified capital expenditures completed or anticipated in a future period. The infrastructure rehabilitation surcharge is capped at a percentage of base rates, generally 5% of base rates, and is reset to zero when new base rates that reflect the costs of those additions become effective or when a utility's earnings exceed a regulatory benchmark. Infrastructure rehabilitation surcharges provided revenues of \$7,817,000 in 2004, \$8,147,000 in 2003 and \$5,518,000 in 2002.

In general, we believe that Aqua America, Inc. and its subsidiaries have valid authority, free from unduly burdensome restrictions, to enable us to carry on our business as presently conducted in the franchised or contracted areas we now serve. The rights to provide water or wastewater service to a particular franchised service territory are generally non-exclusive, although the applicable regulatory commissions usually allow only one regulated utility to provide service to a given area. In some instances, another water utility provides service to a separate area within the same political subdivision served by one of our subsidiaries.

In the states where our subsidiaries operate, it is possible that portions of our subsidiaries' operations could be acquired by municipal governments by one or more of the following methods:

- o eminent domain;
- o the right of purchase given or reserved by a municipality or political subdivision when the original franchise was granted; and
- o the right of purchase given or reserved under the law of the state in which the subsidiary was incorporated or from which it received its permit.

The price to be paid upon such an acquisition by the municipal government is usually determined in accordance with applicable law governing the taking of lands and other property under eminent domain. In other instances, the price may be negotiated, fixed by appraisers selected by the parties or computed in accordance with a formula prescribed in the law of the state or in the particular franchise or charter.

In December 2004, as a result of the settlement of a condemnation action, our Ohio operating subsidiary sold its water utility assets within the municipal boundaries of the City of Geneva in Ashtabula County, Ohio for net

proceeds of approximately \$4,716,000, which was in excess of the book value for these assets. The sale resulted in the recognition in the fourth quarter of 2004 of a gain on the sale of these assets, net of expenses, of \$2,342,000. We continue to operate this water system for the City of Geneva under an operating contract that began upon the closing of the sale for a period through December 2006. The operating contract provides for an annual base operating fee of \$135,000 and allows for additional fees to be earned commensurate with the services provided. These water utility assets represent less than 1% of Aqua America's total assets, and the total number of customers included in the water system sold represents less than 1% of our total customer base.

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In December 2002, as a result of the settlement of a condemnation action, our Ohio operating subsidiary sold its water utility assets in the unincorporated areas of Ashtabula County and the area within the Village of Geneva on the Lake to Ashtabula County, Ohio for approximately \$12,118,000, which was in excess of the book value for these assets. The sale resulted in the recognition in the fourth quarter of 2002 of a gain on the sale of these assets, net of expenses, of \$5,676,000. We continue to operate this water system for Ashtabula County under a multi-year operating contract. The water utility assets sold represent less than 1% of our total assets, and the total number of customers included in the water system sold represents less than 1% of our total customer base. The increase in earnings associated with reinvesting the sale's proceeds and the operating income generated by the operating contract has offset the loss of this water system's historic contribution to income.

The City of Fort Wayne, Indiana has authorized the acquisition, by eminent domain or otherwise, of a portion of the utility assets of one of the operating subsidiaries that we acquired in connection with the AquaSource acquisition in 2003. We have challenged whether the City is following the correct legal procedures in connection with the City's attempted condemnation and we have challenged the City's valuation of this portion of our system. The portion of the system under consideration represents approximately 1% of our total customer base. While we continue to discuss this matter with officials from the City of Fort Wayne, we continue to protect our interests in this proceeding.

We believe that our operating subsidiaries will be entitled to fair market value for any assets that are condemned, and we believe the fair market value will be in excess of the book value for such assets. Despite the sales and possible condemnation referred to above, our strategy continues to be to acquire additional water and wastewater systems, maintain our existing systems, and actively oppose efforts by municipal governments to acquire any of our operations, particularly for less than the fair market value of our operations or where the municipal government seeks to acquire more than it is entitled to under the applicable law or agreement.

Environmental, Health and Safety Regulation

Provision of water and wastewater services is subject to regulation under the federal Safe Drinking Water Act, the Clean Water Act and related state laws, and under federal and state regulations issued under these laws. These laws and regulations establish criteria and standards for drinking water and for wastewater discharges. In addition, we are subject to federal and state laws and other regulations relating to solid waste disposal, dam safety and other operations. Capital expenditures and operating costs required as a result of water quality standards and environmental requirements have been traditionally recognized by state public utility commissions as appropriate for inclusion in establishing rates.

Environmental compliance issues remain at various water and wastewater facilities associated with acquired systems, including facilities acquired in connection with the AquaSource acquisition that was completed in July 2003, the Heater and Florida Water Service acquisitions completed in June 2004 and the acquisitions of small utilities in Northeastern Pennsylvania. We believe that the capital expenditures required to address these compliance issues have been budgeted in our capital program and represent less than 10% of our total capital expenditures over the next five years. We are parties to agreements with regulatory agencies in Texas, Florida, Indiana, Virginia and North Carolina under which we have committed to make certain improvements for environmental compliance. These agreements are intended to provide the regulators with

assurance that problems covered by these agreements will be addressed, and the agreements generally provide protection to us from fines, penalties and other actions while corrective measures are being implemented. We are actively working directly with state environmental officials to implement or amend these agreements as necessary. Regulatory agencies have imposed some fines and penalties with respect to existing compliance issues at the acquired operations, but none have been material. To the extent they have arisen from incidents that occurred prior to our purchase of the acquired operations, we have made indemnity claims for such amounts against the sellers under the applicable purchase agreements.

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Safe Drinking Water Act - The Safe Drinking Water Act establishes criteria and procedures for the U.S. Environmental Protection Agency to develop national quality standards for drinking water. Regulations issued pursuant to the Safe Drinking Water Act and its amendments set standards on the amount of certain microbial and chemical contaminants and radionuclides allowable in drinking water. Current requirements under the Safe Drinking Water Act are not expected to have a material impact on our operations or financial condition as we have made and are making investments to meet existing water quality standards. We may, in the future, be required to change our method of treating drinking water at certain sources of supply if additional regulations become effective.

EPA's issuance of a rule regulating radon in tap water has been postponed repeatedly since 1991. Limits for radon in tap water, if promulgated, would probably become effective 4 or 5 years after promulgation and would likely contain two standards to recognize cost-effective alternative approaches to dealing with radon in indoor air. We anticipate that the higher level established by such a rule might require treatment at a small percentage of our wells, primarily in North Carolina, Pennsylvania and Virginia. If the states in which we operate elect not to implement general radon reduction (Multi-Media Mitigation) programs, then a more stringent limit for radon could apply and a larger number of wells would be affected. We anticipate that states will adopt Multi-Media Mitigation programs, and the capital costs to comply with this future regulation could approximate \$4,000,000 over a five year period, and is less than 3% of our typical annual capital expenditures. The costs could be higher if a promulgated regulation does not allow for Multi-Media Mitigation, or states choose not to adopt such programs. It is not possible at this time to reasonably project what the potential impact on the capital budget, if any, might be from these rules, but the impact is not expected to have a material impact on our results of operations or financial condition.

The Safe Drinking Water Act provides for the regulation of radionuclides other than radon, such as radium and uranium. The new Radionuclides Rule that became effective in December 2003 left unchanged the existing standards for gross alpha and radium, but changed the monitoring protocol. The rule also added a maximum contaminant level for uranium. The rule will require additional testing over the next two years and will require treatment at some of our smaller groundwater facilities by January 2006. The capital cost of compliance is expected to be less than \$3,300,000. The impact of the new rulemaking is not expected to have a material impact on our results from operations or financial condition.

In order to remove or inactivate microbial organisms, rules were issued by the EPA to improve disinfection and filtration of potable water and reduce consumers' exposure to disinfectants and by-products of the disinfection process. In the future, we may be required to install filtration or other treatment, for one currently unfiltered surface water supply. The cost of this treatment, should it be required, is not expected to exceed \$5,000,000. Certain small groundwater systems could be reclassified as being influenced by surface water. This may require additional treatment or the development of replacement sources of supply over time, the cost for which is not expected to exceed a total of \$3,000,000.

The EPA is expected to promulgate a Long Term 2 Enhanced Surface Water Treatment Rule and a Stage 2 Disinfection/Disinfection By-product Rule in 2005. These rules are expected to result in additional one-time special monitoring costs of approximately \$200,000 over a two-year period in 2006 and 2007. The results of the monitoring might require modification of treatment, including capital improvements, in year 2008 and beyond. It is not possible at this time to reasonably project the potential impact on the capital budget, if any, from these rules, but the impact is not expected to have a material impact on our results of operations or financial condition.

The new rule lowering the limit on arsenic which was promulgated in 2001 and becomes effective in 2006, with a provision for further time extensions for small systems. The new rule will require installation of treatment or development of alternative supplies at a very limited number of our groundwater sources. The largest of these, in Pennsylvania, was equipped with a treatment mechanism in 2004 and the treatment mechanism is performing as designed. The cost of additional capital improvements elsewhere in our systems to fully achieve compliance with this regulation is not expected to exceed \$500,000.

In April 2000, the gasoline additive Methyl tert-Butyl Ether ("MtBE") was discovered in a production well in one of our operating subsidiaries at levels exceeding the state drinking water standard. The well was immediately taken out of service and alternate water supplies were obtained. Pursuant to a legal settlement reached with the company believed to be responsible for the contamination, we received \$2,000,000 in September 2004. The settlement amount was sufficient to cover our costs to develop a permanent replacement well and to cover our purchased water costs incurred on an interim basis. The replacement well was completed and placed in service in October 2004. Traces of MtBE may be found throughout the environment as the result of extensive use of MtBE as a gasoline additive.

Clean Water Act - The Clean Water Act regulates discharges from drinking water and wastewater treatment facilities into lakes, rivers, streams, and groundwater. We operate 213 facilities with such discharges in nine states. It is our policy to obtain and maintain all required permits and approvals for the discharges from these water and wastewater facilities, and to comply with all conditions of those permits and other regulatory requirements. A program is in place to monitor facilities for compliance with permitting, monitoring and reporting for wastewater discharges. From time to time, discharge violations may occur which may result in fines. We are also parties to compliance agreements with regulatory agencies in several states where we operate while improvements are being made to address wastewater discharge compliance issues. These fines and penalties, if any, are not expected to have a material impact on our results of operations or financial condition. The required costs to comply with the agreements previously cited are included in the capital budget are not expected to be significant, and are expected to be recoverable in rates.

Solid Waste Disposal - The handling and disposal of residuals and solid waste generated from water and wastewater treatment facilities is governed by federal and state laws and regulations. A program is in place to monitor our facilities for compliance with regulatory requirements, and we do not currently anticipate any major expenditures in connection with the handling and disposal of waste material from our water and wastewater operations.

Dam Safety - Our subsidiaries own seventeen major dams that are subject to the requirements of the Federal and state regulations related to dam safety. All major dams undergo an annual engineering inspection. We believe that all seventeen dams are structurally sound and well-maintained.

In Pennsylvania, the Department of Environmental Protection has recently adopted the use of a new formula for determining the magnitude of a probable maximum flood. We are studying our dams to determine what improvements may be needed to our dams as a result of this new calculation. As a result of the initial results of the studies, we have identified three dams that could require capital improvements of approximately \$7 million in the aggregate. We believe that the capital expenditures that could be required by the new formula would be recoverable in our rates. Similarly, in Ohio, the Department of Natural Resources has adopted the use of a new formula. We have studied our dams in Ohio and it has been determined that some of the dams will require improvements. Based on the preliminary results, we believe that capital expenditures of approximately \$4.2 million in the aggregate will be required on three dams in Ohio over the next two years.

Safety Standards - Our facilities and operations may be subject to inspections by representatives of the Occupational Safety and Health Administration from time to time. We maintain safety policies and procedures to maintain compliance with the Occupational Safety and Health Administration's rules and regulations, but violations may occur from time to time, which may result in fines and penalties, which are not expected to be material. We endeavor to correct such violations promptly after they are brought to our attention.

Employee Relations

As of December 31, 2004, we employed a total of 1,442 full-time employees. Our subsidiaries are parties to 10 agreements with labor unions covering 434 employees that expire at various times between March 2006 and May 2009. Based on the number of employees covered by each agreement, a substantial portion of the agreements expire in 2006.

Risk Factors

OUR BUSINESS REQUIRES SIGNIFICANT CAPITAL EXPENDITURES AND THE RATES WE CHARGE OUR CUSTOMERS ARE SUBJECT TO REGULATION. IF WE ARE UNABLE TO OBTAIN GOVERNMENT APPROVAL OF OUR REQUESTS FOR RATE INCREASES, OR IF APPROVED RATE INCREASES ARE UNTIMELY OR INADEQUATE TO COVER OUR INVESTMENTS, OUR PROFITABILITY MAY SUFFER.

The water utility business is capital intensive. On an annual basis, we spend significant sums for additions to or replacement of property, plant and equipment. Our ability to maintain and meet our financial objectives is dependent upon the rates we charge our customers. These rates are subject to approval by the public utility commissions or similar regulatory bodies in the states in which we operate. We file rate increase requests, from time to time, to recover our investments in utility plant and expenses. Once a rate increase petition is filed with a public utility commission, the ensuing administrative and hearing process may be lengthy and costly. The timing of our rate increase requests are therefore partially dependent upon the estimated cost of the administrative process in relation to the investments and expenses that we hope to recover through the rate increase to the extent approved. We can provide no assurances that any future rate increase request will be approved by the appropriate state public utility commission; and, if approved, we cannot guarantee that these rate increases will be granted in a timely or sufficient manner to cover the investments and expenses for which we initially sought the rate increase.

OUR OPERATING COSTS COULD BE SIGNIFICANTLY INCREASED IN ORDER TO COMPLY WITH NEW OR STRICTER REGULATORY STANDARDS IMPOSED BY FEDERAL AND STATE ENVIRONMENTAL AGENCIES.

Our water and wastewater services are governed by various federal and state environmental protection and health and safety laws and regulations, including the federal Safe Drinking Water Act, the Clean Water Act and similar state laws, and federal and state regulations issued under these laws by the United States Environmental Protection Agency and state environmental regulatory agencies. These laws and regulations establish, among other things, criteria and standards for drinking water and for discharges into the waters of the United States and states. Pursuant to these laws, we are required to obtain various environmental permits from environmental regulatory agencies for our operations. We cannot assure you that we have been or will be at all times in total compliance with these laws, regulations and permits. If we violate or fail to comply with these laws, regulations or permits, we could be fined or otherwise sanctioned by regulators. Environmental laws and regulations are complex and change frequently. These laws, and the enforcement thereof, have tended to become more stringent over time. While we have budgeted for future capital and operating expenditures to maintain compliance with these laws and our permits, it is possible that new or stricter standards could be imposed that will raise our operating costs. Although these costs may

be recovered in the form of higher rates, there can be no assurance that the various state public utility commissions or similar regulatory bodies that govern our business would approve rate increases to enable us to recover such

costs. In summary, we cannot assure you that our costs of complying with, or discharging liability under, current and future environmental and health and safety laws will not adversely affect our business, results of operations or financial condition.

OUR BUSINESS IS SUBJECT TO SEASONAL FLUCTUATIONS, WHICH COULD AFFECT DEMAND FOR OUR WATER SERVICE AND OUR REVENUES.

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

DROUGHT CONDITIONS MAY IMPACT OUR ABILITY TO SERVE OUR CURRENT AND FUTURE CUSTOMERS, AND MAY IMPACT OUR CUSTOMERS' USE OF OUR WATER, WHICH MAY ADVERSELY AFFECT OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

We depend on an adequate water supply to meet the present and future demands of our customers. Drought conditions could interfere with our sources of water supply and could adversely affect our ability to supply water in sufficient quantities to our existing and future customers. An interruption in our water supply could have a material adverse effect on our financial condition and results of operations. Moreover, governmental restrictions on water usage during drought conditions may result in a decreased demand for our water, even if our water reserves are sufficient to serve our customers during these drought conditions, which may adversely affect our revenues and earnings.

AN IMPORTANT ELEMENT OF OUR GROWTH STRATEGY IS THE ACQUISITION OF WATER AND WASTEWATER SYSTEMS. ANY FUTURE ACQUISITIONS WE DECIDE TO UNDERTAKE MAY INVOLVE RISKS.

An important element of our growth strategy is the acquisition and integration of water and wastewater systems in order to broaden our current, and move into new, service areas. We will not be able to acquire other businesses if we cannot identify suitable acquisition opportunities or reach mutually agreeable terms with acquisition candidates. It is our intent, when practical, to integrate any businesses we acquire with our existing operations. The negotiation of potential acquisitions as well as the integration of acquired businesses could require us to incur significant costs and cause diversion of our management's time and resources. Future acquisitions by us could result in:

- o dilutive issuances of our equity securities;
- o incurrence of debt and contingent liabilities;
- o failure to have effective internal control over financial reporting;
- o fluctuations in quarterly results; and
- o other acquisition-related expenses.

Some or all of these items could have a material adverse effect on our business and our ability to finance our business and comply with regulatory requirements. The businesses we acquire in the future may not achieve sales and profitability that would justify our investment and any difficulties we encounter in the integration process, including in the integration of controls necessary for internal control and financial reporting, could interfere with our operations, reduce our operating margins and adversely affect our internal controls. In addition, as consolidation becomes more prevalent in the water and wastewater industries, the prices for suitable acquisition candidates may increase to unacceptable levels and limit our ability to grow through acquisitions.

CONTAMINATION TO OUR WATER SUPPLY MAY RESULT IN DISRUPTION IN OUR SERVICES AND LITIGATION WHICH COULD ADVERSELY AFFECT OUR BUSINESS, OPERATING RESULTS AND FINANCIAL CONDITION.

Our water supplies are subject to contamination, including contamination from the development of naturally-occurring compounds, chemicals in groundwater systems, pollution resulting from man-made sources, such as MtBE, and possible terrorist attacks. In the event that our water supply is contaminated, we may have to interrupt the use of that water supply until we are

able to substitute the flow of water from an uncontaminated water source. In addition, we may incur significant costs in order to treat the contaminated source through expansion of our current treatment facilities, or development of new treatment methods. If we are unable to substitute water supply from an uncontaminated water source, or to adequately treat the contaminated water source in a cost-effective manner, there may be an adverse effect on our revenues, operating results and financial condition. The costs we incur to decontaminate a water source or an underground water system could be significant and could adversely affect our business, operating results and financial condition and may not be recoverable in rates. We could also be held liable for consequences arising out of human exposure to hazardous substances in our water supplies or other environmental damage. For example, private plaintiffs have the right to bring personal injury or other toxic tort claims arising from the presence of hazardous substances in our drinking water supplies. Our insurance policies may not be sufficient to cover the costs of these claims.

In addition to the potential pollution of our water supply as described above, in the wake of the September 11, 2001 terrorist attacks and the ensuing threats to the nation's health and security, we have taken steps to increase security measures at our facilities and heighten employee awareness of threats to our water supply. We have also tightened our security measures regarding the delivery and handling of certain chemicals used in our business. We have and will continue to bear increased costs for security precautions to protect our facilities, operations and supplies. These costs may be significant. We are currently not aware of any specific threats to our facilities, operations or supplies; however, it is possible that we would not be in a position to control the outcome of terrorist events should they occur.

WE DEPEND SIGNIFICANTLY ON THE SERVICES OF THE MEMBERS OF OUR MANAGEMENT TEAM, AND THE DEPARTURE OF ANY OF THOSE PERSONS COULD CAUSE OUR OPERATING RESULTS TO SUFFER.

Our success depends significantly on the continued individual and collective contributions of our management team. The loss of the services of any member of our management team or the inability to hire and retain experienced management personnel could harm our operating results.

Item 2. Properties.

Our properties consist of transmission and distribution mains and conduits, water and wastewater treatment plants, pumping facilities, wells, tanks, meters, supply lines, dams, reservoirs, buildings, vehicles, land, easements, rights and other facilities and equipment used for the operation of our systems, including the collection, treatment, storage and distribution of water and the collection and treatment of wastewater. Substantially all of our properties are owned by our subsidiaries and are subject to liens of mortgage or indentures. These liens secure bonds, notes and other evidences of long-term indebtedness of our subsidiaries. For certain properties that we acquired through the exercise of the power of eminent domain and certain other properties we purchased, we hold title for water supply purposes only. We own, operate and maintain several thousand miles of transmission and distribution mains, 21 water treatment plants, many well treatment stations, and 213 wastewater treatment plants. Some properties are leased under long-term leases. The following table indicates our net utility plant, in thousands of dollars, as of December 31, 2004 in the principal states where we operate:

	Net Property Plant and Equipment -----
Pennsylvania	\$1,225,914
Illinois	168,940
Ohio	166,439

Texas	148,836
North Carolina	121,326
New Jersey	104,273
Indiana	82,443
Florida	49,772
Maine	39,300
Virginia	29,107
Missouri	4,187
Inter-company eliminations and other states	(70,725)

	\$2,069,812
	=====

We believe that our properties are generally maintained in good condition and in accordance with current standards of good waterworks industry practice. We believe that the facilities used in the operation of our business are in good condition in terms of suitability, adequacy and utilization.

Our corporate offices are leased from Aqua Pennsylvania, Inc. and located in Bryn Mawr, Pennsylvania.

Item 3. Legal Proceedings

There are various legal proceedings in which we are involved. Although the results of legal proceedings cannot be predicted with certainty, there are no pending legal proceedings to which we or any of our subsidiaries is a party or to which any of our properties is the subject that are material or are expected to have a material effect on our financial position, results of operations or cash flows.

Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of security holders during the fourth quarter of 2004.

PART II

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

Our common stock is traded on the New York Stock Exchange and the Philadelphia Stock Exchange under the ticker symbol WTR. As of February 18, 2005, there were approximately 24,306 holders of record of our common stock.

The following table shows the high and low intraday sales prices for our common stock as reported on the New York Stock Exchange composite transactions reporting system and the cash dividends paid per share for the periods indicated (all per share data as presented has been adjusted for the 2003 5-for-4 common stock split effected in the form of a stock distribution):

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year

2004					

Dividend paid per common share	\$ 0.12	\$ 0.12	\$ 0.12	\$ 0.13	\$ 0.49
Dividend declared per common share	0.12	0.12	0.25	-	0.49
Price range of common stock					
- high	22.85	21.96	22.22	24.64	24.64
- low	20.00	18.98	18.90	20.77	18.90

2004					

Dividend paid per common share	\$0.112	\$ 0.112	\$0.112	\$0.120	\$0.456
Dividend declared per common share	0.112	0.112	0.232	-	0.456

Price range of common stock					
- high	17.83	19.85	20.07	22.40	22.40
- low	15.77	17.22	18.28	18.71	15.77

We have paid common dividends consecutively for 60 years. Effective December 1, 2004, our Board of Directors authorized an increase of 8.3% in the dividend rate over the amount Aqua America, Inc. paid in the previous quarter. As a result of this authorization, beginning with the dividend payment in December 2004, the annualized dividend rate increased to \$0.52 per share. We presently intend to pay quarterly cash dividends in the future, on March 1, June 1, September 1 and December 1, subject to our earnings and financial condition, regulatory requirements and such other factors as our Board of Directors may deem relevant. During the past five years, our common dividends paid have averaged 56.6% of net income.

In August 2003, our Board of Directors declared a 5-for-4 common stock split effected in the form of a 25% stock distribution for all common shares outstanding, to shareholders of record on November 14, 2003. The new shares were distributed on December 1, 2003. Aqua America's par value of \$0.50 per share remained unchanged and \$9,244,000 was transferred from Capital in Excess of Par Value to Common Stock to record the split. All share and per share data for all periods presented have been restated to give effect to the stock split.

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The following table summarizes the Company's purchases of its common stock for the quarter ending December 31, 2004:

Issuer Purchases of Equity Securities				
Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet be Purchased Under the Plan or Programs (2)
October 1-31, 2004	6,307	\$21.78	-	411,209
November 1-30, 2004	7,608	\$23.30	-	411,209
December 1-31, 2004	10,058	\$23.65	-	411,209
Total	23,973	\$23.04	-	411,209

Item 6. Selected Financial Data

The information appearing in the section captioned "Summary of Selected Financial Data" from the portions of our 2004 Annual Report to Shareholders filed as Exhibit 13.1 to this Form 10-K Report is incorporated by reference herein.

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

The information appearing in the section captioned "Management's Discussion and Analysis" from the portions of our 2004 Annual Report to Shareholders filed as Exhibit 13.1 to this Form 10-K Report is incorporated by reference herein.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

We are subject to market risks in the normal course of business, including changes in interest rates and equity prices. The exposure to changes in interest rates is a result of financings through the issuance of fixed-rate, long-term debt. Such exposure is typically related to financings between utility rate increases, since generally our rate increases include a revenue level to allow recovery of our current cost of capital. Interest rate risk is managed through the use of a combination of long-term debt, which is at fixed interest rates and short-term debt, which is at floating interest rates. As of December 31, 2004, the debt maturities by period, in thousands of dollars, and the weighted average interest rate for fixed-rate, long-term debt are as follows:

	2005	2006	2007	2008	2009	Thereafter	Total	Fair Value
Long-term debt (fixed rate)	\$50,195	\$24,623	\$31,068	\$23,756	\$6,816	\$698,198	\$834,656	\$863,247
Weighted average interest rate	7.19%	5.69%	5.10%	6.66%	4.89%	5.93%	6.00%	

From time to time, we make investments in marketable equity securities. As a result, we are exposed to the risk of changes in equity prices for the "available-for-sale" marketable equity securities. As of December 31, 2004, we owned no marketable equity securities as we sold the balance of our securities during 2004. The market risks that we are exposed to are less than the risks that we were exposed to in the prior year.

Item 8. Financial Statements and Supplementary Data

Information appearing under the captions "Consolidated Statements of Income and Comprehensive Income", "Consolidated Balance Sheets", "Consolidated Cash Flow Statements", "Consolidated Statements of Capitalization", "Consolidated Statements of Common Stockholders' Equity" and "Notes to Consolidated Financial Statements" from the portions of our 2004 Annual Report to Shareholders filed as Exhibit 13.1 to this Form 10-K Report is incorporated by reference herein. Also, the information appearing in the sections captioned "Management's Report on Internal Control Over Financial Reporting" and "Report of Independent Registered Public Accounting Firm" from the portions of our 2004 Annual Report to Shareholders filed as Exhibit 13.1 to this Form 10-K Report is incorporated by reference herein.

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

None.

Item 9A. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures - Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures as of the end of the period covered by this report are functioning effectively to provide reasonable assurance that the information required to be disclosed by us in reports filed under the Securities Exchange Act of 1934 is (i) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding disclosure. A controls system cannot provide absolute assurance, however, that

the objectives of the controls system are met, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

(b) Management's Report on Internal Control Over Financial Reporting - Our management's report on internal control over financial reporting is set forth in Item 8 of this annual report on Form 10-K and is incorporated by reference herein.

(c) Changes in Internal Control over Financial Reporting - No change in our internal control over financial reporting occurred during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

On December 9, 2004, the Board of Directors approved the following recommendations of the Executive Compensation and Employee Benefits Committee regarding compensation for Aqua America's Non-employee Directors:

Effective January 1, 2005, Non-Employee Director members of the Board of Directors will receive an annual retainer fee of \$12,500, payable quarterly, plus an annual grant of restricted stock with a value of \$25,000 to be issued on the first of the month following the Annual

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Meeting of Shareholders. The restricted stock vests six months after the date of grant. Non-Employee Directors also receive a fee of \$1,500 for attendance at each meeting of the Board of Directors and a meeting fee for attendance at each committee meeting of \$1,250 for the Audit Committee and \$1,000 for other committees. In addition, each committee Chairman who is a Non-Employee Director receives an annual retainer fee of \$5,000 for the Chairmen of the Audit Committee and Corporate Governance Committee and \$2,500 for the Chairmen of other committees.

All directors are reimbursed for reasonable expenses incurred in connection with attendance at Board or Committee meetings. Directors who are full-time employees of Aqua America do not receive a retainer or fees for service on the Board of Directors or committees of the Board. Directors are eligible to defer part or all of their fees under Aqua America's Director Deferral Plan. Amounts deferred accrue interest at the prime interest rate plus 1.0%. Amounts deferred are not funded.

PART III

Item 10. Directors and Executive Officers of the Registrant

We make available free of charge within the Investor Relations / Corporate Governance section of our Internet Web site, at www.aquaamerica.com, and in print to any shareholder who requests, our Corporate Governance Guidelines, the Charters of each Committee of our Board of Directors, and our Code of Ethical Business Conduct. Requests for copies may be directed to Investor Relations Department, Aqua America, Inc., 762 W. Lancaster Avenue, Bryn Mawr, PA 19010-3489. Amendments to the Code, and any grant of waiver from a provision of the Code requiring disclosure under applicable SEC rules will be disclosed on the Company's Web site. The information contained on our Internet website is not incorporated by reference into this Form 10-K and should not be considered part of this or any other report that we file with or furnish to the SEC.

Directors of the Registrant, Audit Committee Financial Expert and Filings under Section 16(c)

The information appearing in the sections captioned "Information Regarding Nominees and Directors", "Corporate Governance" and "Section 16(a) Beneficial Ownership Reporting Compliance" of the Proxy Statement relating to our May 19, 2005, annual meeting of shareholders, to be filed within 120 days

after the end of the fiscal year covered by this Form 10-K Report, is incorporated herein by reference.

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Executive Officers of the Registrant

The following table and the notes thereto set forth information with respect to our executive officers, including their names, ages, positions with Aqua America, Inc. and business experience during the last five years:

Name ----	Age ---	Position with Aqua America, Inc. (1) -----
Nicholas DeBenedictis	59	President and Chairman (May 1993 to present); President and Chief Executive Officer (July 1992 to May 1993); Chairman and Chief Executive Officer, Aqua Pennsylvania, Inc. (July 1992 to present); President, Philadelphia Suburban Water Company (February 1995 to January 1999) (2)
Roy H. Stahl	52	Executive Vice President and General Counsel (May 2000 to present); Secretary (June 2001 to present); Senior Vice President and General Counsel (April 1991 to May 2000) (3)
David P. Smeltzer	46	Senior Vice President - Finance and Chief Financial Officer (December 1999 to present); Vice President - Finance and Chief Financial Officer (May 1999 to December 1999); Vice President - Rates and Regulatory Relations, Philadelphia Suburban Water Company (March 1991 to May 1999) (4)
Richard R. Riegler	58	Senior Vice President - Engineering and Environmental Affairs (January 1999 to present); Senior Vice President - Operations, Philadelphia Suburban Water Company (April 1989 to January 1999) (5)
Richard D. Hugus	55	President, Southern Operations (August 2003 to present); Vice President - Corporate Development, Pennsylvania Suburban Water Company (March 1991 to August 2003) (6)
Karl M. Kyriss	54	President - Aqua Pennsylvania (March 2003 to present) (7)
Robert G. Liptak, Jr.	57	President, Northern Operations (March 1999 to present); President, Consumers Pennsylvania Water Company (1980 to March 1999) (8)
Robert A. Rubin	42	Controller and Chief Accounting Officer (March 2004 to present); Controller (March 1999 to March 2004) (9)

- (1) In addition to the capacities indicated, the individuals named in the above table hold other offices or directorships with subsidiaries of the Registrant. Officers serve at the discretion of the Board of Directors.
- (2) Mr. DeBenedictis was Secretary of the Pennsylvania Department of Environmental Resources from 1983 to 1986. From December 1986 to April 1989, he was President of the Greater Philadelphia Chamber of Commerce. Mr. DeBenedictis was Senior Vice President for Corporate and Public Affairs of Philadelphia Electric Company from April 1989 to June 1992.
- (3) From January 1984 to August 1985, Mr. Stahl was Corporate Counsel, from August 1985 to May 1988 he was Vice President - Administration and Corporate Counsel of Aqua America, Inc., and from May 1988 to April 1991 he was Vice President and General Counsel of Aqua America, Inc..
- (4) Mr. Smeltzer was Vice President - Controller of Philadelphia Suburban Water Company from March, 1986 to March 1991.
- (5) Mr. Riegler was Chief Engineer of Philadelphia Suburban Water Company from 1982 to 1984. He then served as Vice President and Chief Engineer from 1984 to 1986 and Vice President of Operations from 1986 to 1989.

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- (6) Mr. Hugus was Vice President and Treasurer of Philadelphia Suburban Water Company from December 1988 to March 1991.
- (7) Mr. Kyriss was Vice President - Northeast Region of American Water Works Services Company from 1997 to 2003.
- (8) Mr. Liptak was President of Consumers Pennsylvania Water Company

from 1980 to March 1999.

- (9) Mr. Rubin was Accounting Manager with Aqua America, Inc. from June 1989 to June 1994. He then served from June 1994 to March 1999 as Assistant Controller of Philadelphia Suburban Water Company.

Item 11. Executive Compensation

The information appearing in the sections captioned "Executive Compensation" of the Proxy Statement relating to our May 19, 2005, annual meeting of shareholders, to be filed within 120 days after the end of the fiscal year covered by this Form 10-K Report, is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and related Stockholder matters

Ownership of Common Stock - The information appearing in the section captioned "Ownership of Common Stock" of the Proxy Statement relating to our May 19, 2005, annual meeting of shareholders, to be filed within 120 days after the end of the fiscal year covered by this Form 10-K Report, is incorporated herein by reference.

Securities Authorized for Issuance under Equity Compensation Plans - The following table provides information for our equity compensation plan as of December 31, 2004:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities) reflected in column (a)
Equity compensation plans approved by security holders	3,050,237	\$14.96	3,678,584
Equity compensation plans not approved by security holders	0	0	0
Total	3,050,237	\$14.96	3,678,584

Item 13. Certain Relationships and Related Transactions

The information appearing in the sections captioned "Certain Relationships and Related Transactions" of the Proxy Statement relating to our May 19, 2005, annual meeting of shareholders, to be filed within 120 days after the end of the fiscal year covered by this Form 10-K Report, is incorporated herein by reference.

Item 14. Principal Accountant Fees and Services

The information appearing in the section captioned "Independent Registered Public Accounting Firm - Services and Fees" of the Proxy Statement relating to our May 19, 2005, annual meeting of shareholders, to be filed within 120 days after the end of the fiscal year covered by this Form 10-K Report, is incorporated herein by reference.

PART IV

Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K

Financial Statements. The following is a list of our consolidated financial statements and supplementary data incorporated by reference in Item 8 hereof:

Management's Report on Internal Control Over Financial Reporting
Report of Independent Registered Public Accounting Firm
Consolidated Balance Sheets - December 31, 2004 and 2003
Consolidated Statements of Income and Comprehensive Income - 2004, 2003 and 2002
Consolidated Cash Flow Statements - 2004, 2003 and 2002
Consolidated Statements of Capitalization - December 31, 2004 and 2003
Consolidated Statements of Common Stockholders' Equity - December 31, 2004, 2003 and 2002
Notes to Consolidated Financial Statements

Financial Statement Schedules. The financial statement schedules, or supplemental schedules, filed as part of this annual report on Form 10-K are omitted because they are not applicable or not required, or because the required information is included in the consolidated financial statements or notes thereto.

Exhibits, Including Those Incorporated by Reference. The following is a list of exhibits filed as part of this annual report on Form 10-K. Where so indicated by footnote, exhibits which were previously filed are incorporated by reference. For exhibits incorporated by reference, the location of the exhibit in the previous filing is indicated in parentheses.

EXHIBIT INDEX

Exhibit No.

3.1	Restated Articles of Incorporation (as of December 9, 2004) (20) (Exhibit 3.1)
3.2	By-Laws, as amended (9) (Exhibit 3.2)
3.3	Amendment to Section 3.03 and addition of Section 3.17 to Bylaws (11) (Exhibits 1 and 2)
3.4	Amendment to Section 3.03 of the Bylaws (13) (Exhibit 3.8)
3.5	Amendments to Sections 2.01(a), 2.02 and 3.08(b) of the Bylaws (14) (Exhibit 3.10)
4.1	Indenture of Mortgage dated as of January 1, 1941 between Philadelphia Suburban Water Company and The Pennsylvania Company for Insurance on Lives and Granting Annuities (now First Pennsylvania Bank, N.A.), as Trustee, with supplements thereto through the Twentieth Supplemental Indenture dated as of August 1, 1983 (2) (Exhibits 4.1 through 4.16)
4.2	Agreement to furnish copies of other long-term debt instruments (1) (Exhibit 4.7)
4.3	Twenty-fourth Supplemental Indenture dated as of June 1, 1988 (3) (Exhibit 4.5)
4.4	Twenty-fifth Supplemental Indenture dated as of January 1, 1990 (4) (Exhibit 4.6)
4.5	Twenty-sixth Supplemental Indenture dated as of November 1, 1991 (5) (Exhibit 4.12)
4.6	Twenty-eighth Supplemental Indenture dated as of April 1, 1993 (6) (Exhibit 4.15)

- 4.7 Twenty-ninth Supplemental Indenture dated as of March 30, 1995 (7) (Exhibit 4.17)
- 4.8 Thirtieth Supplemental Indenture dated as of August 15, 1995 (8) (Exhibit 4.18)
- 4.9 Thirty-first Supplemental Indenture dated as of July 1, 1997 (10) (Exhibit 4.22)
- 4.10 First Amended and Restated Rights Agreement, dated as of February 20, 2004 between Aqua America, Inc. and Equiserve Trust Company, N.A., as Rights Agent. (22) (Exhibit 4.10)
- 4.11 Thirty-second Supplement Indenture, dated as of October 1, 1999 (12) (Exhibit 4.26)
- 4.12 Thirty-third Supplemental Indenture, dated as of November 15, 1999.(13) (Exhibit 4.27)
- 4.13 Revolving Credit Agreement between Philadelphia Suburban Water Company and PNC Bank National Association, First Union National Bank, N.A., Mellon Bank, N.A. dated as of December 22, 1999 (13) (Exhibit 4.27)
- 4.14 First Amendment to Revolving Credit Agreement dated as of November 28, 2000, between Philadelphia Suburban Water Company and PNC Bank, National Association, First Union National Bank, N.A., Mellon Bank, N.A. dated as of December 22, 1999 (14) (Exhibit 4.19)
- 4.15 Second Amendment to Revolving Credit Agreement dated as of December 18, 2001, between Philadelphia Suburban Water Company (and its successor Pennsylvania Suburban Water Company) and PNC Bank, National Association, Citizens Bank of Pennsylvania, First Union National Bank, N.A., Fleet National Bank dated as of December 22, 1999 (15) (4.20)

EXHIBIT INDEX

Exhibit No.

- 4.16 Thirty-fourth Supplemental Indenture, dated as of October 15, 2001. (15) (4.21)
- 4.17 Thirty-fifth Supplemental Indenture, dated as of January 1, 2002. (15) (4.22)
- 4.18 Thirty-sixth Supplemental Indenture, dated as of June 1, 2002. (17) (4.23)
- 4.19 Thirty-seventh Supplemental Indenture, dated as of December 15, 2002. (18) (4.23)
- 4.20 Credit Agreement dated as of October 25, 2002, between Philadelphia Suburban Corporation and PNC Bank, National Association. (18) (4.24)
- 4.21 Third Amendment to Revolving Credit Agreement dated as of December 16, 2002, between Philadelphia Suburban Water Company (and its successor Pennsylvania Suburban Water Company) and PNC Bank, National Association, Citizens Bank of Pennsylvania, Fleet National Bank dated as of December 22, 1999. (18) (4.25)
- 4.22 Fourth Amendment to Revolving Credit Agreement dated as of December 24, 2002, between Philadelphia Suburban Water Company (and its successor Pennsylvania Suburban Water Company) and PNC Bank, National Association, Citizens Bank of Pennsylvania, Fleet National Bank, National City Bank dated as of December 22, 1999. (18) (4.26)
- 4.23 Note Purchase Agreement among the note purchasers and Philadelphia Suburban Corporation, dated July 31, 2003 (19) (4.27)
- 4.24 Credit Agreement dated as of July 31, 2003, between Philadelphia Suburban Corporation and PNC Bank, National Association (19) (4.28)
- 4.25 Fifth Amendment to Revolving Credit Agreement dated as of December 14, 2003, between Philadelphia Suburban Water Company (and its successor Pennsylvania Suburban Water Company) and PNC Bank, National Association, Citizens Bank of Pennsylvania, Fleet National Bank, National City Bank dated as of December 22, 1999. (22) (Exhibit 4.25)
- 4.26 Credit Agreement dated as of May 28, 2004, between Aqua America, Inc. and PNC Bank, National Association (21) (4.26)
- 4.27 Sixth Amendment to Revolving Credit Agreement dated as of December 12, 2004 between Aqua Pennsylvania, Inc. (formerly known as Pennsylvania Suburban Water Company, successor by merger to Philadelphia Suburban Water Company) and PNC Bank, National Association, Citizens Bank of Pennsylvania, Fleet National Bank, National City Bank dated as of December 22, 1999.
- 4.28 Thirty-eighth Supplemental Indenture, dated as of November 15, 2004.

- 10.1 Excess Benefit Plan for Salaried Employees, effective December 1, 1989* (4) (Exhibit 10.4)
- 10.2 Supplemental Executive Retirement Plan, effective December 1, 1989* (4) (Exhibit 10.5)
- 10.3 Supplemental Executive Retirement Plan, effective March 15, 1992* (1) (Exhibit 10.6)
- 10.4 Employment letter agreement with Mr. Nicholas DeBenedictis* (1) (Exhibit 10.8)
- 10.5 1994 Equity Compensation Plan, as amended by Amendment effective August 5, 2003* (22) (Exhibit 10.5)
- 10.6 Placement Agency Agreement between Philadelphia Suburban Water Company and PaineWebber Incorporated dated as of March 30, 1995 (7) (Exhibit 10.12)

EXHIBIT INDEX

Exhibit No.

- 10.7 Bond Purchase Agreement among the Delaware County Industrial Development Authority, Philadelphia Suburban Water Company and Legg Mason Wood Walker, Incorporated dated August 24, 1995 (8) (Exhibit 10.13)
- 10.8 Construction and Financing Agreement between the Delaware County Industrial Development Authority and Philadelphia Suburban Water Company dated as of August 15, 1995 (8) (Exhibit 10.14)
- 10.9 Philadelphia Suburban Corporation Amended and Restated Executive Deferral Plan* (22) (Exhibit 10.9)
- 10.10 Philadelphia Suburban Corporation Deferred Compensation Plan Master Trust Agreement with PNC Bank, National Association, dated as of December 31, 1996* (9) (Exhibit 10.24)
- 10.11 First Amendment to Supplemental Executive Retirement Plan* (9) (Exhibit 10.25)
- 10.12 Placement Agency Agreement between Philadelphia Suburban Water Company and A.G. Edwards and Sons, Inc., Janney Montgomery Scott Inc., HSBC Securities, Inc., and PaineWebber Incorporated (10) (Exhibit 10.26)
- 10.13 The Director Deferral Plan* (22) (Exhibit 10.13)
- 10.14 Bond Purchase Agreement among the Delaware County Industrial Development Authority, Philadelphia Suburban Water Company and Commerce Capital Markets dated September 29, 1999 (12) (Exhibit 10.37)
- 10.15 Construction and Financing Agreement between the Delaware County Industrial Development Authority and Philadelphia Suburban Water Company dated as of October 1, 1999 (12) (Exhibit 10.38)
- 10.16 Placement Agency Agreement between Philadelphia Suburban Water Company and Merrill Lynch & Co., PaineWebber Incorporated, A.G. Edwards & Sons, Inc., First Union Securities, Inc., PNC Capital Markets, Inc. and Janney Montgomery Scott, Inc., dated as of November 15, 1999 (13) (Exhibit 10.41)
- 10.17 Bond Purchase Agreement among the Delaware County Industrial Development Authority, Philadelphia Suburban Water Company and The GMS Group, L.L.C., dated October 23, 2001 (15) (10.35)
- 10.18 Construction and Financing Agreement between the Delaware County Industrial Development Authority and Philadelphia Suburban Water Company dated as of October 15, 2001 (15) (10.36)
- 10.19 Agreement among Philadelphia Suburban Corporation, Philadelphia Suburban Water Company and Nicholas DeBenedictis, dated August 7, 2001* (15) (10.37)
- 10.20 Agreement among Philadelphia Suburban Corporation, Philadelphia Suburban Water Company and Roy H. Stahl, dated August 7, 2001* (15) (10.38)
- 10.21 Agreement among Philadelphia Suburban Corporation, Philadelphia Suburban Water Company and Richard R. Riegler, dated August 7, 2001* (15) (10.39)

EXHIBIT INDEX

Exhibit No.

10.22	Agreement among Philadelphia Suburban Corporation, Philadelphia Suburban Water Company and David P. Smeltzer, dated August 7, 2001* (15) (10.40)
10.23	Agreement among Philadelphia Suburban Corporation, Philadelphia Suburban Water Company and Richard D. Hugus, dated August 7, 2001* (22) (Exhibit 10.23)
10.24	2003 Annual Cash Incentive Compensation Plan* (18) (Exhibit 10.46)
10.25	Bond Purchase Agreement among the Bucks County Industrial Development Authority, Pennsylvania Suburban Water Company and Janney Montgomery Scott LLC, dated May 21, 2002 (17) (Exhibit 10.42)
10.26	Construction and Financing Agreement between the Bucks County Industrial Development Authority and Pennsylvania Suburban Water Company dated as of June 1, 2002 (17) (Exhibit 10.43)
10.27	Bond Purchase Agreement among the Delaware County Industrial Development Authority, Pennsylvania Suburban Water Company, and The GMS Group, L.L.C., dated December 19, 2002 (18) (Exhibit 10.44)
10.28	Construction and Financing Agreement between the Delaware County Industrial Development Authority and Pennsylvania Suburban Water Company dated as of December 15, 2002 (18) (Exhibit 10.45)
10.29	2005 Annual Cash Incentive Compensation Plan*
10.30	2004 Annual Cash Incentive Compensation Plan* (22) (Exhibit 10.30)
10.31	Bond Purchase Agreement among the Northumberland County Industrial Development Authority, Aqua Pennsylvania, Inc., and Sovereign Securities Corporation, LLC, dated November 16, 2004.
10.32	Aqua America, Inc. 2004 Equity Compensation Plan* (23)
10.33	2005 Executive Deferral Plan*
10.34	2005 Director Deferral Plan*
10.35	Directors' Compensation*
13.1	Selected portions of Annual Report to Shareholders for the year ended December 31, 2004 incorporated by reference in Annual Report on Form 10-K for the year ended December 31, 2004
21.	Subsidiaries of Aqua America, Inc.
23.1	Consent of Independent Registered Public Accounting Firm - PricewaterhouseCoopers LLP
24.	Power of Attorney (set forth as a part of this report)
31.1	Certification of Chief Executive Officer, pursuant to Rule 13a-14(a) under the Securities and Exchange Act of 1934
31.2	Certification of Chief Financial Officer, pursuant to Rule 13a-14(a) under the Securities and Exchange Act of 1934
32.1	Certification of Chief Executive Officer, pursuant to 18 U.S.C. Section 1350
32.2	Certification of Chief Financial Officer, pursuant to 18 U.S.C. Section 1350

- (1) Filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 1992.
- (2) Indenture of Mortgage dated as of January 1, 1941 with supplements thereto through the Twentieth Supplemental Indenture dated as of August 1, 1983 were filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 1983.
- (3) Filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 1988.
- (4) Filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 1989.
- (5) Filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 1991.
- (6) Filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 1993.
- (7) Filed as an Exhibit to Quarterly Report on Form 10-Q for the quarter ended March 31, 1995.
- (8) Filed as an Exhibit to Quarterly Report on Form 10-Q for the quarter ended September 30, 1995.
- (9) Filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 1996.
- (10) Filed as an Exhibit to Quarterly Report on Form 10-Q for the quarter ended June 30, 1997.
- (11) Filed as an Exhibit to Form 8-K filed August 7, 1997.
- (12) Filed as an Exhibit to Quarterly Report on Form 10-Q for the quarter ended September 30, 1999.
- (13) Filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 1999.
- (14) Filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 2000.
- (15) Filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 2001.
- (16) Filed as an Exhibit to Quarterly Report on Form 10-Q for the quarter ended March 31, 2002.
- (17) Filed as an Exhibit to Quarterly Report on Form 10-Q for the quarter ended June 30, 2002.
- (18) Filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 2002.
- (19) Filed as an Exhibit to Quarterly Report on Form 10-Q for the quarter ended September 30, 2003.
- (20) Filed as an Exhibit to Form 8-K filed December 9, 2004.
- (21) Filed as an Exhibit to Quarterly Report on Form 10-Q for the quarter ended June 30, 2004.
- (22) Filed as an Exhibit to Annual Report on Form 10-K for the year ended December 31, 2003.

- (23) Filed as Appendix C to definitive Proxy Statement dated April 2, 2004.

*Indicates management contract or compensatory plan or arrangement.

SIGNATURES

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

AQUA AMERICA, INC.

By NICHOLAS DEBENEDICTIS

 Nicholas DeBenedictis
 President and Chairman

Date: March 14, 2005

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

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NICHOLAS DEBENEDICTIS

Nicholas DeBenedictis
President and Chairman
(principal executive officer)
and Director

DAVID P. SMELTZER

David P. Smeltzer
Senior Vice President - Finance and
Chief Financial Officer

ROBERT A. RUBIN

Robert A. Rubin
Principal Accounting Officer

MARY C. CARROLL

Mary C. Carroll
Director

RICHARD H. GLANTON

Richard H. Glanton
Director

WILLIAM P. HANKOWSKY

William P. Hankowsky
Director

JOHN F. MCCAUGHAN

John F. McCaughan
Director

JOHN E. MENARIO

John E. Menario
Director

RICHARD L. SMOOT

Richard L. Smoot
Director

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SIXTH AMENDMENT TO CREDIT AGREEMENT

THIS SIXTH AMENDMENT TO CREDIT AGREEMENT is made as of this 12th day of December, 2004, by and among AQUA PENNSYLVANIA, INC., a Pennsylvania corporation (formerly known as Pennsylvania Suburban Water Company, successor by merger to Philadelphia Suburban Water Company) ("Borrower"), the several banks which are parties to this Agreement (each a "Bank" and collectively, "Banks") and PNC BANK, NATIONAL ASSOCIATION in its capacity as agent for Banks (in such capacity, "Agent").

BACKGROUND

A. Borrower, Agent and Banks are parties to a Credit Agreement, dated as of December 22, 1999, as amended by a First Amendment to Credit Agreement dated as of November 28, 2000, a Second Amendment to Credit Agreement dated as of December 18, 2001, a Third Amendment to Credit Agreement dated as of December 16, 2002, a Fourth Amendment dated as of December 24, 2002 and a Fifth Amendment to Credit Agreement dated as of December 14, 2003 (as so amended, the "Credit Agreement"), pursuant to which Banks agreed to make revolving credit loans to Borrower in an aggregate outstanding amount of up to \$70,000,000 (the "Loans"). The Loans are evidenced by Borrower's Revolving Credit Notes in the aggregate principal face amount of \$70,000,000.

B. Borrower, Agent and Banks desire to extend the Termination Date of the facility, all on the terms and subject to the conditions herein set forth.

NOW THEREFORE, the parties hereto, intending to be legally bound hereby, agree as follows:

AGREEMENT

1. Terms. Capitalized terms used herein and not otherwise defined herein shall have the meanings given to such terms in the Credit Agreement.

2. Amendments to Credit Agreement. Effective on December 12, 2004 (the "Effective Date") the Credit Agreement is hereby amended as follows:

(a) The definition of Termination Date in Section 1.1 is hereby amended and restated to read in full as follows:

"Termination Date": the earlier of (a) December 10, 2005 or any later date to which the Termination Date shall have been extended pursuant to subsection 2.8(d) hereof and (b) the date the Commitments are terminated as provided herein."

3. Loan Documents. Except where the context clearly requires otherwise, all references to the Credit Agreement in any of the Loan Documents or any other document

delivered to Banks or Agent in connection therewith shall be to the Credit Agreement as amended by this Agreement.

4. Borrower's Ratification. Borrower agrees that it has no defenses or set-offs against Banks or Agent or their respective officers, directors, employees, agents or attorneys, with respect to the Loan Documents, all of which are in full force and effect, and that all of the terms and conditions of the Loan Documents not inconsistent herewith shall remain in full force and effect unless and until modified or amended in writing in accordance with their terms. Borrower hereby ratifies and confirms its obligations under the Loan Documents as amended hereby and agrees that the execution and delivery of this Agreement does not in any way diminish or invalidate any of its obligations thereunder.

5. Representations and Warranties. Borrower hereby represents and warrants to Agent and Banks that:

(a) Except as otherwise previously disclosed to Agent and Banks, the representations and warranties made in the Credit Agreement, as amended by this Agreement, are true and correct as of the date hereof;

(b) No Default or Event of Default under the Credit Agreement exists on the date hereof; and

(c) This Agreement has been duly authorized, executed and delivered so as to constitute the legal, valid and binding obligations of Borrower, enforceable in accordance with its terms.

All of the above representations and warranties shall survive the making of this Agreement.

6. Conditions Precedent. The effectiveness of the amendments set forth herein is subject to the fulfillment, to the satisfaction of Agent and its counsel, of the following conditions precedent on or before the Effective Date:

(a) Borrower shall have delivered to Agent, with copies or counterparts for each Bank as appropriate, the following, all of which shall be in form and substance satisfactory to Agent and shall be duly completed and executed:

(i) This Agreement;

(ii) Copies, certified by the Secretary or an Assistant Secretary of Borrower as of a recent date, of resolutions of the board of directors of Borrower in effect on the date hereof authorizing the execution, delivery and performance of this Agreement and the other documents and transactions contemplated hereby;

(iii) Copies, certified by its corporate secretary as of a recent date, of the articles of incorporation, certificate of formation, and by-laws of Borrower as in effect, or a certificate stating that there have

been no changes to any such documents since the most recent date, true and correct copies thereof were delivered to Agent; and

(iv) Such additional documents, certificates and information as Agent or Banks may require pursuant to the terms hereof or otherwise reasonably request.

(b) The representations and warranties set forth in the Credit Agreement shall be true and correct on and as of the date hereof.

(c) No Default or Event of Default shall have occurred and be continuing as of the date hereof.

(d) Borrower shall have paid to Agent for the benefit of Banks an extension fee of \$84,000 to be distributed pro rata to Banks.

7. Miscellaneous.

(a) All terms, conditions, provisions and covenants in the Loan Documents and all other documents delivered to Agent and Banks in connection therewith shall remain unaltered and in full force and effect except as modified or amended hereby. To the extent that any term or provision of this Agreement is or may be deemed expressly inconsistent with any term or provision in any Loan Document or any other document executed in connection therewith, the terms and provisions hereof shall control.

(b) The execution, delivery and effectiveness of this Agreement shall neither operate as a waiver of any right, power or remedy of Agent or Banks under any of the Loan Documents nor constitute a waiver of any Default or Event of Default or default thereunder.

(c) In consideration of Agent's and Banks' agreement to amend the existing credit facility, Borrower hereby waives and releases Agent and Banks and their respective officers, attorneys, agents and employees from any liability, suit, damage, claim, loss or expense of any kind or failure whatsoever and howsoever arising that it ever had up until, or has as of, the date of this Agreement.

(d) This Agreement constitutes the entire agreement of the

parties with respect to the subject matter hereof and supersedes all prior and contemporaneous understandings and agreements.

(e) In the event any provisions of this Agreement shall be held invalid or unenforceable by any court of competent jurisdiction, such holding shall not invalidate or render unenforceable any other provision hereof.

(f) This Agreement shall be governed by and construed according to the laws of the Commonwealth of Pennsylvania.

(g) This Agreement shall inure to the benefit of, and be binding upon, the parties hereto and their respective successors and assigns and may be executed in one or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

(h) The headings used in this Agreement are for convenience of reference only, do not form a part of this Agreement and shall not affect in any way the meaning or interpretation of this Agreement.

IN WITNESS WHEREOF, Borrower, Agent and Banks have caused this Agreement to be executed by their duly authorized officers as of the date first above written.

AQUA PENNSYLVANIA, INC.

By: KATHY L. PAPE

Title: Vice President and Treasurer

PNC BANK, NATIONAL ASSOCIATION, as a
Bank and as Agent

By: FORREST B. PATTERSON, JR.

Title: SVP

CITIZENS BANK OF PENNSYLVANIA

By: MARK W. TORIE

Title: SVP

FLEET NATIONAL BANK

By: HENRY F. BULLITT

Title: Senior Vice President

NATIONAL CITY BANK

By: DAVID P. DOBSTAFF

Title: Senior Vice President

THIRTY-EIGHTH SUPPLEMENTAL
INDENTURE
DATED AS OF NOVEMBER 15, 2004
TO
INDENTURE OF MORTGAGE
DATED AS OF JANUARY 1, 1941

AQUA PENNSYLVANIA, INC.

TO
J.P. MORGAN TRUST COMPANY, NATIONAL ASSOCIATION

THIRTY-EIGHTH SUPPLEMENTAL INDENTURE dated as of November 15, 2004, by and between AQUA PENNSYLVANIA, INC. (f/k/a/ Pennsylvania Suburban Water Company), a corporation duly organized and existing under the laws of the Commonwealth of Pennsylvania (the "Company") as successor by merger to the Philadelphia Suburban Water Company (the "Original Company"), party of the first part, and J.P. MORGAN TRUST COMPANY, NATIONAL ASSOCIATION, a national banking association (the "Trustee"), party of the second part.

WHEREAS, the Original Company heretofore duly executed and delivered to The Pennsylvania Company for Insurances on Lives and Granting Annuities, as trustee, an Indenture of Mortgage dated as of January 1, 1941 (the "Original Indenture"), which by reference is hereby made a part hereof, and in and by the Original Indenture the Original Company conveyed and mortgaged to such trustee certain property therein described, to secure the payment of its bonds to be generally known as its "First Mortgage Bonds" and to be issued under the Original Indenture in one or more series as therein provided; and

WHEREAS, through a series of mergers, changes of names and successions, J.P. Morgan Trust Company, National Association, became the successor trustee; such mergers, changes of name and successions not involving any change in the title, powers, rights or duties of the trustee, as trustee under the Original Indenture as supplemented at the respective dates thereof; and

WHEREAS, the Original Company duly executed and delivered to the Trustee thirty-seven supplemental indentures supplemental to the Original Indenture, and the Company duly executed and delivered to the Trustee a Thirty-Fifth Supplemental Indenture dated as of January 1, 2002 (the "Thirty-Fifth Supplemental Indenture"), a Thirty-Sixth Supplemental Indenture dated as of June 1, 2002 (the "Thirty-Sixth Supplemental Indenture") and a Thirty-Seventh Supplemental Indenture dated as of December 15, 2002 (the "Thirty-Seventh Supplemental Indenture") so as to subject certain additional property to the lien of the Original Indenture and to provide for the creation of additional series of bonds; and

WHEREAS, pursuant to an Agreement and Plan of Merger and Reorganization dated December 20, 2001, and effective on January 1, 2002, the Original Company agreed to merge, in conjunction with its affiliated corporations, Consumers Pennsylvania Water Company - Shenango Valley Division, Consumers Pennsylvania Water Company - Roaring Creek Division, Consumers Pennsylvania Water Company - Susquehanna Division, Waymart Water Company, Fawn Lake Forrest Water Company, Western Utilities, Inc., and Northeastern Utilities, Inc. (such affiliates referred to hereinafter as the "Merging Entities") with and into the Company; and

WHEREAS, pursuant to the Thirty-Fifth Supplemental Indenture, the Company agreed to assume the obligations of the Original Company under the

Original Indenture and all supplements thereto; and

WHEREAS, the Original Company has issued under the Original Indenture, as supplemented at the respective dates of issue, forty-three series of First Mortgage Bonds

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designated, respectively, as set forth in the following table, the Original or Supplemental Indenture creating each series and the principal amount of bonds thereof issued being indicated opposite the designation of such series:

DESIGNATION	INDENTURE	AMOUNT
3 1/4% Series due 1971	Original	\$ 16,375,000
9 5/8% Series due 1975	Thirteenth Supplemental	10,000,000
9.15% Series due 1977	Fourteenth Supplemental	10,000,000
3% Series due 1978	First Supplemental	2,000,000
3 3/8% Series due 1982	Second Supplemental	4,000,000
3.90% Series due 1983	Third Supplemental	5,000,000
3 1/2% Series due 1986	Fourth Supplemental	6,000,000
4 1/2% Series due 1987	Fifth Supplemental	4,000,000
4 1/8% Series due 1988	Sixth Supplemental	4,000,000
5% Series due 1989	Seventh Supplemental	4,000,000
4 5/8% Series due 1991	Eighth Supplemental	3,000,000
4.70% Series due 1992	Ninth Supplemental	3,000,000
6 7/8% Series due 1993	Twelfth Supplemental	4,500,000
4.55% Series due 1994	Tenth Supplemental	4,000,000
10 1/8% Series due 1995	Sixteenth Supplemental	10,000,000
5 1/2% Series due 1996	Eleventh Supplemental	4,000,000
7 7/8% Series due 1997	Fifteenth Supplemental	5,000,000
8.44% Series due 1997	Twenty-Third Supplemental	12,000,000
9.20% Series due 2001	Seventeenth Supplemental	7,000,000
8.40% Series due 2002	Eighteenth Supplemental	10,000,000
5.95% Series due 2002	Twenty-Seventh Supplemental	4,000,000
12.45% Series due 2003	Twentieth Supplemental	10,000,000
13% Series due 2005	Twenty-First Supplemental	8,000,000
10.65% Series due 2006	Twenty-Second Supplemental	10,000,000
9.89% Series due 2008	Twenty-Fourth Supplemental	5,000,000
7.15% Series due 2008	Twenty-Eighth Supplemental	22,000,000
9.12% Series due 2010	Twenty-Fifth Supplemental	20,000,000
8 7/8% Series due 2010	Nineteenth Supplemental	8,000,000
6.50% Series due 2010	Twenty-Seventh Supplemental	3,200,000
9.17% Series due 2011	Twenty-Sixth Supplemental	5,000,000
9.93% Series due 2013	Twenty-Fourth Supplemental	5,000,000
9.97% Series due 2018	Twenty-Fourth Supplemental	5,000,000
9.17% Series due 2021	Twenty-Sixth Supplemental	8,000,000
9.29% Series due 2026	Twenty-Sixth Supplemental	12,000,000
1995 Medium Term Note Series	Twenty-Ninth Supplemental	77,000,000
6.35% Series due 2025	Thirtieth Supplemental	22,000,000

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1997 Medium Term Note Series	Thirty-First Supplemental	65,000,000
6.75% Subseries A due 2007	10,000,000	
6.30% Subseries B due 2002	10,000,000	
6.14% Subseries C due 2008	10,000,000	
5.80% Subseries D due 2003	10,000,000	
5.85% Subseries E due 2004	10,000,000	
6.00% Subseries F due 2004	15,000,000	
6.00% Series due 2029	Thirty-Second Supplemental	25,000,000
1999 Medium Term Note Series	Thirty-Third Supplemental	222,333,480
7.40% Subseries A due 2005	15,000,000	
7.40% Subseries B due 2005	11,000,000	
6.21% Subseries C due 2011	15,000,000	
9.53% Subseries D due 2019	4,000,000	
6.375% Subseries E due 2023	14,000,000	
8.26% Subseries F due 2022	1,500,000	
9.50% Subseries G due 2006	1,440,000	
9.22% Subseries H due 2019	2,534,480	
8.32% Subseries I due 2022	3,500,000	
8.14% Subseries J due 2025	4,000,000	
6.00% Subseries K due 2030	18,360,000	

5.93% Subseries L due 2012	25,000,000	
2.65% Subseries M due 2006	5,000,000	
3.461% Subseries N due 2007	12,000,000	
5.08% Subseries O due 2015	20,000,000	
5.17% Subseries P due 2017	7,000,000	
5.751% Subseries Q due 2019	15,000,000	
5.751% Subseries R due 2019	15,000,000	
6.06% Subseries S due 2027	15,000,000	
6.06% Subseries T due 2027	5,000,000	
5.98% Subseries U due 2028	3,000,000	
5.35% Series due 2031	Thirty-Fourth Supplemental	30,000,000
5.55% Series due 2032	Thirty-Sixth Supplemental	25,000,000
3.75% Series due 2010	Thirty-Seventh Supplemental	3,200,000
5.15% Series due 2032	Thirty Seventh Supplemental	25,000,000

WHEREAS, the bonds of each of said series that are presently outstanding are listed on Exhibit A attached hereto and made a part hereof; and

WHEREAS, the Original Indenture and the first thirty-seven supplemental indentures supplemental to the Original Indenture were duly recorded in the Commonwealth of Pennsylvania on the dates and in the office for the Recording of Deeds for the counties and in the Mortgage Books at the pages indicated in Exhibit B hereto; and

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WHEREAS, in order to secure the Lien of the Original Indenture on the properties of the Merging Entities, the Thirty-Fifth Supplemental Indenture, with a true and correct copy of the Original Indenture attached thereto (redacted to delete property descriptions for counties in which such Original Indenture had already been recorded), the Thirty-Sixth Supplemental Indenture and the Thirty-Seventh Supplemental Indenture were also recorded in the Commonwealth of Pennsylvania on the dates and in the office for the Recording of Deeds for the counties and in the Mortgage Books at the pages indicated on Exhibit B hereto;

WHEREAS, in addition to the property described in the Original Indenture and the First through Thirty-Seventh Supplemental Indentures thereto, the Company has acquired certain other property and desires to confirm the lien of the Original Indenture thereon and in order to confirm such lien shall cause this Thirty-Eighth Supplemental Indenture, with a true and correct copy of the Original Indenture attached hereto as Exhibit D (redacted to delete property descriptions for counties in which such Original Indenture has already been recorded) to be recorded in the offices for the Recording of Deeds for the counties of Adams, Carbon, Cumberland, Forest, Juniata, Lackawanna, Luzerne, Monroe, Northampton, Snyder, Susquehanna, Wayne and Wyoming; and

WHEREAS, the lien of the Original Indenture, as supplemented, has been perfected as a security interest under the Pennsylvania Uniform Commercial Code by filing a financing statement in the office of the Secretary of the Commonwealth; and

WHEREAS, the Company proposes to create under the Original Indenture, as supplemented by this Thirty-Eighth Supplemental Indenture, a new series of bonds to be designated "First Mortgage Bonds, 5.05% Series due 2039" (herein referred to as the "5.05% Series due 2039" to be limited in aggregate principal amount to \$14,000,000, to bear interest at the rate of 5.05% per annum, and to mature on October 1, 2039, to be issued only as registered bonds without coupons and to be dated the date of delivery thereof; and

WHEREAS, the Northumberland County Industrial Development Authority (the "Authority") previously issued its Exempt Facilities Revenue Bonds, Series 1993 (Roaring Creek Water Company Project) (the "Prior Bonds") in the aggregate principal amount of \$14,000,000, all of which are currently outstanding, to finance the construction of an 8 million gallon per day treatment facility, an interconnecting water main, and laboratory and service facilities, located in Northumberland and Columbia Counties (the "Facilities") on behalf of Roaring Creek Water Company, one of the Merging Entities ("Roaring Creek Company");

WHEREAS, Roaring Creek Company previously issued its 6.375% Secured Notes due October 15, 2023 (the "6.375% Secured Notes") to secure the obligations of Roaring Creek Company to pay the costs of the Facilities; and

WHEREAS, pursuant to the Thirty-Third Supplemental Indenture and in

connection with the execution and delivery of the Thirty-fifth Supplemental Indenture and an Exchange Agreement dated as of December 15, 2001, the Company issued its First Mortgage Bonds, 1999 Medium Term Note Series, Subseries E in the aggregate principal amount of \$14,000,000 (the "Subseries E Bond") in exchange for the 6.375% Secured Notes;

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WHEREAS, in order to finance the refunding of the Prior Bonds, the Company has requested the Authority to issue a new series of bonds to be known as the Authority's Water Facilities Revenue Refunding Bonds (Aqua Pennsylvania, Inc. Project), Series of 2004 in the aggregate principal amount of \$14,000,000 (the "Authority Bonds"); and

WHEREAS, in connection with the refunding of the Prior Bonds, the Subseries E Bond will be cancelled; and

WHEREAS, the Company proposes to issue the 5.05% Series due 2039 under the provisions of Article IV of the Original Indenture, and will comply with the provisions thereof as well as with other provisions of the Original Indenture and indentures supplemental thereto in connection with the issuance of additional bonds so that it will be entitled to procure the authentication and delivery of the Bonds; and

WHEREAS, the Authority Bonds are to be issued under a Trust Indenture, dated as of November 15, 2004 (the "Authority Indenture"), between the Authority and Wachovia Bank, National Association, as trustee (the "Authority Trustee"); and

WHEREAS, the proceeds of the Authority Bonds are to be loaned to the Company pursuant to the terms of a Financing Agreement dated as of November 15, 2004 between the Company and the Authority (the "Financing Agreement") and the Bonds are to be issued by the Company to secure the obligation of the Company to pay to or for the account of the Authority an amount equal to the principal of, redemption premium, if any, and interest on the Authority Bonds pursuant to the Financing Agreement; and

WHEREAS, the right, title and interest of the Authority in and to the Financing Agreement and the payments thereunder and the security for such payments are to be assigned by the Authority to the Authority Trustee, and the Bonds are to be delivered by the Company on behalf of the Authority directly to the Authority Trustee, as assignee of the Trustee, as security for the payment of the principal of, redemption premium, if any, and interest on, the Authority Bonds; and

WHEREAS, Article XVIII of the Original Indenture provides that the Company, when authorized by resolution of its Board of Directors, may with the Trustee enter into an indenture supplemental to the Original Indenture, which thereafter shall form a part of the Original Indenture, for the purposes, inter alia, of subjecting to the lien of the Original Indenture additional property, of defining the covenants and provisions applicable to any bonds of any series other than the 3 1/4% Series due 1971, of adding to the covenants and agreements of the Company contained in the Original Indenture other covenants and agreements thereafter to be observed by the Company, of surrendering any right or power in the Original Indenture reserved to or conferred upon the Company, and of making such provisions in regard to matters or questions arising under the Original Indenture as may be necessary or desirable and not inconsistent therewith; and

WHEREAS, the Company, by proper corporate action, has duly authorized the creation of the 5.05% Series due 2039 (to be issued in accordance with the terms and provisions

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of the Original Indenture and indentures supplemental thereto, including this Thirty-Eighth Supplemental Indenture, and to be secured by said Original Indenture and indentures supplemental thereto, including this Thirty-Eighth Supplemental Indenture) and has further duly authorized the execution, delivery and recording of this Thirty-Eighth Supplemental Indenture setting forth the terms and provisions of the 5.05% Series due 2039 insofar as said terms and provisions are not set forth in said Original Indenture; and

WHEREAS, the 5.05% Series due 2039 Bonds and the Trustee's certificate upon said Bonds are to be substantially in the following form - the proper amount, names of registered owners and numbers to be inserted therein, and such appropriate insertions, omissions and changes to be made therein as may be required or permitted by this Indenture to conform to any pertinent law or usage:

No. R-1

\$ 14,000,000

AQUA PENNSYLVANIA, INC.

(Incorporated under the Laws of the Commonwealth
of Pennsylvania)

First Mortgage Bond, 5.05% Series Due 2039

Aqua Pennsylvania, Inc. (f/k/a known as Pennsylvania Suburban Water Company, successor by merger to Philadelphia Suburban Water Company), a corporation organized and existing under the laws of the Commonwealth of Pennsylvania (hereinafter called the "Company", which term shall include any successor corporation as defined in the Indenture hereinafter referred to), for value received, hereby promises to pay to Northumberland County Industrial Development Authority or its registered assigns, on the 1st day of October, 2039, at the designated office of J.P. Morgan Trust Company, National Association (hereinafter called the "Trustee") in Philadelphia, Pennsylvania, the sum of Fourteen Million Dollars in such coin or currency of the United States of America as at the time of payment is legal tender for the payment of public and private debts and to pay interest thereon to the registered owner hereof by draft or check of the Trustee mailed to such registered owner from the interest payment date next preceding the date of the authentication of this Bond (or if this Bond is authenticated after a Record Date as defined below and on or before the succeeding interest payment date, from such succeeding interest payment date, or if this Bond is authenticated on or prior to March 15, 2005, from the date hereof) until the principal hereof shall become due and payable, at the rate of five and five-one-hundredths percent (5.05%) per annum, payable semiannually in like coin or currency on the first day of April and the first day of October in each year, commencing April 1, 2005 and to pay interest on overdue principal (including any overdue required or optional prepayment of principal) and premium, if any, and, to the extent legally enforceable, on any overdue installment of interest at a rate of 5.05% per annum after maturity whether by acceleration or otherwise until paid.

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The interest so payable will (except as otherwise provided in the Thirty-Eighth Supplemental Indenture referred to herein) be calculated on the basis of a 360-day year of twelve 30-day months and be paid to the person in whose name this Bond (or a Bond or Bonds in exchange for which this Bond was issued) is registered at the close of business on the fifteenth day of the calendar month next preceding the month in which the interest payment date occurs whether or not such day is a business day (a "Record Date") and principal, premium, if any, and interest on this Bond shall be paid in accordance with written payment instructions of the registered owner delivered to the Trustee on or before such record date.

This Bond is one of a duly authorized issue of bonds of the Company known as its First Mortgage Bonds, issued and to be issued without limitation as to aggregate principal amount except as set forth in the Indenture hereinafter mentioned in one or more series and equally secured (except insofar as a sinking fund or other similar fund established in accordance with the provisions of the Indenture may afford additional security for the bonds of any specific series) by an Indenture of Mortgage (herein called the "Indenture") dated as of January 1, 1941, executed by the Philadelphia Suburban Water Company (now Aqua Pennsylvania, Inc., f/k/a Pennsylvania Suburban Water Company, as successor by merger) to The Pennsylvania Company for Insurances on Lives and Granting Annuities (succeeded as trustee by J.P. Morgan Trust Company, National Association), as Trustee, to which Indenture and all indentures supplemental thereto reference is hereby made for a description of the property mortgaged and pledged, the nature and extent of the security, the rights of the holders and registered owners of the bonds and of the Trustee in respect of such security, and the terms and conditions under which the bonds are and are to be secured and may be issued under the Indenture; but neither the foregoing reference to the Indenture nor any provision of this Bond or of the Indenture or of any indenture

supplemental thereto shall affect or impair the obligation of the Company, which is absolute and unconditional, to pay at the stated or accelerated maturity herein and in the Indenture provided, the principal of and premium, if any, and interest on this Bond as herein provided. As provided in the Indenture, the bonds may be issued in series for various principal amounts, may bear different dates and mature at different times, may bear interest at different rates and may otherwise vary as in the Indenture provided or permitted. This Bond is one of the Bonds described in an indenture supplemental to said Indenture known as the "Thirty-Eighth Supplemental Indenture" dated as of November 15, 2004, and designated therein as "First Mortgage Bonds, 5.05% Series due 2039" (the "Bonds").

To the extent permitted by and as provided in the Indenture, modifications or alterations of the Indenture, or of any indenture supplemental thereto, and of the rights and obligations of the Company and of the holders and registered owners of bonds issued and to be issued thereunder may be made with the consent of the Company by an affirmative vote of the holders and registered owners of not less than 75% in principal amount of bonds then outstanding under the Indenture and entitled to vote, at a meeting of the bondholders called and held as provided in the Indenture, and, in case one or more but less than all of the series of bonds then outstanding under the Indenture are so affected, by an affirmative vote of the holders and registered owners of not less than 75% in principal amount of bonds of any series then outstanding under the Indenture and entitled to vote on and affected by such modification or alteration, or by the written consent of the holders and registered owners of such percentages of

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bonds; provided, however, that no such modification or alteration shall be made which shall reduce the percentage of bonds the consent of the holders or registered owners of which is required for any such modification or alteration or which shall affect the terms of payment of the principal of or interest on the bonds, or permit the creation by the Company of any lien prior to or on a parity with the lien of the Indenture with respect to any property subject to the lien of the Indenture as a first mortgage lien thereon, or which shall affect the rights of the holders or registered owners of less than all of the bonds of any series affected thereby.

The Bonds have been issued by the Company to secure the obligation of the Company to pay to or for the account of the Authority (defined below) an amount equal to the principal, premium, if any, of, and interest on, the Authority Bonds (defined below) pursuant to the Financing Agreement (the "Financing Agreement") dated as of November 15, 2004, between the Northumberland County Industrial Development Authority, a Pennsylvania body politic and corporate (the "Authority"), and the Company, which Authority Bonds are being issued to finance the refunding of the Authority's Exempt Facilities Revenue Bonds, Series 1993 (Roaring Creek Water Company Project), previously issued by the Authority on behalf of Roaring Creek Water Company (predecessor company to the Company) (the "Refunding Project"). The Refunding Project is to be financed through the sale of the Authority's Water Facilities Revenue Refunding Bonds (Aqua Pennsylvania, Inc. Project), Series of 2004 (the "Authority Bonds").

The Authority Bonds are to be issued under a Trust Indenture, dated as of November 15, 2004 (the "Authority Indenture"), between the Authority and Wachovia Bank, National Association, as trustee (the "Authority Trustee"). The right, title and interest of the Authority in and to the Financing Agreement and the payments thereunder and the security for such payments have been assigned by the Authority to the Authority Trustee, and the Bonds have been delivered by the Company on behalf of the Authority directly to the Authority Trustee, as assignee, as security for the payment of the principal of, and premium, if any, and interest on, the Authority Bonds. The Authority Trustee may not sell, assign or otherwise transfer the Bonds except for a transfer of the entire outstanding principal amount thereof to its successor as Trustee under the Authority Indenture, which successor and each subsequent successor shall hold such Bonds subject to the same restriction on transfer.

In the event any Authority Bonds shall be purchased by the Company and cancelled pursuant to the Authority Indenture, Bonds corresponding in principal amount to the Authority Bonds so purchased and cancelled shall be deemed to be paid in full, and in the event and to the extent the principal of, and premium, if any, or interest on, any Authority Bonds is paid out of funds held by the Authority Trustee other than payments on Bonds, the corresponding payment of the principal of and premium, if any, or interest on, an aggregate principal amount of Bonds shall be deemed to have been satisfied.

In the event this Bond shall be deemed to have been paid in full, this Bond shall be surrendered to the Trustee for cancellation. In the event this Bond shall be deemed to have been paid in part, this Bond shall be presented to the Trustee for notation hereon of the payment of the portion of the principal hereof so deemed to have been paid.

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The Bonds are redeemable only as follows:

(a) The Bonds are subject to redemption prior to maturity, at the option of the Company, on or after October 1, 2014, in whole or in part, at a redemption price of 100% of the principal amount of the Bonds to be redeemed, plus interest accrued thereon to the date fixed for redemption.

(b) The Bonds are also subject to redemption at the direction of the Company, in whole, at any time prior to maturity, at a redemption price of 100% of the principal amount of the bonds to be redeemed, plus interest accrued thereon to the date fixed for redemption, at any time the Authority Bonds are subject to extraordinary optional redemption pursuant to Section 7.01(b) of the Authority Indenture.

(c) The Bonds are also subject to mandatory redemption by the Company in whole if the Trustee shall receive a written demand from the Authority Trustee for redemption of all such Bonds held by the Authority Trustee stating that an "Event of Default" as defined in Section 9.01(a) of the Authority Indenture has occurred and is continuing and that payment of the principal of the Authority Bonds has been accelerated pursuant to Section 9.01(b) of the Authority Indenture, provided that at the time of notice of such redemption as provided in Section 2 of Article V of the Original Indenture (i) said written demand shall not have been withdrawn by the Authority Trustee, and (ii) no event of default under Section 1 of Article XI of the Original Indenture shall have occurred and be continuing.

If this Bond or any portion hereof is called for redemption and payment thereof is duly provided for as specified in the Indenture, interest shall cease to accrue hereon or on such portion, as the case may be, from and after the date fixed for redemption.

The principal hereof may be declared or may become due prior to its maturity date on the conditions, in the manner and with the effect set forth in the Indenture upon the happening of an event of default, as in the Indenture provided; subject, however, to the right, under certain circumstances, of the registered owners of a majority in principal amount of Bonds outstanding to annul such declaration.

This Bond is transferable by the registered owner hereof in person or by attorney duly authorized in writing, on books of the Company to be kept for that purpose at the designated office of the Trustee in Philadelphia, Pennsylvania upon surrender hereof for cancellation at such office and upon presentation of a written instrument of transfer duly executed, and thereupon the Company shall issue in the name of the transferee or transferees, and the Trustee shall authenticate and deliver, a new Bond or Bonds in authorized denominations, of equal aggregate unpaid principal amount. Any such transfer or exchange shall be subject to the terms and conditions and to the payment of the charges specified in the Indenture.

The Company and the Trustee may deem and treat the registered owner of this Bond as the absolute owner hereof for the purpose of receiving payment of or on account of the principal hereof and the interest hereon, and for all other purposes, and shall not be affected by any notice to the contrary.

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No recourse shall be had for the payment of the principal of or interest on this Bond or for any claim based hereon or otherwise in respect hereof or of the Indenture or of any indenture supplemental thereto against any incorporator or any past, present or future stockholder, officer or director of the Company or of any predecessor or successor corporation, as such, either directly or through the Company or through any such predecessor or successor corporation or through any receiver or trustee in bankruptcy, by virtue of any constitutional provision, statute or rule of law or equity, or by the

enforcement of any assessment or penalty or otherwise; all such liability being, by the acceptance hereof and as part of the consideration for the issue hereof, expressly waived and released by every holder or registered owner hereof, as more fully provided in the Indenture.

This Bond shall not be entitled to any benefit under the Indenture or any indenture supplemental thereto, or become valid or obligatory for any purpose, until J.P. Morgan Trust Company, National Association, as Trustee under the Indenture, or a successor trustee thereunder, shall have signed the certificate of authentication endorsed hereon.

IN WITNESS WHEREOF, Aqua Pennsylvania, Inc. has caused this Bond to be signed by its President or a Vice President and its corporate seal to be hereto affixed and attested by its Secretary or an Assistant Secretary, and this Bond to be dated November 30, 2004.

Attest: AQUA PENNSYLVANIA, INC.

By: _____
Vice President and Treasurer

(Assistant) Secretary

(Form of Trustee's Certificate)

This Bond is one of the Bonds, of the series designated therein, referred to in the within-mentioned Thirty-Eighth Supplemental Indenture.

J.P. MORGAN TRUST COMPANY,
NATIONAL ASSOCIATION

By: _____
Authorized Signer

and;

WHEREAS, all acts and things necessary to make the Bonds, when executed by the Company and authenticated and delivered by the Trustee as in this Thirty-Eighth Supplemental Indenture provided and issued by the Company, valid, binding and legal obligations of the Company, and this Thirty-Eighth Supplemental Indenture a valid and enforceable supplement to said Original Indenture, have been done, performed and fulfilled, and the execution of this Thirty-Eighth Supplemental Indenture has been in all respects duly authorized; and

NOW, THEREFORE, THIS THIRTY-EIGHTH SUPPLEMENTAL INDENTURE WITNESSETH: That, in order to secure the payment of the principal and interest of all bonds issued under the Original Indenture and all indentures supplemental thereto, according to their tenor and effect, and according to the terms of the Original Indenture and of any indenture supplemental thereto, and to secure the performance of the covenants and obligations in said bonds and in the Original Indenture and any indenture supplemental thereto respectively contained, and to provide for the proper issuing, conveying and confirming unto the Trustee, its successors in said trust and its and their assigns forever, upon the trusts and for the purposes expressed in the Original Indenture and in any indenture supplemental thereto, all and singular the estates, property and franchises of the Company thereby mortgaged or intended so to be, the Company, for and in consideration of the premises and of the sum of One Dollar (\$1.00) in hand paid by the Trustee to the Company upon the execution and delivery of this Thirty-Eighth Supplemental Indenture, receipt whereof is hereby acknowledged, and of other good and valuable consideration, and intending to be legally bound, has granted, bargained, sold, aliened, enfeoffed, released and confirmed and by these presents does grant, bargain, sell, alien, enfeoff, release and confirm unto J.P. Morgan Trust Company, National Association, as Trustee, and to its successors in said trust and its and their assigns forever:

All and singular the premises, property, assets, rights and franchises of the Company, whether now or hereafter owned, constructed or acquired, of whatever character and wherever situated (except as herein expressly excepted), including among other things the following, but reference to or enumeration of any particular kinds, classes, or items of property shall not be deemed to

exclude from the operation and effect of the Original Indenture or any indenture supplemental thereto any kind, class or item not so referred to or enumerated:

I.

REAL ESTATE AND WATER RIGHTS.

The real estate described in the deeds from the grantors named in Exhibit C hereto, dated and recorded as therein set forth, and any other real estate and water rights acquired since the date of the Thirty-Seventh Supplemental Indenture.

II.

BUILDINGS AND EQUIPMENT.

All mains, pipes, pipe lines, service pipes, buildings, improvements, standpipes, reservoirs, wells, flumes, sluices, canals, basins, cribs, machinery, conduits, hydrants, water works, plants and systems, tanks, shops, structures, purification systems, pumping stations, fixtures, engines, boilers, pumps, meters and equipment which are now owned or may hereafter be acquired by the Company (except as herein expressly excepted), including all improvements, additions and extensions appurtenant to any real or fixed property now or hereafter subject to the lien of the Original Indenture or any indenture supplemental thereto which are used or useful in connection with the business of the Company as a water company or as a water utility, whether any of the foregoing property is now owned or may hereafter be acquired by the Company.

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It is hereby declared by the Company that all property of the kinds described in the next preceding paragraph, whether now owned or hereafter acquired, has been or is or will be owned or acquired with the intention of using the same in carrying on the business or branches of the business of the Company, and it is hereby declared that it is the intention of the Company that all thereof (except property hereinafter specifically excepted) shall be subject to the lien of the Original Indenture.

It is agreed by the Company that so far as may be permitted by law, tangible personal property now owned or hereafter acquired by the Company, except such as is hereafter expressly excepted from the lien hereof, shall be deemed to be and construed as fixtures and appurtenances to the real property of the Company.

III.

FRANCHISES AND RIGHTS OF WAY.

All the corporate and other franchises of the Company, all water and flowage rights, riparian rights, easements and rights of way, and all permits, licenses, rights, grants, privileges and immunities, and all renewals, extensions, additions or modifications of any of the foregoing, whether the same or any thereof, or any renewals, extensions, additions or modifications thereof, are now owned or may hereafter be acquired, owned, held, or enjoyed by the Company.

IV.

AFTER ACQUIRED PROPERTY.

All real and fixed property and all other property of the character hereinabove described which the Company may hereafter acquire.

TOGETHER WITH all and singular the tenements, hereditaments and appurtenances belonging or in any way appertaining to the aforesaid property or any part thereof, with the reversion and reversions, remainder and remainders, tolls, rents, revenues, issues, income, product and profits thereof, and all the estate, right, title, interest and claim whatsoever, at law as well as in equity, which the Company now has or may hereafter acquire in and to the aforesaid premises, property, rights and franchises and every part and parcel thereof.

EXCEPTING AND RESERVING, HOWEVER, certain premises, not used or useful in the supplying of water by the Company, expressly excepted and reserved from

the lien of the Original Indenture and not subject to the terms thereof.

AND ALSO SAVING AND EXCEPTING from the property hereby mortgaged and pledged, all of the following property (whether now owned by the Company or hereafter acquired by it): All bills, notes and accounts receivable, cash on hand and in banks, contracts, choses in action and leases to others (as distinct from the property leased and without limiting any rights of the Trustee with respect thereto under any of the provisions of the Original

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Indenture or of any indenture supplemental thereto), all bonds, obligations, evidences of indebtedness, shares of stock and other securities, and certificates or evidences of interest therein, all automobiles, motor trucks, and other like automobile equipment and all furniture, and all equipment, materials, goods, merchandise and supplies acquired for the purpose of sale in the ordinary course of business or for consumption in the operation of any properties of the Company other than any of the foregoing which may be specifically transferred or assigned to or pledged or deposited with the Trustee hereunder or required by the provisions of the Original Indenture or any indenture supplemental thereto so to be; provided, however, that if, upon the happening of a completed default, as specified in Section 1 of Article XI of the Original Indenture, the Trustee or any receiver appointed hereunder shall enter upon and take possession of the mortgaged property, the Trustee or any such receiver may, to the extent permitted by law, at the same time likewise take possession of any and all of the property described in this paragraph then on hand and any and all other property of the Company then on hand, not described or referred to in the foregoing granting clauses, which is used or useful in connection with the business of the Company as a water company or as a water utility, and use and administer the same to the same extent as if such property were part of the mortgaged property, unless and until such completed default shall be remedied or waived and possession of the mortgaged property restored to the Company, its successors or assigns.

SUBJECT, HOWEVER, to the exceptions, reservations and matters hereinabove and in the Original Indenture recited, to releases executed since the date of the Original Indenture in accordance with the provisions thereof, to existing leases, to easements and rights of way for pole lines and electric transmission lines and other similar encumbrances and restrictions which the Company hereby certifies, in its judgment, do not impair the use of said property by the Company in its business, to liens existing on or claims against, and rights in and relating to, real estate acquired for right-of-way purposes, to taxes and assessments not delinquent, to alleys, streets and highways that may run across or encroach upon said lands, to liens, if any, incidental to construction, and to Permitted Liens, as defined in the Original Indenture; and, with respect to any property which the Company may hereafter acquire, to all terms, conditions, agreements, covenants, exceptions and reservations expressed or provided in such deeds and other instruments, respectively, under and by virtue of which the Company shall hereafter acquire the same and to any and all liens existing thereon at the time of such acquisition.

TO HAVE AND TO HOLD, all and singular the property, rights, privileges and franchises hereby conveyed, transferred or pledged or intended so to be unto the Trustee and its successors in the trust heretofore and hereby created, and its and their assigns forever.

IN TRUST NEVERTHELESS, for the equal pro rata benefit and security of each and every entity who may be or become the holders of bonds and coupons secured by the Original Indenture or by any indenture supplemental thereto, or both, without preference, priority or distinction as to lien or otherwise of any bond or coupon over or from any other bond or coupon, so that each and every of said bonds and coupons issued or to be issued, of whatsoever series, shall have the same right, lien and privilege under the Original Indenture and all indentures supplemental thereto and shall be equally secured hereby and thereby, with the same effect as if said bonds and coupons had all been made, issued and negotiated simultaneously on

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the date thereof; subject, however, to the provisions with reference to extended, transferred or pledged coupons and claims for interest contained in the Original Indenture and subject to any sinking or improvement fund or maintenance deposit provisions, or both, for the benefit of any particular

series of bonds.

IT IS HEREBY COVENANTED, DECLARED AND AGREED, by and between the parties hereto, that all such bonds and coupons are to be authenticated, delivered and issued, and that all property subject or to become subject hereto is to be held subject to the further covenants, conditions, uses and trusts hereinafter set forth, and the Company, for itself and its successors and assigns, does hereby covenant and agree to and with the Trustee and its successor or successors in said trust, for the benefit of those who shall hold said bonds and coupons, or any of them, issued under this Indenture or any indenture supplemental hereto, or both, as follows:

ARTICLE I.
Form, Authentication and Delivery of the Bonds;
Redemption Provisions

SECTION 1. There shall be a forty-fourth series of bonds, limited in aggregate principal amount to \$14,000,000 designated as "Aqua Pennsylvania, Inc., First Mortgage Bonds, 5.05% Series due 2039".

Interest on the 5.05% Series due 2039 shall be payable semiannually on April 1 and October 1 of each year (each an "interest payment date"), commencing April 1, 2005. Each Bond shall be dated the date of its authentication and shall bear interest from the interest payment date next preceding the date of the authentication of such Bond (or if such Bond is authenticated after a Record Date as defined below and on or before the succeeding interest payment date, from such succeeding interest payment date, or if such Bond is authenticated on or prior to the record date for the first interest payment date for the Bonds, in which case it shall bear interest from the date of original issuance of the Bonds); provided, however, that, if at the time of authentication of any Bond, interest on the predecessor Bond of such Bond is in default, such Bond shall bear interest from the date to which interest has been paid, or, if no interest has been paid, from the date of original issuance thereof. The 5.05% Series due 2039 shall be stated to mature (subject to the right of earlier redemption at the prices and dates and upon the terms and conditions hereinafter set forth) on October 1, 2039 and shall bear interest at the rate of 5.05%.

The Bonds shall be issuable only as registered bonds without coupons, shall be in the form hereinabove recited, in the denomination of Five Thousand Dollars (\$5,000) or any integral multiple thereof, shall be lettered "R" and shall bear such numbers as the Company may reasonably require.

The principal of, and interest on the Bonds shall be payable at the designated office of the trustee in Philadelphia, Pennsylvania, and shall be payable, along with interest on the Bonds, in such coin or currency of the United States of America as at the time of payment is legal tender for the payment of public and private debts; each installment of interest shall be paid by check to the order of the person entitled thereto, mailed to such person's address as the same appears on the books maintained for such purpose by or on behalf of the Company, or by bank

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wire transfer of immediately available funds pursuant to instructions and conditions incorporated in an agreement between such person and the Trustee or the Company.

The person in whose name any Bond is registered at the close of business on any Record Date (as hereinafter defined) with respect to any interest payment date shall be entitled to receive the interest payable on such interest payment date notwithstanding the cancellation of such Bond upon any transfer or exchange subsequent to the Record Date and prior to such interest payment date; provided, however, that if and to the extent the Company shall default in the payment of the interest due on such interest payment date, such defaulted interest shall be paid to the persons in whose names outstanding Bonds are registered at the close of business on a subsequent Record Date established by notice given by mail by or on behalf of the Company to the holders of Bonds not less than fifteen days preceding such subsequent Record Date, such Record Date to be not less than ten days preceding the date of payment of such defaulted interest. The term "Record Date" with respect to any regular interest payment date shall mean the fifteenth day of the calendar month next preceding the month in which such interest payment date occurs.

The Bonds are being issued by the Company to secure the obligation of

the Company to pay to or for the account of the Authority an amount equal to the principal of, at maturity or earlier redemption, and interest on, the Authority Bonds pursuant to the Financing Agreement. The Authority Bonds are being sold to finance the refunding of the Prior Bonds.

The Authority Bonds are to be issued under the Authority Indenture and the right, title and interest of the Authority in and to the Financing Agreement and the payments thereunder and the security for such payments have been assigned by the Authority to the Authority Trustee, and the Bonds are to be delivered by the Company on behalf of the Authority directly to the Authority Trustee, as assignee, as security for the payment of the principal of, at maturity or earlier redemption, and premium, if any, and interest on, the Authority Bonds. The Authority Trustee may not sell, assign or otherwise transfer the Bonds except for a transfer of the entire outstanding principal amount thereof to its successor as Trustee under the Authority Indenture, which successor and each subsequent successor shall hold the Bonds subject to the same restriction on transfer.

The text of the Bonds and of the certificate of the Trustee upon such Bonds shall be, respectively, substantially of the tenor and effect hereinbefore recited.

Exchange of any Bonds shall be effected in accordance with the applicable provisions of Sections 7, 8 and 9 of Article II of the Original Indenture.

SECTION 2. The Bonds are redeemable only as follows:

(a) The 5.05% Series due 2039 are subject to redemption prior to maturity on or after October 1, 2014 by the Company, to the extent that the Authority Bonds are called for redemption under Section 7.01(a) of the Authority Indenture, and then out of moneys deposited with or held by the Trustee for such purpose, as a whole or in part, at any time in the manner

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described below, at the redemption price of one hundred percent (100%) of the principal amount to be redeemed, plus interest accrued thereon to the date fixed for redemption;

(b) The Bonds are subject to redemption at the direction of the Company, in whole, at any time prior to maturity, at a redemption price of 100% of the principal amount of the bonds to be redeemed, plus interest accrued thereon to the date fixed for redemption, at any time the Authority Bonds are subject to extraordinary optional redemption pursuant to Section 7.01(b) of the Authority Indenture; and

(c) The Bonds are also subject to mandatory redemption by the Company in whole if the Trustee shall receive a written demand from the Authority Trustee for redemption of all such Bonds held by the Authority Trustee stating that an "Event of Default" as defined in Section 9.01(a) of the Authority Indenture has occurred and is continuing and that payment of the principal of the Authority Bonds has been accelerated pursuant to Section 9.01(b) of the Authority Indenture, provided that at the time of notice of such redemption as provided in Section 2 of Article V of the Original Indenture (i) said written demand shall not have been withdrawn by the Authority Trustee, and (ii) no event of default under Section 1 of Article XI of the Original Indenture shall have occurred and be continuing.

SECTION 3. Any redemption of the Bonds shall be effected in accordance with the provisions of Article V of the Original Indenture.

SECTION 4. In the event any Authority Bonds shall be purchased by the Company, surrendered by the Company to the Authority Trustee for cancellation and cancelled by the Authority Trustee, Bonds corresponding in principal amount to the Authority Bonds so purchased, surrendered and cancelled shall be deemed to have been paid in full.

SECTION 5. In the event and to the extent the principal of and premium, if any, or interest on, any Authority Bonds is paid out of funds held by the Authority Trustee other than payments of Bonds, the corresponding payment of the principal of, and premium, if any, or interest on, an aggregate principal amount of Bonds equal to the aggregate principal amount of such Authority Bonds shall be deemed to have been satisfied.

SECTION 6. All Bonds deemed to have been paid in full as provided in Section 4 and 5 of this Article I of this Thirty-Eighth Supplemental Indenture shall be surrendered to the Trustee for cancellation, and the Trustee shall forthwith cancel the same and, in accordance with applicable laws and regulations and the Trustee's policies and procedures, and on the written request of the Company, deliver the same to the Company. In case part of an outstanding Bond shall be deemed to have been partially paid as provided in said Section 4 or Section 5, upon presentation of such Bond at the designated office of the Trustee, the Trustee shall make a notation thereon of the payment of the portion of the principal amount of such Bond so deemed to have been paid unless the registered owner shall elect to surrender such Bond to the Trustee, in which case the Company shall execute and the Trustee shall authenticate and deliver, without charge to the registered owner, Bonds in such authorized denominations as shall be specified by the registered owner for the unpaid balance of the principal amount of such outstanding Bond.

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SECTION 7. The 5.05% Series due 2039 in the aggregate principal amount of \$14,000,000 may be issued under the provisions of Article IV of the Original Indenture and may forthwith be executed by the Company and delivered to the Trustee and shall be authenticated by the Trustee and delivered to or upon the order of the Company, upon receipt by the Trustee of the resolutions, certificates, opinions or other instruments or all of the foregoing required to be delivered upon the issue of bonds pursuant to the provisions of the Original Indenture.

ARTICLE II.

Maintenance or Improvement Deposit.

SECTION 1. The Company covenants that it will deposit with the Trustee on or before the March 1 next occurring after the bonds of the 9.89% Series due 2008 cease to be outstanding, or on or before the March 1 next occurring after the bonds of the 9.93% Series due 2013 cease to be outstanding, or on or before the next March 1 next occurring after the bonds of the 9.97% Series due 2018 cease to be outstanding, or on or before the March 1 next occurring after the bonds of the 9.12% Series due 2010 cease to be outstanding, or on or before the March 1 next occurring after the bonds of the 9.29% Series due 2026 cease to be outstanding, or on or before the March 1 next occurring after the bonds of the 9.17% Series due 2021 cease to be outstanding, or on or before the next March 1 next occurring after the bonds of the 9.17% Series due 2011 cease to be outstanding, or on or before the March 1 next occurring after the bonds of the 7.15% Series due 2008 cease to be outstanding, or on or before the March 1 next occurring after the bonds of any of the Subseries of the 1995 Medium Term Note Series issued under the Twenty-Ninth Supplemental Indenture (consisting of the 7.72% Subseries A due 2025, the 6.82% Subseries B due 2005, the 6.89% Subseries C due 2015, and the 6.99% Subseries D due 2006) shall cease to be outstanding, or on or before the March 1 next occurring after bonds of the 6.35% Series due 2025 shall cease to be outstanding, or on or before the March 1 next occurring after the bonds of any of the Subseries of the 1997 Medium Term Note Series issued under the Thirty-First Supplemental Indenture (consisting of the 6.75% Subseries A due 2007 and the 6.14% Subseries C due 2008) cease to be outstanding, or on or before March 1 next occurring after the bonds of 6.00% Series due 2029 cease to be outstanding, or on or before March 1 next occurring after the Bonds of any of the Subseries of the 1999 Medium Term Note Series issued under the Thirty-Third Supplemental Indenture (consisting of the 7.40% Subseries A due 2005, the 7.40% Subseries B due 2005, the 9.53% Subseries D due 2019, the 6.375% Subseries E due 2023, the 8.26% Subseries F due 2022, the 9.50% Subseries G due 2006, the 9.22% Subseries H due 2019, the 8.32% Subseries I due 2022, the 8.14% Subseries J due 2025, the 6.00% Subseries K due 2030, the 5.93% Subseries L due 2012, the 2.65% Subseries M due 2006, the 3.461% Subseries N due 2007, the 5.08% Subseries O due 2015, the 5.17% Subseries P due 2017, the 5.751% Subseries Q due 2019, the 5.751% Subseries R due 2019, the 6.06% Subseries S due 2027, the 6.06% Subseries T due 2027 and the 5.98% Subseries U due 2028) cease to be outstanding, or on or before March 1 next occurring after the bonds of the 5.35% Series due 2031 or on or before March 1 next occurring after the bonds of the 5.55% Series due 2032 cease to be outstanding, or on or before March 1 next occurring after the bonds of the 3.75% Series due 2010 cease to be outstanding, or on or before March 1 next occurring after the bonds of the 5.15% Series due 2032 cease to be outstanding, whichever is latest, an amount in

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cash (the "Maintenance or Improvement Deposit") equal to 9% of the Gross Operating Revenues of the Company during the preceding calendar year less, to the extent that the Company desires to take such credits, the following:

(a) the amount actually expended for maintenance during such calendar year; and

(b) the Cost or Fair Value, whichever is less, of Permanent Additions acquired during such calendar year which at the time of taking such credit constitute Available Permanent Additions; and

(c) the unapplied balance, or any part thereof, of the Cost or Fair Value, whichever is less, of Available Permanent Additions acquired by the Company during the five calendar years preceding such calendar year and specified in the Officers' Certificates delivered to the Trustee pursuant to Section 2 of this Article, but only to the extent that the Permanent Additions with respect to which such Cost or Fair Value was determined shall at the time of taking such credit constitute Available Permanent Additions.

SECTION 2. The Company covenants that it will on or before March 1 in each year, beginning with the first deposit made with the Trustee under the provisions of Section 1 of this Article, as long as any of the Bonds are outstanding, deliver to the Trustee the following:

(a) An Officers' Certificate, which shall state:

(i) The amount of the Gross Operating Revenues for the preceding calendar year;

(ii) 9% of such Gross Operating Revenues;

(iii) The amount actually expended by the Company for maintenance during such calendar year;

(iv) The amount set forth in subparagraph (xii) of each Officers' Certificate delivered to the Trustee pursuant to the provisions of this Section during the preceding five calendar years (specifying each such Officers' Certificate), after deducting from each such amount the aggregate of (a) the Cost or Fair Value, whichever is less, of all Permanent Additions represented by such amount which have ceased to be Available Permanent Additions; and (b) any part of such amount for which the Company has previously taken credit against any Maintenance or Improvement Deposit (specifying the Officers' Certificate in which such credit was taken); and (c) any part of such amount for which the Company then desires to take credit against the Maintenance or Improvement Deposit;

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(v) An amount which shall be the aggregate of all amounts set forth pursuant to the provisions of clause (c) of the foregoing subparagraph (iv);

(vi) The Cost or Fair Value, whichever is less, of Available Permanent Additions acquired by the Company during the preceding calendar year;

(vii) That part of the amount set forth in subparagraph (vi) which the Company desires to use as a credit against the Maintenance or Improvement Deposit;

(viii) The amount of cash payable to the Trustee under the provisions of Section 1 of this Article, which shall be the amount by which the amount set forth in subparagraph (ii) hereof exceeds the sum of the amounts set forth in subparagraphs (iii), (v) and (vii) hereof;

(ix) The sum of all amounts charged on the books of the Company against any reserve for retirement or depreciation during the preceding calendar year representing the aggregate of the Cost when acquired of any part of the Company's plants and property of the character described in the granting clauses hereof which has been permanently retired or abandoned;

(x) The aggregate of the amounts set forth in subparagraphs (v) and (vii) hereof;

(xi) The amount by which the amount set forth in subparagraph (x) exceeds the amount set forth in subparagraph (ix), being the amount required to be deducted from the Cost or Fair Value of Available Permanent Additions in order to determine a Net Amount of Available Permanent Additions pursuant to the provisions of Section 9 of Article I of the Original Indenture;

(xii) The amount set forth in subparagraph (vi) after deducting the amount, if any, set forth in subparagraph (vii); and

(xiii) That all conditions precedent to the taking of the credit or credits so requested by the Company have been complied with.

(b) In the event that the Officers' Certificate delivered to the Trustee pursuant to the provisions of paragraph (A) of this Section shall state, pursuant to the requirements of subparagraph (vi), the Cost or Fair Value of Available Permanent Additions acquired by the Company during the preceding calendar year, the documents specified in paragraphs 2, 3, 5, 6 and 7 of subdivision (B) of Section 3 of Article IV of the Original Indenture.

(c) An amount in cash equal to the sum set forth in subparagraph (viii) of the Officers' Certificate provided for in paragraph (A) hereof.

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SECTION 1. All cash deposited with the Trustee as part of any Maintenance or Improvement Deposit provided for in Section 1 of this Article, may, at the option of the Company, be applied to the purchase of bonds under the provisions of Section 2 of Article X of the Original Indenture or to the redemption of bonds under the provisions of Section 3 of Article X of the Original Indenture or may be withdrawn by the Company at any time to reimburse the Company for the cost of a Net Amount of Available Permanent Additions (excluding, however, from any such Available Permanent Additions all Permanent Additions included in any certificate delivered to the Trustee for the purpose of obtaining a credit against any Maintenance or Improvement Deposit provided for in Section 1 of this Article to the extent that such Permanent Additions have been used for any such credit). The Trustee shall pay to or upon the written order of the Company all or any part of such cash upon the receipt by the Trustee of:

(a) A Resolution requesting such payment; and

(b) The documents specified in paragraphs 2, 5, 6 and 7 of subdivision (B) of Section 3 of Article IV of the Original Indenture, with such modifications, additions and omissions as may be appropriate in the light of the purposes for which they are used.

ARTICLE III. Covenants of the Company.

SECTION 1. The Company hereby covenants and agrees with the Trustee, for the benefit of the Trustee and all the present and future holders of the Bonds, that the Company will pay the principal of, and premium, if any, and interest on, all bonds issued or to be issued as aforesaid under and secured by the Original Indenture as hereby supplemented, as well as all bonds which may be hereafter issued in exchange or substitution therefor, and will perform and fulfill all of the terms, covenants and conditions of the Original Indenture and of this Thirty-Eighth Supplemental Indenture with respect to the additional bonds to be issued under the Original Indenture as hereby supplemented.

SECTION 2. The Company covenants and agrees that so long as any of the Bonds are outstanding (a) the Company will not make any Stock Payment if, after giving effect thereto, its retained earnings, computed in accordance with generally accepted accounting principles consistently applied, will be less than the sum of (i) Excluded Earnings, if any, since December 31, 2003, and (ii) \$20,000,000; (b) Stock Payments made more than 40 days after the commencement, and prior to the expiration, of any Restricted Period shall not exceed 65% of the Company's Net Income during such Restricted Period; and (c) the Company will not authorize a Stock Payment if there has occurred and is continuing an event of default under subsections (a) and (b) of Section 1 of Article XI of the

Original Indenture.

For the purposes of this Section 2 the following terms shall have the following meanings:

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"Capitalization" shall mean the sum of (i) the aggregate principal amount of all Debt at the time outstanding, (ii) the aggregate par or stated value of all capital stock of the Company of all classes at the time outstanding, (iii) premium on capital stock, (iv) capital surplus, and (v) retained earnings.

"Debt" means (i) all indebtedness, whether or not represented by bonds, debentures, notes or other securities, for the repayment of money borrowed, (ii) all deferred indebtedness for the payment of the purchase price of property or assets purchased (but Debt shall not be deemed to include Customer Advances for Construction or any bonds issued under the Indenture which are not Outstanding Bonds), (iii) leases which have been or, in accordance with generally accepted accounting principles, should be recorded as capital leases and (iv) guarantees of the obligations of another of the nature described in clauses (i), (ii) or (iii) which have been or, in accordance with generally accepted accounting principles, should be recorded as debt.

"Determination Date" shall mean the last day of each calendar quarter. Any calculation with respect to any Determination Date shall be based on the Company's balance sheet as of such date.

"Excluded Earnings" shall mean 35% of the Company's Net Income during any Restricted Period.

"Net Income" for any particular Restricted Period shall mean the amount of net income properly attributable to the conduct of the business of the Company for such period, as determined in accordance with generally accepted accounting principles consistently applied, after payment of or provision for taxes on income for such period.

"Outstanding Bonds" shall mean bonds which are outstanding within the meaning indicated in Section 20 of Article I of the Original Indenture except that, in addition to the bonds referred to in clauses (a), (b) and (c) of said Section 20, said term shall not include bonds for the retirement of which sufficient funds have been deposited with the Trustee with irrevocable instructions to apply such funds to the retirement of such bonds at a specified time, which may be either the maturity thereof or a specified redemption date, whether or not notice of redemption shall have been given.

"Restricted Period" shall mean a period commencing on any Determination Date on which the total Debt of the Company is, or as the result of any Stock Payment then declared or set aside and to be made thereafter will be, more than 70% of Capitalization, and continuing until the third consecutive Determination Date on which the total Debt of the Company does not exceed 70% of Capitalization.

"Stock Payment" shall mean any payment in cash or property (other than stock of the Company) to any holder of shares of any class of capital stock of the Company as such holder, whether by dividend or upon the purchase, redemption, conversion or other acquisition of such shares, or otherwise.

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SECTION 3. The Company covenants and agrees that so long as any of the Bonds are outstanding, neither the Company nor any subsidiary of the Company will, directly or indirectly, lend or in any manner extend its credit to, or indemnify, or make any donation or capital contribution to, or purchase any security of, any corporation which directly or indirectly controls the Company, or any subsidiary or affiliate (other than an affiliate which is a subsidiary of the Company) of any such corporation.

ARTICLE IV.
The Trustee.

SECTION 1. The Trustee hereby accepts the trust hereby declared and provided, and agrees to perform the same upon the terms and conditions in

the Original Indenture, as supplemented by this Thirty-Eighth Supplemental Indenture.

SECTION 2. Subject to the provisions of Article XIII of the Original Indenture, the Trustee may execute any of the trusts or powers hereof and perform any of its duties by or through and consult with attorneys, agents, officers or employees selected by the Trustee in its sole discretion. The Trustee shall be entitled to advice of counsel concerning all matters of trusts hereof and the duties hereunder and may in all cases pay such reasonable compensation to all such attorneys, agents, officers and employees as may reasonably be employed in connection with the trusts hereof. The Trustee may act or refrain from acting and rely upon and be free from all liability for so relying upon the opinion or advice of any attorney (who may be the attorney or attorneys for the Company). The Trustee may act and rely on written opinions of experts employed by the Trustee and such advice shall be full and complete authorization and protection in respect of any action taken, suffered or omitted by the Trustee hereunder in good faith and in reliance thereon. The Trustee shall not be responsible for any loss or damage resulting from any action or non-action in good faith taken in reliance upon such opinion or advice. The Trustee shall not be bound to confirm, verify or make any investigation into the facts or matters stated in any financial or other statements, resolution, certificate, statement, instrument, opinion, report, notice, request, direction, consent, order or other paper or document furnished pursuant to the terms hereof.

SECTION 3. Before the Trustee shall be required to foreclose on, or to take control or possession of, the real property or leasehold interest (the "Premises") which may be the subject of any mortgage or mortgages for which the Trustee is mortgagee in connection with the issuance of the Bonds, the Trustee shall be indemnified and held harmless by the holders and/or beneficial owners of the Bonds from and against any and all expense, loss, or liability that may be suffered by the Trustee in connection with any spill, leak or release which may have occurred on or invaded the Premises or any contamination by any Hazardous Substance (hereinafter defined), whether caused by the Company or any other person or entity, including, but not limited to, (1) any and all reasonable expenses that the Trustee may incur in complying with any of the Environmental Statutes (hereinafter defined), (2) any and all reasonable costs that the Trustee may incur in studying or remedying any spill, leak or release which may have occurred on or invaded the Premises or any contamination, (3) any and all fines or penalties assessed upon the Trustee by reason of such contamination, (4) any and all loss of

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value of the Premises or the improvements thereon by reason of such contamination, and (5) any and all legal fees and costs reasonably incurred by the Trustee in connection with any of the foregoing. As used in this Section, contamination by any Hazardous Substance shall include contamination, arising from the presence, creation, production, collection, treatment, disposal, discharge, release, storage, transport or transfer of any Hazardous Substance at or from the Premises or any improvements thereon. As used in this Section, the term "Hazardous Substance" shall mean petroleum hydrocarbons or any substance which (a) constitutes a hazardous waste or substance under any applicable federal, state or local law, rule, order or regulation now or hereafter adopted; (b) constitutes a "hazardous substance" as such term is defined under the Comprehensive Environmental Response, Compensation and Liability Act, as amended (42 U.S.C. Section 9601 et seq.) and the regulations issued thereunder and any comparable state or local law or regulation; (c) constitutes a "hazardous waste" under the Resource Conservation and Recovery Act, (42 U.S.C. Section 6991) and the regulations issued thereunder and any comparable state or local law or regulation; (d) constitutes a pollutant, contaminant, chemical or industrial, toxic or hazardous substance or waste as such terms are defined under Federal Clean Water Act, as amended (33 U.S.C. Section 1251 et seq.), the Toxic Substances Control Act, as amended (15 U.S.C. Section 2601 et seq.), or any comparable state or local laws or regulations; (e) exhibits any of the characteristics enumerated in 40 C.F.R. Sections 261.20 - 261.24, inclusive; (f) those extremely hazardous substances listed in Section 302 of the Superfund Amendments and Reauthorization Act of 1986 (Public Law 99-499, 100 Stat. 1613) which are present in threshold planning or reportable quantities as defined under such act; (g) toxic or hazardous chemical substances which are present in quantities which exceed exposure standards as those terms are defined under Sections 6 and 8 of the Occupational Safety and Health Act, as amended (29 U.S.C. Sections 655 and 657 and 29 C.F.R. Part 1910, subpart 2); and (h) any asbestos, petroleum-based products or any Hazardous Substance contained within

or release from any underground or aboveground storage tanks. As used in this Section, the term "Environmental Statutes" shall mean the statutes, laws, rules, orders and regulations referred to in (a) through (g) inclusive in the preceding sentence.

ARTICLE V.
Miscellaneous.

SECTION 1. This instrument is executed and shall be construed as an indenture supplemental to the Original Indenture, and shall form a part thereof, and except as hereby supplemented, the Original Indenture and the First, Second, Third, Fourth, Fifth, Sixth, Seventh, Eighth, Ninth, Tenth, Eleventh, Twelfth, Thirteenth, Fourteenth, Fifteenth, Sixteenth, Seventeenth, Eighteenth, Nineteenth, Twentieth, Twenty-First, Twenty-Second, Twenty-Third, Twenty-Fourth, Twenty-Fifth, Twenty-Sixth, Twenty-Seventh, Twenty-Eighth, Twenty-Ninth, Thirtieth, Thirty-First, Thirty-Second, Thirty-Third, Thirty-Fourth, Thirty-Fifth, Thirty-Sixth and Thirty-Seventh Supplemental Indentures are hereby confirmed. All references in this Thirty-Eighth Supplemental Indenture to the Original Indenture shall be deemed to refer to the Original Indenture as heretofore amended and supplemented, and all terms used herein and not specifically defined herein shall be taken to have the same meaning as in the Original Indenture, as so amended, except in the cases where the context clearly indicates otherwise.

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SECTION 2. Any notices to the Trustee under this Thirty-Eighth Supplemental Indenture shall be delivered to the Trustee by registered or certified mail, hand delivery or other courier or express delivery service (with receipt confirmed) or by telecopy (with receipt confirmed) at the following address:

J.P. Morgan Trust Company, National Association
Institutional Trust Services
1650 Market Street, Suite 4700
Philadelphia, PA 19103
Attention: Aqua Pennsylvania, Inc. Administrator
Telecopy: (215) 640-3420

Any change in such address or telecopy number may be made by notice to the Company delivered in the manner set forth above.

SECTION 3. All recitals in this Thirty-Eighth Supplemental Indenture are made by the Company only and not by the Trustee; and all of the provisions contained in the Original Indenture in respect of the rights, privileges, immunities, powers and duties of the Trustee shall be applicable in respect hereof as fully and with like effect as if set forth herein in full.

SECTION 4. Although this Thirty-Eighth Supplemental Indenture is dated as of November 15, 2004 for convenience and for the purpose of reference, the actual date or dates of execution hereof by the Company and the Trustee are as indicated by their respective acknowledgments annexed hereto.

SECTION 5. In order to facilitate the recording or filing of this Thirty-Eighth Supplemental Indenture, the same may be simultaneously executed in several counterparts, each of which shall be deemed to be an original and such counterparts shall together constitute but one and the same instrument.

SECTION 6. This Thirty-Eighth Supplemental Indenture shall become effective for the incurrence of debt upon delivery to the Trustee by the Company of the certificates required by Articles IV, VI and VII of the Original Indenture, which shall occur concurrently with or prior to the authentication of the 5.05% Series due 2039 Bonds. This Thirty-Eighth Supplemental Indenture is effective to evidence the Trustee's lien on the property described herein immediately upon execution.

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IN WITNESS WHEREOF the parties hereto have caused their corporate seals to be hereunto affixed and their authorized officers have hereto affixed their signatures, and their authorized officers have duly attested the execution hereof, as of the 15th day of November, 2004.

[CORPORATE SEAL]

AQUA PENNSYLVANIA, INC.,
as successor by merger to
Philadelphia Suburban Water Company

Attest: ROY H. STAHL

By: KATHY L. PAPE

Vice President and Treasurer

[CORPORATE SEAL]

J.P. MORGAN TRUST COMPANY,
NATIONAL ASSOCIATION,
As Trustee

Attest: NOREEN WICHERT

Authorized Officer

By: ANNE MARIE O'BRIEN

Authorized Officer

EXHIBIT A

OUTSTANDING FIRST MORTGAGE BONDS

EXHIBIT B

RECORDING INFORMATION

BUCKS, CHESTER, DELAWARE AND MONTGOMERY COUNTIES

Indenture	Date of Recording	Bucks		Chester		Delaware		Montgomery	
		Book	Page	Book	Page	Book	Page	Book	Page
Original	2/20/41	496	1	H-13.Vol.307	20	1034	1	1625	1
First Supplemental	8/26/48	632	1	F-16.Vol.380	200	1668	169	2031	257
Second Supplemental	7/1/52	768	438	18.Vol.425	186	1962	376	2360	517
Third Supplemental	11/25/53	895	1	18.Vol.442	325	2052	1	2493	1
Fourth Supplemental	1/9/56	1089	155	Z-20.Vol.499	1	2199	1	2722	425
Fifth Supplemental	3/20/57	1181	316	B-22.Vol.536	601	2294	50	2850	335
Sixth Supplemental	5/9/58	1254	1	G-23	201	2380	039	2952	289
Seventh Supplemental	9/25/59	1332	509	B-25	109	2442	1	3090	249
Eighth Supplemental	5/9/61	-	-	Z-26	17	2526	312	-	-
Eighth Supplemental	5/10/61	1409	225	-	-	-	-	3249	289
Ninth Supplemental	4/10/62	1458	372	G-28	126	2581	463	3307	169
Tenth Supplemental	3/19/64	1568	1	M-30	967	2976	1043	3310	237
Eleventh Supplemental	11/4/66	1655	695	Q-32	6682	762	223	3549	129
Twelfth Supplemental	1/23/68	1691	531	N-33	219	2792	708	3542	315
Thirteenth Supplemental	7/2/70	1763	1167	D-35	80	2850	301	3687	23
Fourteenth Supplemental	11/5/70	1774	331	K-35	713	2858	3113	700	548
Fifteenth Supplemental	12/11/72	1869	196	O-37	998	2926	550	3786	96
Sixteenth Supplemental	5/28/75	1979	14	E-44	77	3005	511	4010	307
Seventeenth Supplemental	12/18/77	2072	683	L-51	1	3072	43	5002	436
Eighteenth Supplemental	4/29/77	2082	567	B-52	344	3078	728	5003	291
Nineteenth Supplemental	6/23/80	2303	714	J-62	92	3261	293	5030	502
Twentieth Supplemental	8/2/83	2487	370	D-72	1	96	810	5662	1045
Twenty-First Supplemental	8/27/85	2690	806	54	550	-	-	5864	1347
Twenty-First Supplemental	8/28/85	-	-	-	-	264	159	-	-
Twenty-Second Supplemental	4/22/86	2774	160	263	275	326	592	5944	360
Twenty-Third Supplemental	4/1/87	2960	693	-	-	-	-	-	-

Indenture	Date of Recording	Bucks		Chester		Delaware		Montgomery	
		Book	Page	Book	Page	Book	Page	Book	Page
Twenty-Third Supplemental	4/2/87	-	-	680	337	447	1807	6115	602
Twenty-Fourth Supplemental	7/25/88	3199	1095	1224	389	0593	0585	6324	143
Twenty-Fifth Supplemental	1/12/90	0136	0250	1848	205	731	1571	6538	376
Twenty-Sixth Supplemental	11/8/91	369	2190	2660	205	894	2241	6780	891
Twenty-Seventh Supplemental	6/29/92	0487	1829	3055	182	0969	2023	6918	302
Twenty-Eighth Supplemental	4/22/93	0652	1335	3542	1542	1081	0852	7112	0539
Twenty-Ninth Supplemental	3/30/95	1045	1872	3875	1368	1349	0829	7561	1155
Thirtieth Supplemental	8/30/95	1111	0798	3932	0471	1393	2255	7631	0689
Thirty-First Supplemental	7/11/97	1421	2196	4201	2133	1607	138	7968	779
Thirty-Second Supplemental	10/6/99	1939	421	4646	642	1936	1207	8548	1067
Thirty-Third Supplemental	11/30/99	1970	1573	4675	1272	1936	1207	8548	1067

Thirty-Fourth Supplemental	10/31/01	2471	1207	5101	2142	2288	0174	9225	761
Thirty-Fifth Supplemental	1/10/02	2541	765	5152	818	2329	1019	9314	1079
Thirty-Sixth Supplemental	6/5/02	2731	1881	5296	356	2448	1862	9593	1416
Thirty-Seventh Supplemental	12/27/02	3036	1425	12/31/02	1552	12/31/02	0294	12/30/02	0204
				B-5514		02631		10018	

BERKS COUNTY

Indenture	Date of Recording	Book	Page
Original	8/16/99	3113	707
Thirty-Second Supplement	10/6/99	3132	1510
Thirty-Third Supplement	11/30/99	3149	1260
Thirty-Fourth Supplement	10/31/01	3421	896
Thirty-Fifth Supplement	1/10/02	3461	417
Thirty-Sixth Supplement	6/4/02	3544	1357
Thirty-Seventh Supplement	12/30/02	3664	0001

BRADFORD, COLUMBIA, LAWRENCE, MERCER, NORTHUMBERLAND, PIKE, SCHUYLKILL AND WAYNE COUNTIES

Indenture	BRADFORD			COLUMBIA			LAWRENCE			MERCER		
	Date of Recording	Book	Page	Date of Recording	Book	Page	Date of Recording	Book	Page	Date of Recording	Book	Page
Thirty-Fifth Supplemental	12/21/01		200115497				1688	744				
Thirty-Sixth Supplemental	07/04/02		200207151									
Thirty-Seventh Supplemental	12/30/02		200216472									

Indenture	NORTHUMBERLAND			PIKE			SCHUYLKILL			WAYNE		
	Date of Recording	Book	Page									
Thirty-Fifth Supplemental		1404	246		1909	2328		1413	1		1911	1
Thirty-Sixth Supplemental		1445	028					1584	0259			
Thirty-Seventh Supplemental	12/30/02	1500	911	12/30/02	1959	2447	12/27/02	2022	1006	12/30/02	2136	148

EXHIBIT C

County and Grantor	Company's Real Estate Index No.	Date of Deed	Book	Recorded Page	Tax Parcel I.D. Number
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[See Attached]

EXHIBIT D

The Original Indenture, redacted to delete property descriptions contained therein for property contained in bucks, Chester, Delaware and Montgomery counties.

J.P. Morgan Trust Company National Association, Mortgagee and Trustee named in the foregoing Thirty-Eighth Supplemental Indenture, hereby certifies that its precise name and the post office address of its Institutional Trust Services Group in Philadelphia, Pennsylvania are as follows:

J.P. Morgan Trust Company, National Association
 Institutional Trust Services
 1650 Market Street, Suite 4700
 Philadelphia, PA 19103
 Attention: Pennsylvania Suburban Water
 Administrator

J.P. MORGAN TRUST COMPANY,
NATIONAL ASSOCIATION

By: _____
Authorized Officer

COMMONWEALTH OF PENNSYLVANIA

COUNTY OF MONTGOMERY

On the _____ day of November, 2004, before me, the Subscriber, a Notary Public for the Commonwealth of Pennsylvania, personally appeared Kathy L. Pape, who acknowledged herself to be the Vice President and Treasurer of Aqua Pennsylvania, Inc., a corporation, and that she as such Vice President and Treasurer, being authorized to do so, executed the foregoing Thirty-Eighth Supplemental Indenture as and for the act and deed of said corporation and for the uses and purposes therein mentioned, by signing the name of the corporation by herself as such officer.

In Witness Whereof I hereunto set my hand and official seal.

[NOTARIAL SEAL]

COMMONWEALTH OF PENNSYLVANIA

COUNTY OF PHILADELPHIA

On the _____ day of November, 2004 before me, the Subscriber, a Notary Public for the Commonwealth of Pennsylvania, personally appeared _____, who acknowledged herself to be a _____ of J.P. Morgan Trust Company, National Association, Trustee, a national banking association, and that she as such _____, being authorized to do so, executed the foregoing Thirty-Eighth Supplemental Indenture as and for the act and deed of said national banking association and for the uses and purposes therein mentioned by signing the name of said national banking association by herself as such officer.

In Witness Whereof I hereunto set my hand and official seal.

[NOTARIAL SEAL]

This Thirty-Eighth Supplemental Indenture was recorded in the Office for the Recording of Deeds for each of the counties tabulated below in the Mortgage Book, at the page and on the date indicated:

County	Date	Mortgage Book	Page
-----	----	-----	----
Adams			
Berks.....			
Bradford.....			
Bucks.....			
Carbon.....			
Chester.....			
Columbia.....			
Cumberland.....			
Delaware.....			
Forest.....			
Juniata.....			
Lackawanna.....			
Lawrence.....			
Luzerne.....			
Mercer.....			
Monroe.....			
Montgomery.....			
Northampton.....			
Northumberland.....			

Pike.....
Schuylkill.....
Snyder
Susquehanna
Wayne.....
Wyoming

For the recording information with respect to the Original Indenture and the first thirty-seven supplemental indentures, see Exhibit B of this Thirty-Eighth Supplemental Indenture.

AQUA AMERICA, INC.
AND SUBSIDIARIES
2005 ANNUAL CASH INCENTIVE COMPENSATION PLAN

BACKGROUND

- o In 1989, the Company and its compensation consultant conducted a feasibility study to determine whether the Company should implement an incentive compensation plan. The study was prompted by the positive experience of other investor-owned water companies with incentive compensation.
- o The study included interviews with executives and an analysis of competitive compensation levels. Based on the results, the compensation consultant recommended that the Company's objectives and competitive practice supported the adoption of an annual incentive plan (the "Plan"). The Company has had a cash incentive compensation plan in place since 1990 and management and the Board of Directors believe it has had a positive effect on the Company's operations, aiding employees, shareholders (higher earnings) and customers (better service and controlling expenses).
- o The Plan has two components - a Management Incentive Program and an Employee Recognition ("Chairman's Award") Program.
- o The Plan is designed to provide an appropriate incentive to the officers, managers and certain other key employees of the Company. The 2005 Management Incentive Program will cover officers, managers and certain key employees of Aqua America, Inc., and its subsidiaries.

MANAGEMENT INCENTIVE PROGRAM

o PERFORMANCE MEASURES

- Annual incentive bonus awards are calculated by multiplying an individual's Target Bonus by a Company Rating Factor based on the applicable company's performance and an Individual Rating Factor based on the individual employee's performance.

The approach of having a plan tied to the applicable company's income performance is appropriate as the participants' assume some of the same risks and rewards as the shareholders who are investing in the company and making its capital construction and acquisition programs possible. Customers also benefit from the participants' individual objectives being met, as improvements in performance are accomplished by controlling costs, improving efficiencies and enhancing customer service. For these reasons, future rate relief should be lessened and less frequent, which directly benefits all customers.

- The applicable company's actual after-tax net income from continuing operations or earnings before interest, taxes and depreciation ("EBITD") relative to its annual budget will be the primary measure for the company's performance. The measurement to be used as the Company Factor for each participant will be proposed by the Chairman of the Company and approved by the Executive Compensation Committee. Each year a "Target Net Income or EBITD" level will be established. Starting in 2000, portions of the Company Rating Factor may be tied to the financial targets of more than one company for some participants. For purposes of the Plan, the Target Net Income or EBITD may differ from the budgeted net income or EBITD level. For 2005, the Target Net Income or EBITD will exclude the impact of any unbudgeted extraordinary gains or losses as a result of changes in accounting principles.
- Based on a review of historic performance, the minimum or threshold level of performance is set at 90 percent of the Target Net Income or EBITD. That is, no bonus awards will be

made if actual net income is less than 90 percent of the Target or EBITD for the year. No additional bonus will be earned for results exceeding 110 percent of the Target Net Income or EBITD.

-- Each individual's performance and achievement of his or her objectives will also be evaluated and factored into the bonus calculation (the "Individual Factor"). Performance objectives for each participant are established at the beginning of the year and are primarily directed toward controlling costs, improving efficiencies and productivity, enhancing customer service and growing the company's customer base. Each objective has specific performance measures that are used to determine the level of achievement for each objective. A participant's target Individual Factor should be no more than 90 points, with the possibility of

additional points being awarded for measurable performance above the participant's targeted performance level. Participants must achieve at least 70 points for their Individual Factor to be eligible for a bonus award under the Plan.

o PARTICIPATION

-- Eligible participants consist of officers, managers and certain key employees.

-- Participation in the Management Incentive Program will be determined each year. Each participant will be assigned a "Target Bonus Percentage" ranging from 5 to 70 percent depending on duties and responsibilities.

-- For each company, the Target Bonus Percentage for all the participants within that company will be applied to their base salary.

-- Actual bonuses may range from 0, if the company's financial results fall below the minimum threshold or the participant does not make sufficient progress toward achieving his or her objectives (i.e. performance measure points totaling less than 70 points), to 187.5 percent if performance -- both Company and individual -- is rated at the maximum.

-- New employees who are hired into a position that is eligible to participate in the Management Incentive Plan, will normally be eligible to receive a portion of the bonus calculated in accordance with this Plan that is pro-rated based on the number of full calendar months between the new employee's hire date and the end of the calendar year.

-- Employees who would otherwise be eligible to participate in this Management Incentive Plan, but who leave employment with the company either voluntarily, involuntarily or as a result of retirement, will not receive a bonus for the year in which their employment terminates. If an employee who would otherwise be eligible to participate in this Management Incentive Plan dies, the company will pay the deceased employee's estate a portion of the bonus the deceased employee would otherwise have been entitled to assuming a 100% Individual Rating Factor, but pro-rated for the number of full calendar months the employee completed before his or her death.

o COMPANY PERFORMANCE

-- Company performance will be measured on the following schedule:

	Percent of Target -----	Company Rating -----
Threshold.....	<90%	0%
	90	50

	92	65
	95	80
	96	85
	97	90
	98	94
	99	97
Plan.....	100	100
	105	110
	>110	125

-- The actual Company Factor should be calculated by interpolation between the points shown in the table above.

-- Regardless of the Company rating resulting from this Schedule, the Executive Compensation and Employee Benefits Committee retains the authority to determine the final Company Rating for purposes of this Plan.

o INDIVIDUAL PERFORMANCE

-- Individual performance will be measured on the following scale:

Performance Measure Points	Individual Rating Factor
-----	-----
0 - 69	0%
70	70%
80	80%
90	90%
100	100%
110	110%

-- In addition, up to 40 additional points and additional percentage points may be awarded to a participant at the discretion of the Chief Executive Officer for exemplary performance. Individual performance points for the Chief Executive Officer are determined by the Executive Compensation and Employee Benefits Committee.

SAMPLE CALCULATIONS

o Example 1

Salary or	\$ 70,000
Target Bonus	10 percent (\$7,000)
Company Rating	100 percent
Individual Rating	90 percent

Calculation:

Target Bonus	x	Rating	x	Company Rating	=	Individual Bonus Earned
-----		-----		-----		-----
\$7,000	x	100%	x	90%	=	\$6,300
						=====

o Example 2

-- Using the same salary and target bonus, but assuming Company performance was less than 90 percent of Target EBITD, there would be no bonus earned.

Calculation:

$$\$7,000 \times 0 \times 90\% = 0$$

o Example 3

-- Similarly, if the Individual Factor is rated below 70 points, no bonus would be earned regardless of the Company Factor.

Calculation:

$$\$7,000 \times 100\% \times 0 = 0$$

o Example 4

-- If the Company Rating Factor is allocated between two companies, the bonus will be calculated separately based on the allocation.

Calculation:

Target Bonus	x	Company Rating	x	Company Allocation	x	Individual Rating	=	Bonus Earned
-----		-----		-----		-----		-----
\$7,000	x	100%	x	20%	x	90%	=	\$1,260
\$7,000	x	110%	x	80%	x	90%	=	\$5,544

Total Bonus							=	\$6,804

o Example 5

-- It is also possible that one portion of the applicable Company Rating Factor is zero, for which there would be no bonus, regardless of the participant's Individual Rating Factor.

Calculation:

Target Bonus	x	Company Rating	x	Company Allocation	x	Individual Rating	=	Bonus Earned
-----		-----		-----		-----		-----
\$7,000	x	0%	x	20%	x	90%	=	\$0
\$7,000	x	110%	x	80%	x	90%	=	\$5,544

Total Bonus							=	\$5,544

EMPLOYEE RECOGNITION ("CHAIRMAN'S AWARD") PROGRAM

1. In addition to the Management Incentive Program, the Company maintains an Employee Recognition Program known as the Chairman's Award program to reward non-union employees not eligible for the management bonus plan for superior performance that contains costs, improves efficiency and productivity of the workforce and better serves our customers. Awards may also be made for a special action or heroic deed, or for a project that positively impacts the performance or image of the Company.
2. Awards will be made from an annual pool designated by the Chairman of Aqua America with the approval of the Executive Compensation and Employee Benefits Committee. Unused funds will not be carried over to the next year. If financial performance warrants, management may request permission from the Executive Compensation and Employee Benefits Committee for special awards under the program.
3. In general, Chairman's Awards will not be made to employees of a company that does not achieve at least 90% of its net income objective for the year.
4. Awards may be made throughout the year, however, no more than one-third of a company's Chairman's Award pool may be awarded until the company's final net income for the year is determined.
5. Nominations for employees to receive Chairman's Awards will be made to the applicable officer and should include documentation on the reasons for the recommendations. The applicable officer will review the nominations and forward their recommendations to the Chairman of Aqua America.
6. The Chairman will determine the individuals to actually receive a bonus and the amount. The maximum award to any one employee is \$5,000.

BOND PURCHASE AGREEMENT

\$14,000,000
NORTHUMBERLAND COUNTY INDUSTRIAL DEVELOPMENT AUTHORITY

WATER FACILITIES REVENUE REFUNDING BONDS
(AQUA PENNSYLVANIA, INC. PROJECT)
SERIES OF 2004

Bond Purchase Agreement dated November 16, 2004, among the NORTHUMBERLAND COUNTY INDUSTRIAL DEVELOPMENT AUTHORITY (the "Authority"), AQUA PENNSYLVANIA, INC., a Pennsylvania corporation (the "Company"), and SOVEREIGN SECURITIES CORPORATION, LLC, a Pennsylvania limited liability company, (the "Underwriter").

1. BACKGROUND.

(a) The Authority proposes to enter into a Financing Agreement (the "Financing Agreement") dated as of November 15, 2004 with the Company, under which the Authority will agree to loan to the Company funds to currently refund (the "Project") the Authority's Exempt Facilities Revenue Bonds (Roaring Creek Water Company Project) Series of 1993 (the "1993 Bonds"), which were issued to finance the construction of an eight (8) million gallon per day treatment facility, an interconnecting water main, and laboratory and service facilities, located in Northumberland and Columbia Counties (collectively, the "Facilities") and pay all costs of issuance of the 1993 Bonds. To finance the loan under the Financing Agreement, the Authority proposes to issue and sell \$14,000,000 aggregate principal amount of Northumberland County Industrial Development Authority Water Facilities Revenue Refunding Bonds, (Aqua Pennsylvania, Inc. Project) Series of 2004 (the "2004 Bonds") to the Underwriter, who will in turn reoffer the 2004 Bonds for sale to the public.

(b) The 2004 Bonds will be issued pursuant to the Pennsylvania Economic Development Financing Law, Act of August 23, 1967, P.L. 251, as amended and supplemented (the "Act"), resolutions adopted by the Authority on September 20, 2004 (the "Authority Resolution") and under a Trust Indenture dated as of November 15, 2004 (the "Trust Indenture"), between the Authority and Wachovia Bank, National Association, as trustee (the "Trustee"). The 2004 Bonds will have such terms as are set forth in Schedule I attached hereto.

The 2004 Bonds will be payable out of payments by the Company under the Financing Agreement, including payments under its First Mortgage Bond issued with respect to the 2004 Bonds in the principal amount of \$14,000,000 (the "First Mortgage Bond"). The First Mortgage Bond will be issued under and secured by the Company's Indenture of Mortgage dated as of January 1, 1941 (the "Indenture of Mortgage"), from the Company to J.P. Morgan Trust Company, National Association, as trustee (successor to The Pennsylvania Company for Insurance on Lives and Granting Annuities, The Pennsylvania Company for Banking and Trusts, The First Pennsylvania Banking and Trust Company, First Pennsylvania Bank, N.A., CoreStates Bank, N.A., Mellon Bank, N.A. and Chase Manhattan Trust Company, National Association)

(the "Mortgage Trustee"), as presently amended and supplemented and as to be further supplemented by a Thirty-Eighth Supplemental Indenture of Mortgage to be dated as of November 15, 2004 (the "Thirty-Eighth Supplemental Mortgage," which together with the Indenture of Mortgage, as amended and supplemented, is referred to hereinafter as the "Mortgage"). The First Mortgage Bond will be issued in the same principal amount and will mature on the date and bear interest at the rate of the 2004 Bonds that it secures. All of the Authority's rights under the Financing Agreement to receive and enforce repayment of its loan to the Company and to enforce payment of the 2004 Bonds, including all of the Authority's rights to the First Mortgage Bond, and all of the Authority's rights to moneys and securities in the Project Fund, the Revenue Fund and the Debt Service Fund (and the accounts within all such Funds applicable to the 2004 Bonds) established by the Trust Indenture, except for the Authority's rights to certain fees and reimbursements for expenses, indemnification and notice thereunder and rights relating to amendments of and notices under the Financing Agreement, will be assigned to the Trustee as security for the 2004 Bonds

pursuant to the Trust Indenture.

(c) The Project will refinance the acquisition, construction, installation and equipping of facilities for the furnishing of water for purposes of Section 142(a)(4) of the Internal Revenue Code of 1986, as amended (the "Code"), so that the interest on the Bonds will not be includable in gross income for federal income tax purposes under the Code and the Underwriter may offer the 2004 Bonds for sale without registration under the Securities Act of 1933, as amended (the "1933 Act") or qualification of the Trust Indenture under the Trust Indenture Act of 1939, as amended (the "1939 Act").

(d) A Preliminary Official Statement dated November 9, 2004, including the Appendices thereto and all documents incorporated therein by reference (the "Preliminary Official Statement"), has been supplied to the parties hereto, and a final Official Statement to be dated as of the date hereof, including the Appendices thereto and all documents incorporated therein by reference, prepared for use in such offerings will be supplied to the parties hereto as soon as it is available, subject to Section 10 hereof (such final Official Statement, as it may be amended or supplemented with the consent of the Authority, the Underwriter and the Company, is hereinafter referred to as the "Official Statement").

2. PURCHASE, SALE AND CLOSING. On the terms and conditions herein set forth, the Underwriter will buy from the Authority, and the Authority will sell to the Underwriter, all (but not less than all) of the 2004 Bonds at a purchase price equal to \$14,000,000, consisting of the aggregate principal amount of the 2004 Bonds. The Underwriter will be paid an Underwriting fee of \$210,000.00 by the Company for its services rendered under this Agreement. Payment shall be made in immediately available funds to the Trustee for the account of the Authority. Closing (the "Closing") will be at the offices of Ballard Spahr Andrews & Ingersoll, LLP, Philadelphia, Pennsylvania bond counsel, at 10:00 a.m., Eastern Daylight Time, on November 30, 2004 or at such other date, time or place or in such other manner as may be agreed on by the parties hereto. The 2004 Bonds will be delivered as a single, fully registered Bond, in the aggregate principal amount of the Bonds for in the name of Cede & Co., as nominee for The Depository Trust Company ("DTC"), with a CUSIP number printed thereon, and shall conform in all respects to DTC's Book-Entry Only System. Delivery of the 2004 Bonds will be made at the office of DTC in New York, New York (or such other location as is acceptable to the Underwriter). If the Underwriter so requests, the 2004 Bonds shall be made available to the

Underwriter (prior to their delivery to DTC) in Philadelphia, Pennsylvania at least three full business days before the Closing for purposes of inspection.

The Underwriter agrees to make a bona fide public offering of the 2004 Bonds at the initial offering prices or yields set forth in the Official Statement; provided, however, that the Underwriter reserves the right (and the Authority and the Company hereby expressly acknowledge such right): (i) to make concessions to dealers; (ii) to effect transactions that stabilize or maintain the market price of the 2004 Bonds above that which might otherwise prevail in the open market and to discontinue at any time such stabilizing transactions; and (iii) to change such initial offering prices, all as the Underwriter shall deem necessary in connection with the marketing of the 2004 Bonds.

3. AUTHORITY'S REPRESENTATIONS AND WARRANTIES. The Authority makes the following representations and warranties, all of which shall survive Closing; that:

(a) The Authority is a body politic and corporate, duly created and existing under the Constitution and laws of the Commonwealth of Pennsylvania (the "Commonwealth"), and has, and at the date of Closing will have, full legal right, power and authority to: (i) enter into this Bond Purchase Agreement; (ii) execute and deliver the 2004 Bonds, the Trust Indenture, the Financing Agreement, and the Authority's tax certificate and the other various certificates executed by the Authority in connection therewith (collectively, with the Authority Resolution, the "Authority Financing Documents"); (iii) issue, sell and deliver the 2004 Bonds to the Underwriter as provided herein; and (iv) carry out and consummate the transactions contemplated by the Authority Financing Documents and the Official Statement to be carried out and/or consummated by it;

(b) The Authority Resolution was duly adopted at a public meeting of the Authority at which a quorum was present and acted throughout; and

the Authority Resolution is in full force and effect and has not been amended, repealed or superseded in any way.

(c) The sections entitled "INTRODUCTORY STATEMENT" (insofar as it relates to the Authority) and "THE AUTHORITY" contained in the Preliminary Official Statement as of its date did not contain any untrue statement of a material fact or omit to state any material fact required to be stated therein or necessary in order to make the statements contained therein, in the light of the circumstances under which they were made, not misleading;

(d) The sections entitled "INTRODUCTORY STATEMENT" (insofar as it relates to the Authority) and "THE AUTHORITY" contained in the Official Statement as of its date does not or will not contain any untrue statement of a material fact or omit to state any material fact required to be stated therein or necessary in order to make the statements contained therein, in the light of the circumstances under which they were made, not misleading;

(e) The Authority has complied, and will at the Closing be in compliance, in all material respects with the provisions of the Act;

(f) To the extent required by law, the Authority has duly authorized and approved the Preliminary Official Statement and the Official Statement; and has duly authorized

and approved the execution and delivery of, and the performance by the Authority of the obligations on its part contained in, the Authority Financing Documents;

(g) To the best of the knowledge of the officer of the Authority executing this Bond Purchase Agreement, the Authority is not in material breach of or in default under any applicable law or administrative regulation of the Commonwealth or the United States; and the execution and delivery of the Authority Financing Documents, and compliance with the provisions of each thereof, do not and will not conflict with or constitute a breach of or default under any existing law, administrative regulation, judgment, decree, loan agreement, note, resolution, agreement or other instrument to which the Authority is a party or is otherwise subject;

(h) All approvals, consents and orders of any governmental authority, board, agency or commission having jurisdiction that would constitute a condition precedent to the Authority's legal ability to issue the 2004 Bonds or to the Authority's performance of its obligations hereunder and under the Authority Financing Documents have been obtained or will be obtained prior to the Closing;

(i) The 2004 Bonds, when issued, authenticated and delivered in accordance with the Trust Indenture and sold to the Underwriter as provided herein, will be validly issued and will be valid and binding limited obligations of the Authority enforceable against the Authority in accordance with their terms (except as enforcement of remedies may be limited by bankruptcy, insolvency, reorganization, moratorium or other laws or legal or equitable principles affecting the enforcement of creditors' rights ("Creditors' Rights Limitations"));

(j) The terms and provisions of the Authority Financing Documents when executed and delivered by the respective parties thereto will constitute the valid, legal and binding obligations of the Authority enforceable against the Authority in accordance with their respective terms (except as enforcement of remedies may be limited by Creditors' Rights Limitations);

(k) There is no action, suit, proceeding, inquiry or investigation, at law or in equity, before or by any court, or public board or body, pending or, to the knowledge of the Authority after due inquiry, threatened against the Authority, affecting the existence of the Authority or the titles of its officers to their respective offices or seeking to prohibit, restrain or enjoin the sale, issuance or delivery of the 2004 Bonds or of the revenues or assets of the Authority pledged or to be pledged to pay the principal of and interest on the 2004 Bonds, or the pledge thereof, or in any way contesting or affecting the validity or enforceability of the Authority Financing Documents or contesting in any way the completeness or accuracy of the Preliminary Official Statement or the Official Statement, or contesting the power or authority of the Authority with respect to the issuance of the 2004 Bonds or the execution, delivery or performance of any of the Authority Financing Documents, wherein an unfavorable decision, ruling or finding would

affect in any way the validity or enforceability of any of the Authority Financing Documents;

(l) The net proceeds received from the 2004 Bonds and applied in accordance with the Trust Indenture and Financing Agreement shall be used in accordance with the Act as described in the Official Statement;

(m) The Authority has not been notified of any listing or proposed listing by the Internal Revenue Service to the effect that the Authority is a bond issuer whose arbitrage certifications may not be relied upon; and

(n) Any certificate signed by any of the authorized officers of the Authority and delivered to the Underwriter shall be deemed a representation and warranty by the Authority to the Underwriter as to the statements made therein.

4. COMPANY'S REPRESENTATIONS AND WARRANTIES. The Company makes the following representations and warranties, all of which will survive the Closing:

(a) The Company has not sustained since September 30, 2004 any material loss or interference with its business from fire, explosion, flood or other calamity, whether or not covered by insurance, or from any labor dispute or court or governmental action, order or decree; and since the respective dates as of which information is given in the Official Statement, there have not been any material changes in the outstanding capital stock or the long-term debt of the Company or any material adverse change, or a development involving a prospective material adverse change, in or affecting the general affairs, management, financial position, stockholders' equity or results of operations of the Company, otherwise than as set forth or contemplated in the Official Statement.

(b) The Company was organized, is in good standing and subsists as a corporation under the laws of the Commonwealth, with power (corporate and other) to own its properties and conduct its business as described in the Official Statement.

(c) Each First Mortgage Bond has been duly authorized; and, when issued and delivered as contemplated by this Bond Purchase Agreement, will have been duly executed, authenticated, issued and delivered and will constitute a valid and legally binding obligation of the Company entitled to the benefits provided by the Mortgage.

(d) The Original Indenture has been duly authorized, executed and delivered by the Company, and the Thirty-Eighth Supplemental Mortgage has been duly authorized by the Company. When the Thirty-Eighth Supplemental Mortgage, in substantially the form approved by the Company, has been executed and delivered by the Company and assuming due authorization and execution by the Mortgage Trustee, and recorded as required by law, the Mortgage (i) will constitute a valid and legally binding instrument enforceable against the Company in accordance with its terms except as enforceability may be limited by Creditors' Rights Limitations; (ii) will constitute a direct, valid and enforceable first mortgage lien (except as enforceability of such lien may be limited by Creditors' Rights Limitations) upon all of the properties and assets of the Company (not heretofore released as provided for in the Mortgage) specifically or generally described or referred to in the Mortgage as being subject to the lien thereof, excepting permitted liens under the Mortgage and excepting property and assets that the Mortgage expressly excludes from the lien thereof; and (iii) and will create a mortgage upon all

properties and assets acquired by the Company after the execution and delivery of the Thirty-Eighth Supplemental Mortgage and required to be subjected to the lien of the Mortgage pursuant thereto when so acquired, except for permitted liens under the Mortgage. The Original Indenture has been and the Thirty-Eighth Supplemental Mortgage will be duly filed, recorded or registered in each place in the Commonwealth in which such filing, recording or registration was or is required to protect and preserve the lien of the Mortgage; and all necessary approvals of regulatory authorities, commissions and other governmental bodies having jurisdiction over the Company required to subject the mortgaged properties and assets or trust estate (as defined in the Mortgage) to the lien of the Mortgage have been duly obtained.

(e) In each of the following cases with such exceptions as are not material and do not interfere with the conduct of the business of the Company, the Company has good and marketable title to (i) all of its real property currently held in fee simple; and (ii) all of its other interests in real property (other than certain rights of way, easements, occupancy rights, riparian and flowage rights, licenses, leaseholds, and real property interests of a similar nature). In each case such title is free and clear of all liens, encumbrances and defects except such as may be described in the Official Statement, the lien of the Mortgage, permitted liens under the Mortgage or such as do not materially affect the value of such property and do not interfere with the use made and proposed to be made of such property by the Company. Any real property and buildings held under lease by the Company are held by it under valid, subsisting and enforceable leases with such exceptions as are not material and do not interfere with the use made and proposed to be made of such property and buildings by the Company.

(f) In each of the following cases except for such exceptions that are not material and do not interfere with the conduct of the business of the Company, the Company has all licenses, franchises, permits, authorizations, rights, approvals, consents and orders of all governmental authorities or agencies necessary for the ownership or lease of the properties owned or leased by it and for the operation of the business carried on by it as described in the Official Statement, and all water rights, riparian rights, easements, rights of way and other similar interests and rights described or referred to in the Mortgage necessary for the operation of the business carried on by it as described in the Official Statement. Except as otherwise set forth in the Official Statement, all such licenses, franchises, permits, orders, authorizations, rights, approvals and consents are in full force and effect and contain no unduly burdensome provisions; except as otherwise set forth in the Official Statement, there are no legal or governmental proceedings pending or, to its knowledge after due inquiry, threatened that would result in a material modification, suspension or revocation thereof. The Company has the legal power to exercise the rights of eminent domain for the purposes of conducting its water utility operations.

(g) The issue and sale of the 2004 Bonds, the issue and delivery of the First Mortgage Bond and the compliance by the Company with all of the applicable provisions of the First Mortgage Bond and the Mortgage and the execution, delivery and performance by the Company of the Thirty-Eighth Supplemental Mortgage, the Financing Agreement, this Bond Purchase Agreement and the Continuing Disclosure Agreement will not conflict with or result in a breach of any of the terms or provisions of, or constitute a default under, or result in the creation or imposition of any lien, charge or encumbrance (other than the lien of the Mortgage) upon any of the property or assets of the Company pursuant to the terms of any indenture, mortgage, deed of trust, loan agreement or other agreement or instrument to which the Company

is a party or by which the Company is bound or to which any of the property or assets of the Company are subject, nor will such action result in a violation of the provisions of the Articles of Incorporation, as amended, or the Bylaws of the Company or any statute or any order, rule or regulation of any court or governmental agency or body having jurisdiction over the Company or any of its property. No consent, approval, authorization, order, registration or qualification of or with any court or any such regulatory authority or other governmental body (other than those already obtained) is required for the issue and sale of the 2004 Bonds, the issue and delivery of the First Mortgage Bond, the execution, delivery and performance by the Company of this Bond Purchase Agreement, the Financing Agreement, the Thirty-Eighth Supplemental Mortgage, the First Mortgage Bond and the Continuing Disclosure Agreement, or the consummation by the Company of the other transactions contemplated by this Bond Purchase Agreement or the Mortgage.

(h) The Pennsylvania Public Utility Commission by order has duly authorized the issuance and delivery of the First Mortgage Bond on terms not inconsistent with this Bond Purchase Agreement.

(i) The Company is not a holding company, a registered holding company or an affiliate of a registered holding company within the meaning of the Public Utility Holding Company Act of 1935, as amended.

(j) There are no legal or governmental proceedings pending to which the Company is a party or to which any property of the Company is

subject, other than as set forth in the Official Statement and other than litigation incident to the kind of business conducted by the Company, wherein an unfavorable ruling, decision or finding is likely that would have a material adverse effect on the financial position, stockholders' equity or results of operations of the Company; and, to the best of the Company's knowledge after due diligence, no such proceedings are threatened by governmental authorities or threatened by others.

(k) (i) The Project consists of either land or property of a character subject to depreciation for federal income tax purposes and will be used to furnish water that is or will be made available to members of the general public (including electric utility, industrial, agricultural, or commercial users); (ii) the rates for the furnishing or sale of the water have been established or approved by a State or political subdivision thereof, by an agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof; and (iii) all other information supplied by the Company to the Underwriter with respect to the exclusion from gross income pursuant to Section 103 of the Code of the interest on the 2004 Bonds is correct and complete;

(l) The Company has not, within the immediately preceding ten (10) years, defaulted in the payment of principal or interest on any of its bonds, notes or other securities, or any legally authorized obligation issued by it; and

(m) The information with respect to the Company and the Project and the descriptions of the First Mortgage Bond and the Mortgage contained in the Preliminary Official Statement and the Official Statement (including appendices A and B thereto) do not contain an untrue statement of a material fact or omit to state a material fact necessary to make such

information and descriptions, in the light of the circumstances under which they were made, not misleading.

5. AUTHORITY'S COVENANTS. The Authority will:

(a) furnish such information, execute such instruments and take such other action in cooperation with the Underwriter as the Underwriter may reasonably request to qualify the 2004 Bonds for offer and sale under the Blue Sky or other securities laws and regulations of such states and other jurisdictions in the United States of America as the Underwriter may designate and will assist, if necessary therefor, in the continuance of such qualifications in effect so long as required for distribution of the 2004 Bonds; provided, however, that the Authority shall in no event be required to file a general consent to suit or service of process or to qualify as a foreign corporation or as a dealer in securities in any such state or other jurisdiction;

(b) not, on its part, amend or supplement the Official Statement without prior notice to and the consent of the Underwriter and the Company and will advise the Underwriter and the Company promptly of the institution of any proceedings by any governmental agency or otherwise affecting the use of the Official Statement in connection with the offer and sale of the 2004 Bonds; and

(c) refrain from knowingly taking any action (and permitting any action with regard to which the Authority may exercise control) which would result in the loss of the exclusion from gross income for federal income tax purposes of interest on the 2004 Bonds referred to under the caption "TAX MATTERS" in the Official Statement.

6. COMPANY'S COVENANTS. The Company agrees that it will:

(a) refrain from knowingly taking any actions (and from permitting any action; with regard to which the Company may exercise control) that would result in the loss of the exclusion from gross income for federal tax purposes of interest on the 2004 Bonds;

(b) indemnify and hold harmless the Authority, its members, directors, officers, agents, attorneys, and employees and the Underwriter, its officers, directors, officials, agents, attorneys, employees, and each person, if any, who controls the Underwriter within the meaning of Section 15 of the 1933 Act or Section 20 of the Securities Exchange Act of 1934, as amended (the

"1934 Act"), from and against all losses, claims, damages, liabilities and expenses, joint or several, to which the Authority and the Underwriter, or either of them, or any of their respective members, directors, officers, agents, attorneys, and employees and each person, if any, who controls the Underwriter within the meaning of the 1933 Act or 1934 Act as aforescribed may become subject, under federal laws or regulations, or otherwise, insofar as such losses, claims, damages, liabilities and expenses (or actions in respect thereof) arise out of or are based upon: (i) a breach of the Company's representations included in this Agreement; (ii) any untrue statement or alleged untrue statement of any material fact pertaining to the Project or the Company set forth in the Official Statement, the Preliminary Official Statement or any amendment to either, or (iii) the willful or negligent omission of (or the alleged omission to state) a material fact in the Official Statement, in the Preliminary Official Statement, or in any amendment or supplement to either, as such fact is required to be stated therein or necessary to

make the statements therein that pertain to the Company or the Project not misleading in the light of the circumstances under which they were made, or (iv) arising by virtue of the failure to register the 2004 Bonds under the 1933 Act or the failure to qualify the Indenture under the 1939 Act;

(c) undertake, pursuant to the Continuing Disclosure Agreement dated November 15, 2004 to be entered into between the Company and the Trustee (the "Continuing Disclosure Agreement"), to provide annual reports and notices of certain material events in accordance with Rule 15c2-12 under the 1934 Act, as amended ("Rule 15c2-12"). A description of this undertaking and the Continuing Disclosure Agreement is set forth in the Preliminary Official Statement and will also be set forth in the Final Official Statement; and

(d) not amend or supplement the Official Statement without prior notice to, and the consent of, the Underwriter, and will advise the Underwriter and the Authority promptly of the institution of any proceedings by any governmental agency or otherwise affecting the use of the Official Statement in connection with the offer and the sale of the 2004 Bonds.

7. UNDERWRITER'S COVENANT. By acceptance hereof the Underwriter agrees to indemnify and hold harmless the Authority, its members, directors, officers, agents, attorneys, and employees and the Company, its officers, directors, agents, attorneys, and employees and each person if any, who controls the Company within the meaning of Section 15 of the 1933 Act against all or several claims, losses, damages, liabilities and expenses asserted against them, or any of them, at law or in equity, in connection with (i) the offering and sale of the 2004 Bonds on the grounds that the information under the caption "UNDERWRITING" in the Preliminary Official Statement or the Official Statement (or any supplement or amendment to said information) contains an untrue or allegedly untrue statement of a material fact or omits or allegedly omits to state any material fact necessary to make the statements therein not misleading in the light of the circumstances under which they were made (it being understood that the Underwriter furnished only the information under such "UNDERWRITING" heading), or (ii) failure on the part of the Underwriter to deliver an Official Statement to any purchaser. The Underwriter will reimburse any legal or other expenses reasonably incurred by a party, person or entity indemnifiable under this Section 7 in connection with investigating or defending any such loss, claim, damage, liability or action. This indemnity agreement will be in addition to any liability that the Underwriter may otherwise have. The Underwriter shall not be liable for any settlement of, any such action effected without its consent.

8. NOTICE OF INDEMNIFICATION; SETTLEMENT. Promptly after a party, person or entity indemnifiable under Section 6 or 7 of this Bond Purchase Agreement (an "Indemnatee") receives notice of the commencement of any action against such Indemnatee in respect of which indemnity is to be sought by the Indemnatee against the Company or an Underwriter, as the case may be (the "Indemnifying Party"), the Indemnatee will notify the Indemnifying Party in writing of such action, and the Indemnifying Party may assume the defense thereof, including the employment of counsel and the payment of all expenses; but the omission so to notify the Indemnifying Party will not relieve the Indemnifying Party from any liability that it may have to the Indemnatee otherwise than hereunder. The Indemnifying Party shall not be liable for any settlement of any such action effected without its consent, but if settled with the consent of the Indemnifying Party or if there is a final judgment for the plaintiff in any such action, the

Indemnifying Party will indemnify and hold harmless the Indemnitee from and against any loss or liability by reason of such settlement or judgment. The indemnity agreements contained in this Bond Purchase Agreement (i) shall include reimbursement for expenses reasonably incurred by an Indemnitee in investigating the claim and in defending it if the Indemnifying Party declines to assume the defense and (ii) shall survive delivery of the 2004 Bonds.

9. **EQUITABLE CONTRIBUTION.** If the indemnification provided for in Section 6(b) of this Bond Purchase Agreement is unavailable to the Underwriter (or any controlling person thereof) in respect of any losses, claims, damages or liabilities referred to therein, then the Company shall, in lieu of indemnifying the Underwriter, contribute to the amount paid or payable by the Underwriter as a result of such losses, claims, damages or liabilities in such proportion as is appropriate to reflect the relative benefits received by the Company and the Underwriter, respectively, from the offering of the 2004 Bonds. If, however, the allocation provided by the immediately preceding sentence is not permitted by applicable law, then the Company shall contribute to such amount paid or payable by the Underwriter in such proportion as is appropriate to reflect not only such relative benefits but also the relative fault of the Company and the Underwriter, respectively, in connection with the statements or omission which resulted in such losses, claims, damages or liabilities, as well as any other relevant equitable considerations. The relative benefit received by the Company or the Underwriter shall be deemed to be in the same proportion as the total proceeds from the offering (before deducting issuance costs and expenses other than underwriting fees and commissions) received by the Company, on the one hand, bear to the total underwriting fees and commissions received by the Underwriter, on the other hand. The relative fault shall be determined by reference to, among other things, whether the untrue or alleged untrue statement of a material fact or the omission or alleged omission to state a material fact related to information supplied by the Company or the Underwriter and the parties' relative intent, knowledge, access to information and opportunity to correct or prevent such statement or omission. The Company and the Underwriter agree that it would not be just and equitable if contribution pursuant to this Section 9 were determined by pro rata allocation or by any other method of allocation that does not take account of the equitable considerations referred to above in this Section 9. The amount paid or payable by the Underwriter as a result of the losses, claims, damages or liabilities referred to above in this Section 9 shall be deemed to include any reasonable legal or other expenses reasonably incurred by the Underwriter in connection with investigating or defending any such action or claim. Notwithstanding the provisions of this Section 9, the Underwriter shall not be required to contribute any amount in excess of the amount by which the total price at which the 2004 Bonds underwritten by it and distributed to the public were offered to the public exceeds the amount of any damages that the Underwriter has otherwise been required to pay by reason of such untrue or allegedly untrue statement or omission or alleged omission.

10. **OFFICIAL STATEMENT; PUBLIC OFFERING.**

(a) In order to enable the Underwriter to comply with Rule 15c2-12: (i) the Company has prepared (or caused to be prepared) the Preliminary Official Statement, which the Company and the Authority (but, in the case of the Authority, only with respect to the information therein under the headings "THE AUTHORITY" and, insofar as it relates to the Authority, "INTRODUCTORY STATEMENT") deem final and complete as of its date except for certain "Permitted Omissions" as described in Rule 15c2-12; (ii) the Company shall provide

to the Underwriter sufficient copies of the Official Statement in sufficient time to accompany any confirmation that requires payment from any customer and in any event within seven business days after the date of this Bond Purchase Agreement; and (iii) if the Company has or gains knowledge that would render the Official Statement misleading in any material respect in the period from the date of its delivery to the Underwriter by the Company (as that phrase is defined in Rule 15c2-12) then the Company shall promptly give the Underwriter notice thereof. The Authority and the Company hereby authorize the use of the Preliminary Official Statement and the Official Statement by the Underwriter in connection with the offering of the 2004 Bonds.

(b) After the Closing, and until the Underwriter has informed the Authority and the Company that the Underwriter has sold all the 2004 Bonds, the Authority and the Company will not adopt or distribute any amendment of or supplement to the Official Statement, except with the prior

written consent of the Underwriter; and if any event relating to or affecting the Authority, the Company or the 2004 Bonds shall occur, the result of which shall make it necessary, in the opinion of the Underwriter, to amend or supplement the Official Statement in order to make it not misleading in the light of the circumstances existing at that time, the Company shall forthwith prepare, and the Company and the Authority shall approve for distribution, a reasonable number of copies of an amendment of or supplement to the Official Statement, in form and substance reasonably satisfactory to the Underwriter, so that the Official Statement then will not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements therein, in the light of the circumstances existing at that time, not misleading. The Authority shall cooperate with the Company in the issuance and distribution of any such amendment or supplement.

(c) Upon Closing, the Underwriter shall promptly provide a Nationally Recognized Municipal Securities Information Repository ("NRMSIR") and the Municipal Securities Rulemaking Board ("MSRB") with a copy of the Official Statement for filing in accordance with Rule 15c2-12, and inform the Authority and the Company in writing as to (i) the date and place of such filing and (ii) the date of the end of the underwriting period.

11. CONDITIONS OF UNDERWRITER'S AND AUTHORITY'S OBLIGATIONS. The Underwriter's obligations to purchase and pay for the 2004 Bonds and the Authority's obligation to issue and deliver the 2004 Bonds are subject to fulfillment of the following conditions at or before Closing:

(a) The representations of the Authority and the Company herein shall be true in all material respects on and as of the date of the Closing and shall be confirmed by appropriate certificates at Closing;

(b) Neither the Authority nor the Company shall be in default in the performance of any of their respective covenants herein;

(c) The Underwriter shall have received:

(i) An opinion of Ballard Spahr Andrews & Ingersoll, LLP, Bond Counsel, dated the date of Closing, substantially in the form attached as Exhibit A hereto,

addressed to (or with reliance letters delivered in respect of) the Authority, the Trustee and the Underwriter;

(ii) An opinion of Ballard Spahr Andrews & Ingersoll, LLP, Bond Counsel, dated the date of Closing, substantially in the form attached as Exhibit B hereto, addressed to the Underwriter;

(iii) An opinion of Garrigan & Rosini, counsel for the Authority, dated the date of Closing, with respect to the matters set forth in Exhibit C hereto, addressed to the Underwriter and in form and substance reasonably satisfactory to the Underwriter and Bond Counsel;

(iv) Opinions of Dilworth Paxson LLP, counsel to the Company, and the Company's Senior Vice President - Law and Administration, dated the date of Closing, substantially in the forms attached as Exhibit D hereto, addressed to the Underwriter, the Authority and Bond Counsel, in form and substance reasonably satisfactory to the Underwriter and to Bond Counsel;

(v) An opinion of Duane Morris LLP and Booth & Tucker, LLP, co-counsel for the Underwriter, in form and substance reasonably satisfactory to the Underwriter;

(vi) An opinion of legal counsel to the "Bond Insurer" in form and substance reasonably satisfactory to Bond Counsel and the Underwriter, relating to the enforceability of a municipal bond insurance policy from the Bond Insurer (the "Bond Insurance Policy") and the information concerning the Bond Insurer in the Official Statement;

(vii) An agreed upon procedures letter dated the date of the Official Statement and addressed to the Company from the Company's auditor with respect to financial information set forth in Appendix A to the Official Statement, in form and substance reasonably satisfactory to the Underwriter;

(viii) A certificate dated the date of Closing executed by the Chairman of the Authority to the effect that:

(A) the representations and warranties of the Authority contained herein, to the best of the knowledge of such Chairman, are true and correct in all material respects as of the date of Closing; and

(B) to the best of the knowledge of such Chairman, the Authority has complied in all material respects with all agreements executed by the Authority in connection with issuance of the 2004 Bonds and satisfied in all material respects the Authority's covenants contained in Section 5 herein and all of the conditions on its part to be performed or satisfied at or prior to the Closing;

(ix) A certificate dated the date of Closing executed by the chief financial officer of the Company to the effect that:

(A) the representations and warranties of the Company in this Bond Purchase Agreement are true and correct in all material respects as of the date of Closing;

(B) the Preliminary Official Statement and the Official Statement, as of their respective dates, insofar as they relate to the Company, do not contain any untrue statement of a material fact or omit to state any material fact required to be stated therein or necessary to make the statements therein, under the circumstances in which they were made, not misleading in any respect; and

(C) no event affecting the Company has occurred since the date of the Bond Purchase Agreement that is required to be disclosed in the Official Statement in order to make the statements and information therein not misleading in any material respect;

(x) Two executed copies of the Trust Indenture, the Financing Agreement, the Bond Purchase Agreement, the Thirty-Eighth Supplemental Mortgage and the Continuing Disclosure Agreement;

(xi) Two copies of the Articles of Incorporation and By-laws of the Company, as amended to the date of Closing, and of the resolutions of the Board of Directors of the Company authorizing and approving the execution and delivery of this Bond Purchase Agreement, the Financing Agreement, the First Mortgage Bond, the Thirty-Eighth Supplemental Mortgage, the Continuing Disclosure Agreement and the incurrence of indebtedness with respect thereto and all transactions described in the Official Statement and contemplated by this Bond Purchase Agreement, all certified by its Secretary or Assistant Secretary;

(xii) Two copies of the Authority Resolution;

(xiii) One or more letters from the Company's auditor, dated the date of the Preliminary Official Statement and the Official Statement and addressed to the Company, consenting to the use of the financial statements prepared by such firm and all references to such firm contained in the Preliminary Official Statement and the Official Statement;

(xiv) Evidence of the issuance of the Bond Insurance Policy by the Bond Insurer, which policy shall unconditionally and irrevocably guarantee the payment when due of the principal of and interest on the 2004 Bonds;

(xv) Evidence satisfactory to the Underwriter of a rating of "AAA" assigned by Standard & Poor's Ratings Services, a Division of The McGraw-Hill Companies, and that such rating is in full force and effect as of the date of Closing;

(xvi) Evidence satisfactory to Bond Counsel and the

Underwriter of the registration of a Securities Certificate relating to the First Mortgage Bond and the 2004 Bonds with the Pennsylvania Public Utility Commission; and

(xvii) Such additional documentation as the Underwriter or its counsel or Bond Counsel may reasonably request to evidence compliance with applicable law and the validity of the 2004 Bonds, the Financing Agreement, the Trust Indenture, this Bond Purchase Agreement, the Mortgage, the First Mortgage Bond and the Continuing Disclosure Agreement, and to evidence that the interest on the 2004 Bonds is not includable in gross income under the Code and the status of the offering under the 1933 Act and the 1939 Act.

(d) At Closing there shall not have been any material adverse change in the financial condition of the Company or any adverse development concerning the business or assets of the Company that would result in a material adverse change in the prospective financial condition or results of operations of the Company from that described in the Official Statement, which, in the judgment of the Underwriter, makes it inadvisable to proceed with the sale of the 2004 Bonds; and the Underwriter shall have received certificates of the Company certifying that no such material adverse change has occurred or, if such a change has occurred, full information with respect thereto; and

(e) The Underwriter shall deliver at Closing a certificate in form acceptable to Bond Counsel to the effect that the Underwriter has sold to the public (excluding bond houses and brokers) a substantial amount of the 2004 Bonds at initial offering prices no higher than, or yields no lower than, those shown on the cover page of the Official Statement and that such certificate may be relied upon for purposes of determining compliance with Section 148 of the Code.

12. EVENTS PERMITTING THE UNDERWRITER TO TERMINATE. The Underwriter may terminate its obligation to purchase the 2004 Bonds at any time before Closing if any of the following occurs:

(a) A legislative, executive or regulatory action or proposed action, or a court decision, which in the reasonable judgment of the Underwriter casts sufficient doubt on the legality of, or the exclusion from gross income for federal income tax purposes of interest on, obligations such as the 2004 Bonds so as to materially impair the marketability or materially lower the market price of the 2004 Bonds; or

(b) Any action by the Securities and Exchange Commission or a court that would require registration of the 2004 Bonds or the First Mortgage Bond under the 1933 Act or qualification of the Indenture under the 1939 Act; or

(c) Any general suspension of trading in securities on the New York Stock Exchange or the establishment, by the New York Stock Exchange, by the Securities and Exchange Commission, by any federal or state agency, or by the decision of any court, of any limitation on prices for such trading, or any outbreak of hostilities or other national or international calamity or crisis, or any material escalation in any such hostilities, calamity or crisis, the effect of which on the financial markets of the United States of America shall be such as to materially impair the marketability or materially lower the market price of the 2004 Bonds; or

(d) Any event or condition occurring or arising after the date hereof, which in the reasonable judgment of the Underwriter renders untrue or incorrect, in any material respect as of the time to which the same purports to relate, the information contained in the Official Statement, or which requires that information not reflected in the Official Statement or Appendices thereto should be reflected therein in order to make the statements and information contained therein not misleading in any material respect as of such time; provided that the Authority, the Company and the Underwriter will use their best efforts to amend or supplement the Official Statement to reflect, to the reasonable satisfaction of the Underwriter, such changes in or additions to the information contained in the Official Statement; or

(e) Pending or threatened litigation affecting or arising out of the ownership of the Facilities or any other facilities of the Company or the issuance of the 2004 Bonds, which, in the reasonable judgment of the

Underwriter, would materially impair the marketability or materially lower the market price of the 2004 Bonds; or

(f) Quantities of the Official Statement are not delivered to the Underwriter in a timely manner as required by Section 10 hereof. If the Underwriter terminates its obligation to purchase the 2004 Bonds because any of the conditions specified in Section 11 hereof or this Section 12 shall not have been fulfilled at or before the Closing, such termination shall not result in any liability on the part of the Authority, the Underwriter, or, except for the payment of such costs of issuance described in Section 13 hereof which are due and payable, the Company.

13. EXPENSES. All expenses and costs of the authorization, issuance, sale and delivery of the 2004 Bonds including, without limitation, accrued interest and redemption premium due on the 1993 Bonds, the preparation of and furnishing to the Underwriter of the Preliminary Official Statement and the Official Statement, the preparation and execution of the 2004 Bonds, the Financing Agreement, the Trust Indenture, the First Mortgage Bond, the Thirty-Eighth Supplemental Mortgage and this Bond Purchase Agreement, the Insurance Policy premium, rating agency fees, the issuance and closing fees of the Authority, the fees and disbursements of counsel to the Authority, the fees and disbursements of Bond Counsel, the fees and disbursements of counsel to the Underwriter and the expenses incurred in connection with qualifying the 2004 Bonds for sale under the securities laws of various jurisdictions and preparing Blue Sky and legal investment memoranda, shall be paid by the Company from funds contributed by the Company and not from proceeds of the 2004 Bonds. The Authority shall, bear no out-of-pocket expense in connection with the transactions contemplated by this Bond Purchase Agreement. The Underwriter will pay all other expenses of the Underwriter in connection with the public offering of the 2004 Bonds.

14. EXECUTION IN COUNTERPARTS. This Bond Purchase Agreement may be executed in any number of counterparts, all of which taken together shall constitute one and the same instrument, and any of the parties hereto may execute this Bond Purchase Agreement by signing any such counterpart.

15. NOTICES AND OTHER ACTIONS. All notices, requests, demands and formal actions hereunder will be in writing mailed, faxed (with confirmation of receipt) or delivered by nationally recognized, next-day delivery service to:

The Underwriter:

Sovereign Securities Corporation, LLC
Mail Code: 20-210-CPC LLC
1500 Market Street
Centre Square-Concourse
Philadelphia, Pennsylvania 19102

Attention: George C. Werner, III
Managing Director

Fax #: (267) 675-0643
Email: gwerner@sovereignbank.com

The Company:

Aqua Pennsylvania, Inc.
762 Lancaster Avenue
Bryn Mawr, Pennsylvania 19010

Attention: Kathy Lee Pape, Vice President, Treasurer &
Rate Counsel

Fax #: (610) 519-0989
Email: klpape@aquaamerica.com

The Authority:

Northumberland County Industrial Development Authority
399 South Fifth Street
Sunbury, Pennsylvania 17801

Attention: James E. King, Executive Director

Fax #: (570) 988-4278
Email: jking@norrycopa.net

16. GOVERNING LAW. This Bond Purchase Agreement shall be governed by and construed in accordance with the laws of the Commonwealth of Pennsylvania, excluding those relating to choice of laws or conflict of laws, and may not be assigned by the Authority, the Company or the Underwriter.

17. SUCCESSORS. This Bond Purchase Agreement will inure to the benefit of and be binding upon the parties and their respective successors and, as to Sections 6, 7 and 8 hereof, the

Indemnitees, and will not confer any rights upon any other person. The term "successor" shall not include any holder of any Bonds merely by virtue of such holding.

18. LIMITATIONS ON LIABILITY. No personal recourse shall be had for any claim based on this Bond Purchase Agreement or the 2004 Bonds against any board member, officer, agent, employee, or attorney past, present or future, of the Authority or any successor body as such, either directly or through the Authority or any successor body, under any constitutional provision, statute, or rule of law or by enforcement of any assessment or penalty or otherwise. Notwithstanding any provision or obligation to the contrary in this Bond Purchase Agreement, the liability of the Authority for payments of any kind, nature or description provided for herein or in any other document executed pursuant hereto shall be limited to the revenues derived by the Authority from the Financing Agreement.

IN WITNESS WHEREOF, the Authority, the Company and the Underwriter have caused their duly authorized Underwriters to execute and deliver this Bond Purchase Agreement as of the date first written above.

NORTHUMBERLAND COUNTY
INDUSTRIAL DEVELOPMENT AUTHORITY

By: GENE ZARTMAN

Chairman

AQUA PENNSYLVANIA, INC.

By: KATHY L. PAPE

Vice President, Treasurer and
Rate Counsel

SOVEREIGN SECURITIES CORPORATION, LLC

By: GEORGE C. WERNER, III

George C. Werner, III
Managing Director

SCHEDULE I

Terms of Bonds

Principal Amounts: \$14,000,000
Dated Date: November 30, 2004
Maturity Date: October 1, 2039
Interest Payment Dates: April 1 and October 1, commencing April 1, 2005
Rate of Interest: 5.05%
Redemption provisions:

The 2004 Bonds are subject to redemption as follows:

OPTIONAL REDEMPTION. The 2004 Bonds are subject to optional redemption prior to maturity by the Authority, at the direction of the Company, on or after October 1, 2014, as a whole or in part at any time, at a redemption price equal to one hundred percent (100%) of the principal amount thereof, plus interest accrued to the date fixed for redemption.

EXTRAORDINARY OPTIONAL REDEMPTION. The Bonds are subject to redemption, at any time prior to maturity, at the option of the Authority, upon the direction of the Company, in whole, at a Redemption Price of 100% of the principal amount of the Bonds to be redeemed, plus interest accrued thereon to the date fixed for redemption, if any of the following events shall have occurred:

(a) The damage or destruction of all or substantially all of the Project Facilities to such extent, that, in the reasonable opinion of the Company, the repair and restoration thereof would not be economical; or

(b) the taking by condemnation, or the threat thereof, of all or substantially all of the Project Facilities or the taking by condemnation of any part, use or control of the Project Facilities so as to render them unsatisfactory to the Company for their intended use; or

(c) in the Company's reasonable opinion, (1) unreasonable burdens or excessive liabilities shall have been imposed upon the Company with respect to the Project Facilities or the operation thereof, including, but not limited to, federal, state or other ad valorem, property, income or other taxes not being imposed on the date of the Agreement other than ad valorem property taxes presently levied upon privately owned property used for the same general purposes as the Project Facilities, or (2) the continued operation of the Project Facilities is impractical, uneconomical or undesirable for any reason.

Any such redemption shall be on any date within 180 days following the occurrence of one of the events listed above permitting the exercise of the option.

EXHIBIT A

FORMS OF APPROVING OPINIONS OF
BALLARD SPAHR ANDREWS & INGERSOLL, LLP
(SEE APPENDIX D OF OFFICIAL STATEMENT)

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EXHIBIT B

FORM OF SUPPLEMENTAL OPINION OF
BALLARD SPAHR ANDREWS & INGERSOLL, LLP

November [__], 2004

Sovereign Securities Corporation, LLC
1500 Market Street
Centre Square - Concourse
Philadelphia, Pennsylvania 19102

Re: \$14,000,000 aggregate principal amount of Northumberland
County Industrial Development Authority Water Facility
Revenue Refunding Bonds (Aqua Pennsylvania, Inc.
Project) Series of 2004

Ladies and Gentlemen:

Reference is made to our opinion as bond counsel identified as Closing Item No. [__] delivered to you concurrently herewith and relating to the above - referenced Bonds (the "Bonds"). At your request we have undertaken a review of certain other matters pertaining to the Bonds. All terms are used herein with the same meanings ascribed to them in the Official Statement dated November [__], 2004 (the "Official Statement") prepared in connection with the public offering of the Bonds.

Based on the review described in our bond opinion, it is our opinion that:

The Bond Purchase Agreement dated November 16, 2004 (the "Bond Purchase Agreement"), among you, the Company and the Authority has been duly authorized, executed and delivered by the Authority and constitutes the legal, valid and binding obligation of the Authority enforceable against the Authority in accordance with its terms, except as enforceability thereof may be limited by bankruptcy, insolvency or similar laws affecting the enforcement of creditors' rights generally and general principles of equity.

The information in the Official Statement under the captions: "INTRODUCTORY STATEMENT - Description of the Bonds" and "- Security for the Bonds," "THE BONDS" (other than the information under the sub-caption "Book-Entry Only System") and "SECURITY FOR THE BONDS" (other than the information under the sub-captions "Mortgage" and "Additional Parity Indebtedness") and the information set forth in Appendix C to the Official Statement (other than information under the headings "THE FIRST MORTGAGE BOND AND THE MORTGAGE") is accurate and fairly presents the information intended to be shown with respect thereto. The information in the Official Statement under the caption "TAX MATTERS" fairly summarizes our firm's opinion with respect to the tax-exempt status of the Bonds in all material respects.

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It is not necessary in connection with the offering and sale of the Bonds to register the Bonds under the Securities Act of 1933, as amended, or to qualify the Indenture under the Trust Indenture Act of 1939, as amended.

This letter is furnished by us solely for your benefit in connection with the provisions of the Bond Purchase Agreement and may not be relied upon by any other persons for any purpose without our express written permission.

Very truly yours,

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EXHIBIT C

Points to be covered in Opinion of Counsel for the Authority

(Terms defined in Bond Purchase Agreement are used here with same meanings)

1. The Authority is a body corporate and politic constituting an instrumentality of the Commonwealth and is duly created and existing pursuant to the Act.

2. The Authority Resolution was duly adopted by the Authority at a public meeting held in accordance with the provisions of Section 13 of the act of July 3, 1986, (P.L. 388, No. 84, as amended), known as the Pennsylvania Sunshine Act; and the Authority resolution remains in full force and effect and has not been amended, repealed or superseded in any way.

3. The Authority has by proper action duly authorized the execution and issuance of the 2004 Bonds and the execution and delivery of the Authority Financing Documents. The 2004 Bonds have been duly and validly issued by the Authority and the Authority Financing Documents have each been duly and validly executed and delivered by the Authority and the 2004 Bonds and each of such documents are valid and binding agreements of the Authority, enforceable against the Authority in accordance with their respective terms, except as enforcement may be limited by bankruptcy, insolvency, reorganization, moratorium or other laws or legal or equitable principles affecting the enforcement of creditor's rights.

4. To the knowledge of such counsel, the execution and the issuance by the Authority of the 2004 Bonds, the execution and delivery by the Authority of the Authority Financing Documents and performance by the Authority of the Authority's obligations under the 2004 Bonds and the Authority's Financing Documents, do not conflict with or constitute on a part of the Authority a violation of, breach of or default under any existing constitutional provision or statute of the Commonwealth, or, to our knowledge without having undertaken

any independent investigation, any indenture, mortgage, deed of trust, resolution, note agreement or other agreement or instrument to which the Authority is a party or by which the Authority is bound, or, to our knowledge, any order, rule or regulation of any court, governmental agency or body of the Commonwealth having jurisdiction over the Authority or any of its activities or property.

5. To the knowledge of such counsel, there is no action, suit, proceeding, inquiry or investigation, at law or in equity, before or by any court, public board or body, pending or threatened against the Authority, wherein an unfavorable decision, ruling or finding would materially and adversely affect the transactions contemplated by the 2004 Bonds.

6. The Authority has approved the distribution of the Preliminary Official Statement and the Official Statement by the Underwriter in connection with the sale of the 2004 Bonds.

7. The information contained in the Preliminary Official Statement and the Official Statement under the headings "INTRODUCTORY STATEMENT - The Authority" and "THE AUTHORITY" has been reviewed by us and nothing has come to our attention which would

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lead us to believe that such information contains any untrue statement of a material fact or omits to state a material fact which is required to be stated therein or which is necessary to make the statements therein, in the light of the circumstances under which they were made, not misleading in any material respect.

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EXHIBIT D

FORM OF OPINIONS OF THE COMPANY'S LEGAL COUNSEL AND
COMPANY'S SENIOR VICE PRESIDENT - LAW AND ADMINISTRATION

November 30, 2004

Northumberland County Industrial
Development Authority
399 South Fifth Street
Sunbury, Pennsylvania 17801

Sovereign Securities Corporation, LLC
1500 Market Street
Philadelphia, PA 19102

RE: \$14,000,000 AGGREGATE PRINCIPAL AMOUNT OF NORTHUMBERLAND COUNTY
INDUSTRIAL DEVELOPMENT AUTHORITY WATER FACILITIES REVENUE
REFUNDING BONDS (AQUA PENNSYLVANIA, INC. PROJECT) SERIES OF 2004

Ladies and Gentlemen:

We have acted as counsel to Aqua Pennsylvania, Inc. (the "Company") in connection with (i) the issuance by Northumberland County Industrial Development Authority (the "Authority"), and the sale to Sovereign Securities Corporation, LLC pursuant to that certain Bond Purchase Agreement dated _____, 2004 (the "Purchase Agreement"), of \$14,000,000 aggregate principal amount of Northumberland County Industrial Development Authority Water Facilities Revenue Refunding Bonds (Aqua Pennsylvania, Inc.) Series of 2002 (the "Authority Bonds"), and (ii) the issuance and delivery of \$14,000,000 principal amount of the Company's First Mortgage Bond, 5.05% Series due 2039 (the "First Mortgage Bond"), issued under an Indenture of Mortgage (the "Original Mortgage") dated as of January 1, 1941, as amended and supplemented by supplemental indentures thereto, including the Thirty-Eighth Supplemental Indenture dated as of November 15, 2004 (the "Thirty-Eighth Supplemental Indenture") under which J.P. Morgan Trust Company, National Association is trustee (the "Mortgage Trustee"). The Original Mortgage as amended and supplemented is hereinafter called the "Mortgage". Capitalized terms used herein and not otherwise defined shall have the meanings ascribed to such terms in the Purchase Agreement.

We have examined and reviewed, among other things:

- (a) a copy of the Articles of Incorporation of the Company, as amended and restated and now in effect;

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- (b) a copy of the bylaws of the Company as now in effect;
- (c) resolutions of the Board of Directors of the Company authorizing the execution and delivery of the Purchase Agreement, the Financing Agreement, the Thirty-Eighth Supplemental Indenture, the First Mortgage Bond, the Continuing Disclosure Agreement and the Official Statement;
- (d) the Purchase Agreement;
- (e) the Financing Agreement dated as of November 15, 2004 (the "Financing Agreement") between the Authority and the Company;
- (f) the Continuing Disclosure Agreement dated _____, 2004 (the "Continuing Disclosure Agreement") between the Company and J.P. Morgan Trust Company, National Association, as trustee for the Authority Bonds (the "Trustee");
- (g) the Official Statement relating to the Authority Bonds dated November __, 2004 (the "Official Statement");
- (h) the Securities Certificate relating to the issue and sale of the First Mortgage Bond, filed by the Company with the Pennsylvania Public Utility Commission pursuant to the provisions of Chapter 19 of the Pennsylvania Public Utility Code, and a copy of the Order of the Public Utility Commission registering such Securities Certificate, certified by the Secretary of the Pennsylvania Public Utility Commission;
- (i) a Subsistence Certificate from the Secretary of the Commonwealth with respect to the Company;
- (j) executed counterparts of the Original Mortgage and of the Thirty-Eighth Supplemental Indenture supplemental thereto and evidence satisfactory to us of the due recordation thereof in the Counties of Adams, Berks, Bradford, Bucks, Carbon, Chester, Columbia, Cumberland, Delaware, Forest, Juniata, Lackawanna, Lawrence, Luzerne, Mercer, Monroe, Montgomery, Northampton, Northumberland, Pike, Schuylkill, Snyder, Susquehanna, Wayne and Wyoming, Pennsylvania;
- (k) the documents delivered to the Mortgage Trustee in connection with the authentication of the First Mortgage Bond pursuant to the provisions of Sections 2(B) and 3 of Article IV of the Original Mortgage;
- (l) the First Mortgage Bond delivered to the Trustee at the Closing held today;
- (m) the certificates of the Company and other documents delivered to the Mortgage Trustee at the Closing;
- (n) a certificate of the Company and various bringdown title searches by Commonwealth Land Title Insurance Company in the Counties of Adams, Berks, Bradford, Bucks, Carbon, Chester, Columbia, Cumberland, Delaware, Forest,

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Juniata, Lackawanna, Lawrence, Luzerne, Mercer, Monroe, Montgomery, Northampton, Northumberland, Pike, Schuylkill, Snyder, Susquehanna, Wayne and Wyoming, Pennsylvania, each dated as of a recent date (collectively, "Title Searches"), as to matters relating to title to real estate and the lien of the Mortgage thereon, on which certificate and searches we are relying for the purposes of this opinion; and

- (o) various certificates of officers of the Company relating to title to real property and the priority of any lien thereon.

In rendering this opinion, we have assumed that all signatures on documents and instruments examined by us are genuine (except signatures of the Company on the Purchase Agreement, the Thirty-Eighth Supplemental Indenture, the Financing Agreement (collectively, the "Company Documents") and the Official Statement), the authenticity of all documents submitted to us as originals and the conformity with the original documents of all documents submitted to us as copies. We have also assumed, with your permission, that none of the signatories of the documents and instruments referred to above is an affiliate of the Company within the meaning of 66 Pa.C.S. Section 2101 (1989).

As to questions of fact material to the opinions hereinafter expressed, we have relied solely and without investigation upon certificates of public officials, certificates of officers of the Company and the representations of the Company contained in the Company Documents (including the exhibits and schedules to such documents) and the certificates and other documents delivered pursuant thereto. To the extent that the opinions contained herein are given to the best of our knowledge, such knowledge means the actual knowledge of those attorneys within our firm who have provided substantive representation to the Company, without investigation and inquiry, and does not include matters of which such attorneys could be deemed to have constructive knowledge.

In rendering this opinion, we have also assumed that each of the Company Documents has been duly authorized, executed and delivered by each party thereto (other than the Company) and that each of the Company Documents is binding and enforceable against each such party in accordance with its respective terms.

Further, as to matters relating to title to real estate and the lien of the Mortgage, we have relied exclusively upon various certificates of officers of the Company and the Title Searches and we have not made, nor undertaken to make, any investigation or inquiry with respect to title to real property or the priority of any lien thereon.

We are generally familiar with the Company's operations as a public utility within the Commonwealth of Pennsylvania (the "Commonwealth").

Based upon the foregoing and such other examination of fact and law as we have deemed necessary for purposes of this opinion, we are of the opinion that:

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1. The Company was organized and subsists under the laws of the Commonwealth, with power (corporate and other) to own its properties and conduct its business as described in the Official Statement.

2. The Company has the corporate power and authority to enter into and perform the Purchase Agreement, the Financing Agreement, the First Mortgage Bond, the Thirty-Eighth Supplemental Indenture and the Continuing Disclosure Agreement. The execution, delivery and performance by the Company of the Financing Agreement, the Bond Purchase Agreement, the First Mortgage Bond, the Thirty-Eighth Supplemental Indenture and the Continuing Disclosure Agreement have been duly authorized by all requisite corporate action.

3. The Purchase Agreement, the Financing Agreement and the Continuing Disclosure Agreement constitute legal, valid and binding obligations of the Company, enforceable against the Company in accordance with their respective terms.

4. The First Mortgage Bond has been duly authorized, executed, authenticated, issued and delivered and each constitutes a valid and legally binding obligation of the Company entitled to the benefits provided by the Mortgage.

5. The First Mortgage Bond is not subject to the registration requirements of the 1933 Act.

6. The Mortgage constitutes a direct, valid and enforceable mortgage lien (except as enforceability of such lien may be limited by bankruptcy, insolvency, reorganization or other laws affecting the enforcement of creditors' rights) upon all of the properties and assets of the Company (not

heretofore released as provided for in the Mortgage) specifically or generally described or referred to in the Mortgage as being subject to the lien thereof, except for permitted liens under the Mortgage; the Original Mortgage and the Thirty-Eighth Supplemental Mortgage have been properly recorded in the Counties of Adams, Berks, Bradford, Bucks, Carbon, Chester, Columbia, Cumberland, Delaware, Forest, Juniata, Lackawanna, Lawrence, Luzerne, Mercer, Monroe, Montgomery, Northampton, Northumberland, Pike, Schuylkill, Snyder, Susquehanna, Wayne and Wyoming in the Commonwealth and such recordings are the only recordings necessary in order to establish, preserve, protect and perfect the lien of the Mortgage on all real estate and fixed property of the Company (excluding easement and other similar rights) described in the Mortgage as subject to the lien thereof.

7. In each of the following cases with such exceptions as are not material and do not interfere with the conduct of the business of the Company, the Company has good and marketable title to all of its real property currently held in fee simple; good and marketable title to all of its other interests in real property (other than to certain rights of way, easements, occupancy rights, riparian and flowage rights, licenses, leaseholds, and real property interests of a similar nature); and good and marketable title to all personal property owned by it; in each case free and clear of all liens, encumbrances and defects except such as may be described in the Official Statement, the lien of the Mortgage, permitted liens under the Mortgage or such as do not materially affect the value of such property and do not interfere with the use made and proposed to be made of such property by the Company; and any real property and buildings held

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under lease by the Company are held by it under valid, subsisting and enforceable leases with such exceptions as are not material and do not interfere with the use made and proposed to be made of such property and buildings by the Company.

8. The Company is not a holding company, a registered holding company or an affiliate of a registered holding company within the meaning of the Public Utility Company Holding Act of 1935, as amended.

9. The Mortgage and the First Mortgage Bond conform in all material respects as to legal matters to the descriptions thereof in the Official Statement.

Without having undertaken to determine independently the accuracy, completeness and fairness of the statements contained in the Official Statement, nothing has come to our attention in connection with our representation of the Company in respect of the issuance of the First Mortgage Bond which leads us to believe that the information with respect to the Company contained in the Official Statement (including Appendix A and the information incorporated therein by reference) contain any untrue statement of a material fact or omit to state a material fact which is required to be stated therein or which is necessary to make such information and descriptions, in the light of the circumstances under which they were made, not misleading in any material respect.

The foregoing opinions are subject to the following qualifications:

(i) The opinions expressed in paragraphs 3 and 4 are subject to the qualifications that the enforceability of the First Mortgage Bond is subject to (i) applicable bankruptcy, insolvency, reorganization, moratorium, and other similar laws of general application relating to or affecting creditors' rights, (ii) certain provisions of Pennsylvania law affecting the availability of certain remedies, and (iii) the further qualification that the availability of specific performance, injunctive relief or other equitable remedies is subject to the discretion of the court before which any proceeding therefor may be brought.

(ii) Our opinions are subject to limitations imposed by general principles of equity, including principles of commercial reasonableness, good faith and fair dealing (regardless of whether enforcement is considered in proceedings at law or in equity).

(iii) We express no opinion as to the enforceability with respect to any provisions purporting to waive the effect of applicable laws and remedies and any provisions releasing any party from, or requiring

indemnification for, liability for gross negligence, recklessness or willful misconduct.

(iv) Any requirements in any of the documents specifying that provisions of a document may only be waived in writing may not be enforced to the extent that an oral agreement or an implied agreement by trade practice or course of conduct has been created modifying any provision of such document.

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(v) We express no opinion as to the applicability to the transactions contemplated by the Company Documents of Section 548 of the Bankruptcy Code or any applicable state law relating to fraudulent transfers and obligations.

(vi) Other applicable local, state and federal laws, regulations and ordinances, court decisions and constitutional requirements may limit or render unenforceable certain of the rights or remedies contained in the Company Documents, but in our opinion, none of the same would materially impair the practical realization of the benefits intended to be provided by the Company pursuant to the Company Documents.

(vii) Our opinion is limited in all respects to the laws of the Commonwealth in effect as of the date hereof and we express no opinion as to the laws of any other jurisdiction.

(viii) This opinion is limited to the matters set forth herein, no opinion may be inferred or implied beyond the matters expressly stated herein, and our statements contained in the opinion portion of this letter must be read in conjunction with the assumptions, limitations, exceptions and qualifications set forth in this letter.

(ix) The opinions herein are expressed as of the date hereof only and not as of some future date. We undertake no responsibility to advise you of any change in law or new laws, regulations or judicial decisions in the future. Nor do we assume any obligation to update or supplement this opinion to reflect any facts or circumstances which may hereafter come to our attention. References to "laws," "regulations" and "judicial decisions" herein shall include only officially published laws and regulations of the Commonwealth of Pennsylvania.

This opinion is solely for the benefit of each of you and the benefit of any subsequent holder of the First Mortgage Bond or the Authority Bonds and may not be relied upon by any other person or for any other purpose.

Very truly yours,

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[Letterhead of Aqua Pennsylvania]

November 30, 2004

Sovereign Securities Corporation, LLC
1500 Market Street
Philadelphia, PA 19102

RE: \$14,000,000 Aggregate Principal Amount of Northumberland County Industrial Development Authority Bonds (Aqua Pennsylvania, Inc. Project), Series of 2004 (the "Authority Bonds")

Ladies and Gentlemen:

I am Senior Vice President-Law and Administration for Aqua Pennsylvania, Inc. (the "Company").

Pursuant to Section 11(c)(iv) of the Bond Purchase Agreement dated November __, 2004 (the "Purchase Agreement") among the Authority, the Underwriter and the Company (f/k/a Pennsylvania Suburban Water Company, as successor by merger to Philadelphia Suburban Water Company) relating to the Authority Bonds, I have been asked to render an opinion to you regarding certain matters involving the Company. Capitalized terms used herein and not otherwise defined shall have the definitions ascribed to such terms in the Purchase

Agreement.

In rendering this opinion, I have assumed the following:

- i. the genuineness of all signatures (other than the signatures of the Company on the Thirty-Eighth Supplemental Mortgage, as hereinafter defined);
- ii. the authenticity and completeness of all documents submitted to me as originals;
- iii. the conformity to original documents of all documents submitted to me as copies, and the authenticity of the originals of such copies;
- iv. the entity executing the Mortgage as trustee is duly organized and validly existing, in good standing under the laws of the jurisdiction of its organization, is properly qualified to do business in all jurisdictions in which the business conducted by it makes such qualification necessary and has all necessary legal and corporate power and authority to enter into and perform its obligations under the Mortgage;
- v. the due authorization, execution and delivery of the Mortgage by or on behalf of the party thereto other than the Company;

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- vi. the enforceability against each party thereto (other than the Company) of the Mortgage in accordance with its respective terms; and
- vii. that the execution, delivery and performance of the Mortgage by the entity other than the Company which is party thereto does not and will not conflict with, result in any breach of, or constitute a default under any order, writ, injunction or decree of any court or governmental authority, or any agreement, indenture or other instrument, to which any such party is a party or by which it or its properties are bound, and that all necessary approvals, consents, permits, registrations, filings or other notices to or grants of authority from any federal or local governmental body necessary for the execution, delivery and performance of the Mortgage by each party thereto (other than the Company) have been duly received or made, with all appeal periods expired and no appeals taken.

I am making each of the foregoing assumptions with your permission and with the disclaimer that we make no representation as to the accuracy of such assumptions, although I have no knowledge that any such assumption is untrue.

In my opinion:

1. In each of the following cases with such exceptions as are not material and do not materially interfere with the conduct of the business of the Company; (a) the Company has all licenses, franchises, permits, authorizations, rights, approvals, consents and order of all governmental authorities or agencies necessary for the ownership or lease of the properties owned or leased by it and for the operation of the business carried on by it as described in the Official Statement, and all water rights, riparian rights, easements, rights of way and other similar interests and rights described or referred to in the Mortgage necessary for the operation of the business carried on by it as described in the Official Statement; (b) except as otherwise set forth in the Official Statement, all such licenses, franchises, permits, orders, authorizations, rights, approvals and consents are in full force and effect and contain no unduly burdensome provisions; (c) to the best of my knowledge, except as otherwise set forth in the Official Statement, there are no legal or governmental proceedings pending or, to my knowledge, threatened that would result in a material modification, suspension or revocation thereof; and (d) the Company has the legal power to exercise the rights of eminent domain for the purposes of conducting its water utility operations.

2. The issue and sale of the Bonds; the issue and delivery of the First Mortgage Bond and the compliance by the Company with all of the applicable provisions of the First Mortgage Bond and the Mortgage; and the execution, delivery and performance by the Company of the Thirty-Eighth Supplemental Mortgage, the Financing Agreement, the Purchase Agreement and the Continuing Disclosure Agreement will not materially conflict with or result in a material

breach of any of the terms or provisions of, or constitute a material default under, or result in the creation or imposition of any material lien, charge or encumbrance (other than the lien of the Mortgage) upon any of the property or assets of the Company pursuant to the terms of, any indenture, mortgage, deed of trust, loan agreement or other agreement or instrument to which the Company is a party or by which the Company is bound or to which any of the property or assets of the Company is subject, nor will such action result in a violation of the provisions of the Articles of Incorporation, as amended, or the Bylaws of the Company or any statute or any order,

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rule or regulation of any court or governmental agency or body having jurisdiction over the Company or any of its property. No consent, approval, authorization, order, registration or qualification of or with any court or any such regulatory authority or other governmental body not already obtained is required for the issue and delivery of the First Mortgage Bonds, the execution, delivery and performance of the Purchase Agreement, the Financing Agreement, the Thirty-Eighth Supplemental Mortgage, the First Mortgage Bonds and the Continuing Disclosure Agreement, or the consummation of the other transactions contemplated by the Purchase Agreement or the Mortgage.

3. There are no legal or governmental proceedings pending to which the Company is a party or of which any property of the Company is the subject, other than as set forth in the Official Statement and other than litigation incident to the kind of business conducted by the Company, wherein an unfavorable ruling, decision or finding is likely that would have a material adverse effect on the financial position, stockholders' equity or results of operations of the Company.

4. Each of the Indenture of Mortgage dated as of January 1, 1941 (the "Original Mortgage"), between the Company and The Philadelphia Company for Insurance on Lives and Exacting Annuities (now J.P. Morgan Trust Company, National Association, as successor in interest), as trustee (the "Trustee") and the thirty-eight indentures supplemental thereto, including the Thirty-Eighth Supplemental Indenture dated as of November 15, 2004 between the Company and the Trustee (the Original Mortgage as so supplemented and amended, the "Mortgage") was duly authorized, executed and delivered by the Company and the Mortgage constitutes a legal, valid and binding obligation of the Company, enforceable against the Company in accordance with its terms (subject to applicable bankruptcy, insolvency, fraudulent transfer, reorganization, moratorium or other similar laws relating to creditors' rights generally from time to time in effect, and subject, as to enforceability, to general principles of equity, regardless of whether such enforceability is considered in a proceeding in equity or at law).

The foregoing opinions are subject to the following qualifications:

i. The enforceability of the Mortgage, including, without limitation, any nonjudicial and self-help remedies and waivers contained therein, may be limited by bankruptcy, insolvency, reorganization, moratorium, fraudulent conveyance or other similar laws affecting the rights of creditors generally and are subject to limitations imposed by general principles of equity, including principles of commercial reasonableness, good faith and fair dealing (regardless of whether enforcement is considered in proceedings at law or in equity), public policy and applicable law which may limit the availability of the remedies provided for therein,

ii. I express no opinion as to the adequacy of any notice with respect to the disposition of any collateral. I also express no opinion as to the effectiveness or enforceability of provisions relating to waivers of notice or waivers of other rights, severability, prepayment fees or penalties, choice of law, or any provisions which release or limit the Company's liability or relate to cumulative remedies or, to the extent they purport to or would have the effect of compensating the Company in amounts in excess of any actual loss suffered by the Company, provisions relating to the payment of a default rate of interest.

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iii. I express no opinion as to enforceability with respect to any provisions in the Mortgage executed by the Company purporting to waive the effect of applicable laws and remedies and any provisions releasing

any party from, or requiring indemnification for, liability for gross negligence, recklessness or wilful misconduct.

iv. Requirements in the Mortgage specifying that provisions of the Mortgage may only be waived in writing may not be enforced to the extent that an oral agreement or an implied agreement by trade practice or course of conduct has been created modifying any provision of such Mortgage.

v. My opinion is limited in all respects to laws of the Commonwealth of Pennsylvania in effect as of the date hereof and we express no opinion as to the laws of any other jurisdiction.

vi. This opinion is limited to the matters set forth herein, no opinion may be inferred or implied beyond the matters expressly stated herein, and our statements contained in the opinion portion of this letter must be read in conjunction with the assumptions, limitations, exceptions and qualifications set forth in this letter.

vii. The opinions herein are expressed as of the date hereof only and not as of some future date. I undertake no responsibility to advise you of any change in law or new laws, regulations or judicial decisions in the future nor do I assume any obligation to update or supplement this opinion to reflect any facts or circumstances which may hereafter come to our attention. References to "laws," "regulations" and "judicial decisions" herein shall include only officially published laws and regulations of the Commonwealth of Pennsylvania.

This opinion is solely for your benefit and may not be relied upon by any other person or for any other purpose.

Very truly yours,

Roy H. Stahl

AQUA AMERICA, INC.
2005 EXECUTIVE DEFERRAL PLAN

In recognition of the services provided by certain key employees, the Board of Directors of Aqua America, Inc. adopted the Plan to make additional retirement benefits available to those individuals. This Plan is intended to replace the Philadelphia Suburban Corporation Executive Deferral Plan (the "Prior Executive Deferral Plan") and no further deferrals will be credited under the Prior Executive Deferral Plan after the effective date of this Plan. The Prior Executive Deferral Plan shall remain in effect with respect to deferrals made prior to January 1, 2005.

ARTICLE 1

Definitions

- 1.1 "Account" means a bookkeeping account established pursuant to Section 3.1 which reflects the amount standing to the credit of the Participant under the Plan.
- 1.2 "Affiliated Company" means any affiliate or subsidiary of the Company.
- 1.3 "Base Salary" means the annual amount of base salary and wages paid by the Employer to an Employee for any calendar year of employment, but excluding all Employer contributions to benefit plans and all other forms of compensation.
- 1.4 "Beneficiary" means the person(s) designated by a Participant to receive any benefits payable under this Plan subsequent to the Participant's death. The Committee shall provide a form for this purpose. In the event a Participant has not filed a Beneficiary designation with the Company, the Beneficiary shall be the Participant's estate.
- 1.5 "Board" means the Board of Directors of the Company.
- 1.6 "Bonus" shall mean bonus compensation due to the Employee, if any, under the Company's Incentive Compensation Plan.
- 1.7 "Code" means the Internal Revenue Code of 1986, as amended.
- 1.8 "Committee" means the Compensation Committee of the Board which shall act for the Company in making decisions and performing specified duties with respect to the Plan.
- 1.9 "Company" means Aqua America, Inc. and its successors.
- 1.10 "Effective Date" means January 1, 2005.
- 1.11 "Employee" means any individual employed by the Employer as an officer, senior manager or other highly compensated employee, as designated by the Committee, on a regular, full-time basis (in accordance with the personnel policies and practices of the Employer).
- 1.12 "Employer" means the Company and/or any Participating Employer, either collectively or individually, as the context requires.
- 1.13 "Key Employee" means (i) an officer of the Company or its affiliates having annual compensation greater than \$130,000 (adjusted for inflation and limited to 50 employees), (ii) a five percent owner of the Company and its affiliates, or (iii) a one percent owner of the Company and its affiliates who has annual compensation from the Company and its affiliates greater than \$150,000, as determined by the Committee in a manner consistent with the regulations issued under section 409A of the Code.
- 1.14 "Participant" means any Employee who satisfies the eligibility requirements set forth in Article 2. In the event of the death or

incompetency of a Participant, the term shall mean his personal representative or guardian. An individual shall remain a Participant until that individual has received full distribution of any amount credited to the Participant's Account.

- 1.15 "Participating Employer" means any Affiliated Company which is designated by the Committee as a Participating Employer under the Plan. The Committee or a Participating Employer may terminate such designation at any time, but until such acceptance has been terminated, all the provisions of the Plan and amendments thereto shall apply to the Employees of the Participating Employer. In the event the designation as a Participating Employer is terminated by the board of directors of an Affiliated Company, the Plan shall be deemed terminated only with respect to such Participating Employer.
- 1.16 "Plan" means the Aqua America, Inc. 2005 Executive Deferral Plan as the same is set forth herein, and as it may be amended from time to time.
- 1.17 "Plan Year" means the calendar year.
- 1.18 "Separates from Employment" means the Employee's termination of employment from the Employer for any reason. Except as otherwise provided herein, a Separation from Employment shall be deemed to have occurred on the last day of the Employee's service to the Employer and shall be determined without reference to any compensation continuation arrangement or severance benefit arrangement that may be applicable.
- 1.18 "Thrift Plan" means the Aqua America, Inc. Thrift Plan, as it may be amended from time to time.

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ARTICLE 2

Eligibility

- 2.1 Each Employee shall be eligible to participate in the Plan on such date as is specified by the Committee. A list of the individuals participating in the Plan on the Effective Date is attached hereto as Exhibit A; such list may be modified from time to time by the Committee.

ARTICLE 3

Benefits

- 3.1 The Employer shall create and maintain on its books an Account for each Participant to which it shall credit amounts contributed to the Plan pursuant to this Article 3. The Employer shall also credit each Participant's Account with deemed earnings for each Plan Year in accordance with the provisions of Article 8 hereof.
- 3.2 Prior to the commencement of any Plan Year, or within 30 days after first being eligible to participate hereunder, a Participant may elect to have the Employer credit to the Participant's Account (as a result of payroll reduction) an amount equal to any whole percentage or dollar amount of the Participant's Bonus, if any, to be earned for such Plan Year. Prior to the commencement of any Plan Year, a Participant may also elect to have the Employer contribute to the Participant's Account (as a result of payroll reduction) an amount equal to any whole percentage or dollar amount of the Participant's Base Salary for services to be rendered during such Plan Year. If an election is made to have a contribution credited to the Participant's Account for a Plan Year, the credit shall be made at the time that such amount would otherwise have been paid and shall reduce the Participant's Bonus or Base Salary, as applicable with respect to that Plan Year by a corresponding amount. The Committee may establish minimum or maximum amounts that may be deferred under this Section and may change such standards from time to time. Any such limits shall be communicated by the Committee to the Participants prior to the commencement of a Plan Year. In addition, at the time of his or her deferral election for each Plan Year, a Participant shall elect the form of payment, as described in Section 4.1 below, with respect to deferred Base Salary and/or Bonus for the upcoming Plan Year.
- 3.3 Any elections under this Article shall be made in writing on such form

and at such time as the Committee shall specify consistent with the provisions of Section 3.2. Any election by a Participant pursuant to this Section 3.3 shall be irrevocable as to any credits made to a Participant's Account in a Plan Year.

- 3.4 For each Plan Year, the Employer shall also credit to the Participant's Account an amount equal to the excess of the contribution that would have been made by the Employer under the Thrift Plan on behalf of the Participant if it were not for the limitations imposed by the Code over the amount actually contributed by the Employer to the Thrift Plan on behalf of the Participant. In addition, the Employer

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may make an additional credit to each Participant's Account for any Plan Year in such amount as shall be approved by the Committee. Such credits shall be deemed to have occurred at the time such amounts would otherwise have been contributed to the Thrift Plan or at such other time as is specified by the Employer.

ARTICLE 4

Distributions to Participants

- 4.1 A Participant's benefit under the Plan shall be distributed in one lump sum, or, if at least \$25,000 is credited to a Participant's Account, in 12 annual installments (with the balance to be distributed continuing to be credited with deemed earnings for each subsequent Plan Year in accordance with the provisions of Article 8 hereof) equal to 1\12, 1\11, 1\10, 1\9, 1\8, 1\7, 1\6, 1\5, 1\4, 1\3, 1\2, and 1\1 of the balance then credited to the Participant's Account, and shall be paid, or commence, as soon as practicable following the completion of the valuation of the Participant's Account for the last day of the month in which the Participant Separates from Employment, as previously elected by the Participant. Notwithstanding anything herein to the contrary, in the event that such a Participant fails to make an election, distribution shall be in the form of one lump sum payment paid as soon as practicable after the first day of the year following the date the Participant Separates from Employment.
- 4.2 The Committee may establish rules allowing Participants to make a "second election" to postpone payment of his or her Account, in accordance with section 409A of the Code and the regulations thereunder. In that event, (i) the subsequent election may not take effect unless the Participant is employed for at least 12 months after the date on which the election is made and (ii) except with respect to an election related to payment upon death, disability or a severe financial hardship, the first payment with respect to which such election is made must be deferred for a period of not less than five years from the date such payment would otherwise have been made.
- 4.3 Notwithstanding any provision of the Plan to the contrary, distributions upon a Separation from Employment to a Participant who is a Key Employee may not be made earlier than the first day of the seventh month following the date of the Participant's Separation from Employment, as required by section 409A of the Code and any regulations issued thereunder.
- 4.4 In the event that a Participant incurs a "significant financial hardship" while employed by the Employer, as determined by the Committee, the Participant may apply, in writing, for a withdrawal of all or a portion of the balance credited to the Participant's Account in the form of a lump sum in cash. All determinations by the Committee regarding the existence of a financial hardship shall be made in accordance with the Section 409A of the Internal Revenue Code of 1986, as amended. The Committee shall determine whether to permit such a withdrawal and, based upon the Participant's application, the amount necessary to satisfy that hardship, which shall be distributed in a single sum as soon as practicable after the Committee's determination. Such a

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request shall be approved, however, only upon a finding that the Participant has suffered a severe financial hardship which has resulted from an illness or accident of the Participant, the Participant's spouse, or a dependent (as defined in section 152(a) of the Code) of the Participant, loss of the Participant's property due to casualty, or other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the Participant's control, and then only in an amount necessary to eliminate such hardship plus amounts necessary to pay taxes reasonably anticipated as a result of the distribution, after taking into account the extent to which such hardship is or may be relieved through reimbursement or compensation by insurance or by liquidation of the Participant's assets (to the extent the liquidation of such assets would not itself cause severe financial hardship).

ARTICLE 5

Death Benefit

- 5.1 In the event of the death of a Participant prior to the payment of the full benefit due pursuant to Article 4, the Participant's Beneficiary shall receive a lump sum distribution equal to the balance of the Participant's Account on the date of death; provided, however, in the event of the death of a Participant after payment of annual installments has commenced pursuant to Section 4.1 hereof, the Participant's Beneficiary will continue to receive the remaining annual installment payments due following the Participant's death. The lump sum benefit payment to the Beneficiary will be made as soon as practicable following the completion of the valuation of the deceased Participant's Account.

ARTICLE 6

Vesting

- 6.1 The balance credited to a Participant's Account attributable to Section 3.2 shall be fully vested at all times. Credits attributable to Section 3.4 shall vest at the same time as the Participant's accrued benefit under the terms of the Retirement Plan for Employees of Aqua America, Inc. and Subsidiaries.

ARTICLE 7

Funding

- 7.1 The Board may, but shall not be required to, authorize the establishment of a trust by the Employer to serve as the funding vehicle for the benefits described in Article 3 hereof. In any event, the Employer's obligation hereunder shall constitute a general, unsecured obligation, payable solely out of its general assets, and no Participant shall have any right to any specific assets of the Employer. In addition, it is the intention of the Employer that the Plan be unfunded for tax purposes and for purposes of Title I of the Employee Retirement Income Security Act of 1974, as amended.

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ARTICLE 8

Investments

- 8.1 Except as provided otherwise below, the balance credited to a Participant's Account shall be deemed to be invested in an interest bearing instrument which shall provide for interest to be credited and compounded monthly at an effective rate equal to 100 basis points in excess of the prime commercial lending rate established by Mellon Bank N.A., or such other bank determined by the Committee to be the Company's primary bank as of the beginning of any Plan Year, as in effect on the 15th day of each month (or if such day is a non-business day, on the first business day thereafter) during which there is a positive balance in a Participant's Account. Interest shall be applied to the average balance of each Participant's Account during the prior 30-day period. For any Plan Year, the Committee may determine to make available, and announce to the Participants the procedure to elect, other deemed forms of investment for the amounts credited to the Accounts. Notwithstanding anything herein to the contrary, the Company may, but shall not be

required to, actually invest any funds in the forms of investment made available hereunder and, in any event, any such investments shall at all times remain the property of the Company. Any such other deemed forms of investment shall be described on Exhibit A hereto, as in effect and amended from time to time, and shall be incorporated herein by reference.

ARTICLE 9

Administration

- 9.1 The Committee shall have full power and authority to interpret the Plan, to prescribe, amend and rescind any rules, forms and procedures as it deems necessary or appropriate for the proper administration of the Plan and to make any other determinations and to take any other such actions as it deems necessary or advisable in carrying out its duties under the Plan. All action taken by the Committee arising out of or in connection with, the administration of the Plan or any rules adopted thereunder, shall in each case, lie within its sole discretion, and shall be final, conclusive and binding upon the Employer, the Board, all Employees, all beneficiaries of Employees and all persons and entities having an interest therein.
- 9.2 Members of the Committee shall serve without compensation for their services unless otherwise determined by the Board. All expenses of administering the Plan shall be paid by the Employer.
- 9.3 The Company shall indemnify and hold harmless each member of the Committee from any and all claims, losses, damages, expenses (including counsel fees) and liability (including any amounts paid in settlement of any claim or any other matter with the consent of the Board) arising from any act or omission of such member, except when the same is due to gross negligence or willful misconduct.
- 9.4 Any decisions, actions or interpretations to be made under the Plan by the Company, Employer or the Committee (other than in the administration of the Plan) shall be made in its sole discretion, not in any fiduciary capacity and need not be uniformly applied to similarly situated individuals and shall be final, binding and conclusive on all persons interested in the Plan.

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ARTICLE 10

Amendment

- 10.1 The Plan may be amended by the Committee at any time and from time to time all without prior notice to any person or entity; provided, however, that no such amendment shall have the effect of divesting a Participant of the benefit which the Participant would otherwise receive hereunder at the time the amendment is adopted. Without limiting the foregoing, the Committee may amend the Plan in any manner that it deems appropriate, including amending outstanding deferral elections, if necessary or appropriate to comply with changes to applicable law, without the consent of any Participant.

ARTICLE 11

Termination

- 11.1 Continuance of the Plan is completely voluntary and is not assumed as a contractual obligation of the Employer. The Committee, acting on behalf of the Employer, shall have the right to terminate the Plan in whole or in part at any time all without prior notice to any person or entity; provided, however, that such termination shall not have the effect of divesting a Participant of the benefit which the Participant would otherwise receive hereunder at the time of the termination. Without limiting the foregoing, the Committee may terminate the Plan or outstanding deferral elections as it deems appropriate, if necessary or appropriate to comply with changes to applicable law, without the consent of any Participant.

ARTICLE 12

Miscellaneous

- 12.1 Nothing contained herein (a) shall be deemed to exclude a Participant from any compensation, bonus, pension, insurance, severance pay or other benefit to which he otherwise is or might become entitled as an Employee or (b) shall be construed as conferring upon an Employee the right to continue in the employ of the Employer.
- 12.2 Any amounts payable hereunder shall not be deemed salary or other compensation to a Participant for the purposes of computing benefits to which the Participant may be entitled under any other arrangement established by the Employer for the benefit of its employees.
- 12.3 The rights and obligations created hereunder shall be binding on a Participant's heirs, executors and administrators and on the successors and assigns of the Employer.
- 12.4 The masculine pronoun whenever used shall include the feminine and the singular shall be construed as the plural, where applicable.
- 12.5 The provisions of the Plan shall be construed and applied under the laws of the Commonwealth of Pennsylvania.
- 12.6 The rights of any Participant under this Plan are personal and may not be assigned, transferred, pledged or encumbered. Any attempt to do so shall be void. In addition, a Participant's rights hereunder are not subject, in any manner, to anticipation, alienation, sale, transfer, assignment, pledge, encumbrance, attachment or garnishment by creditors of the Participant or the Participant's Beneficiary.
- 12.7 If any provision of the Plan shall be held invalid or unenforceable, such invalidity or unenforceability shall not effect any other provisions hereof and the Plan shall be construed and enforced as if such provisions had not been included.
- 12.8 The headings and captions herein are provided for convenience only, and shall not be construed as part of the Plan, and shall not be employed in the construction of the Plan.
- 12.9 Any benefit payable to or for the benefit of a payee who is a minor, an incompetent person, or is otherwise incapable of receipting therefore shall be deemed paid when paid to such person's guardian or to the party providing, or a reasonably appearing to provide, the care for such person, and such payment shall fully discharge the Employer, the Committee, the Board and all other parties with respect thereto.

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EXHIBIT A

The following additional deemed investment may be elected by a Participant:

1. Life Insurance - A Participant (who is insurable) may elect, at the time and in the manner specified by the Committee, to direct that any portion or all of the amounts elected to be deferred under Section 3.2 of the Plan be deemed invested in a life insurance contract on the Participant's life with the amount of the death benefit determined by the Committee (taking into account, among other things the Participant's insurability) and permitting the Participant to direct the investment of any funds deemed invested under the insurance contract in excess of that necessary to keep the death benefit in force. Upon a distribution event under Article 4, and notwithstanding anything in the Plan to the contrary, the Committee may determine to distribute an insurance contract to the Participant in the event that the Company had determined to purchase such a life insurance contract in light of the Participant's election hereunder. If the Company determines to purchase a contract hereunder, it may permit the Participant to designate a beneficiary under the contract to receive the death benefit in the event of the Participant's death prior to a distribution event under Article 4, which shall be taken into account in determining whether any additional sums are owed under Article 5.

AQUA AMERICA, INC.
2005 DIRECTOR DEFERRAL PLAN

In recognition of the services provided by non-employee directors, Aqua America, Inc. wishes to make a vehicle available to them that will facilitate the provision of additional retirement benefits to those individuals under the terms and conditions hereinafter set forth. This Plan is intended to replace the Philadelphia Suburban Corporation Director Deferral Plan (the "Prior Deferral Plan") and no further deferrals will be credited under the Prior Deferral Plan after the effective date of this Plan. The Prior Deferral Plan shall remain in effect with respect to deferrals made prior to January 1, 2005.

ARTICLE 1
DEFINITIONS

1.1 "Account" means a bookkeeping account established pursuant to Section 3.1 which reflects the amount standing to the credit of the Participant under the Plan.

1.2 "Affiliated Company" means any affiliate or subsidiary of the Company.

1.3 "Beneficiary" means the person(s) designated by a Participant to receive any benefits payable under this Plan subsequent to the Participant's death. The Committee shall provide a form for this purpose. In the event a Participant has not filed a Beneficiary designation with the Company, the Beneficiary shall be the Participant's estate.

1.4 "Board" means the Board of Directors of the Company or the board of directors of an Employer.

1.5 "Committee" means the Compensation Committee of the Board which shall act for the Company in making decisions and performing specified duties with respect to the Plan.

1.6 "Company" means Aqua America, Inc. and its successors.

1.7 "Director" means each individual who serves as a non-employee member of the Board.

1.8 "Director's Fees" means the annual amount of retainer paid by the Company to a Director for any calendar year including meeting fees, committee fees and fees for committee chairs.

1.9 "Effective Date" means January 1, 2005.

1.10 "Employer" means the Company and/or any Participating Employer, either collectively or individually, as the context requires.

1.11 "Participant" means any Director.

1.12 "Participating Employer" means any Affiliated Company which is designated by the Board as a Participating Employer under the Plan and whose designation as such has become effective upon acceptance of such status by the board of directors of the Affiliated Company. A Participating Employer may revoke its acceptance of such designation at any time, but until such acceptance has been revoked, all the provisions of the Plan and amendments thereto shall apply to each Director of the Participating Employer. In the event the designation as a Participating Employer is revoked by the board of directors of an Affiliated Company, the Plan shall be deemed terminated only with respect to such Participating Employer.

1.13 "Plan" means the Aqua America, Inc. 2005 Director Deferral Plan as the same is set forth herein, and as it may be amended from time to time.

1.14 "Plan Year" means the calendar year.

1.15 "Termination from Service" means the Director's resignation or other termination from service as a member of the Board for any reason. Except

as otherwise provided herein, a Termination from Service shall be deemed to have occurred on the last day of the Director's service as a member of the Board.

ARTICLE 2
ELIGIBILITY

2.1 Each Director shall be eligible to participate in the Plan on the first day of the calendar quarter following election as a Director. Participants in the Prior Deferral Plan who are Directors shall be eligible to participate in the Plan as of the Effective Date.

ARTICLE 3
BENEFITS

3.1 The Employer shall create and maintain on its books an Account for each Participant to which it shall credit amounts contributed to the Plan pursuant to this Article 3. The Employer shall also credit each Participant's Account with deemed earnings for each Plan Year in accordance with the provisions of Article 8 hereof.

3.2 Prior to the commencement of any Plan Year, a Participant may elect to have the Employer credit to the Participant's Account an amount equal to any whole percentage or dollar amount (or shares of stock of the Employer ("Shares") to the extent that the Director's Fees would otherwise be paid in Shares) of the Participant's Director's Fees if any, to be earned for such Plan Year. If an election is made to have a contribution credited to the Participant's Account for a Plan Year, the credit shall be made at the time that such amount would otherwise have been paid (or Shares distributed) and shall reduce the Participant's Director's Fees with respect to that Plan Year by a corresponding amount. The Committee may establish minimum or maximum amounts that may be deferred under this Section and may change such standards from time to time. Any such limits shall be communicated by the Committee to the Participants prior to the commencement of a Plan Year. In addition, at the time of his or her deferral election for

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each Plan Year, a Participant shall elect the form of payment, as described in Section 4.1 below, with respect to deferred Director's Fees for the upcoming Plan Year.

3.3 Any elections under this Article shall be made in writing on such form as the Committee shall specify. Any election by a Director pursuant to this Section 3.3 shall be irrevocable and may not be modified in any respect.

ARTICLE 4
DISTRIBUTIONS TO PARTICIPANTS

4.1 A Participant's benefit under the Plan shall be distributed in one lump sum (including Shares to the extent the Director elected to defer the receipt of such Shares pursuant to Section 3.2), or, if the value of the Participant's Account is at least \$25,000, in 12 annual installments (with the balance to be distributed, including Shares, if applicable, continuing to be credited with deemed earnings for each subsequent Plan Year in accordance with the provisions of Article 8 hereof) equal to $\frac{1}{12}$, $\frac{1}{11}$, $\frac{1}{10}$, $\frac{1}{9}$, $\frac{1}{8}$, $\frac{1}{7}$, $\frac{1}{6}$, $\frac{1}{5}$, $\frac{1}{4}$, $\frac{1}{3}$, $\frac{1}{2}$, and $\frac{1}{1}$ of the balance then credited to the Participant's Account, and shall be paid, or commence, as soon as practicable following the completion of the valuation of the Participant's Account for the last day of the month in which the Participant has a Termination from Service as previously elected by the Participant. Notwithstanding anything herein to the contrary in the event that such a Participant fails to make an election, distribution shall be in the form of one lump sum payment, including Shares, paid as soon as practicable after the first day of the year following the date the Participant has a Termination from Service. Interest credited in accordance with Article 8 during the period in which periodic installments are paid pursuant to this Section 4.1 shall be distributed currently.

4.2 In the event that a Participant incurs a "significant financial hardship" while a Participant, as determined by the Committee, the Participant may apply, in writing, for a withdrawal of all or a portion of the balance credited to the Participant's Account (including Shares, if elected by the Participant) in the form of a lump sum. All determinations by the Committee regarding the existence of a financial hardship shall be made in accordance with the Section 409A of the Internal Revenue Code of 1986, as amended. The Committee

shall determine whether to permit a such a withdrawal and, based upon the Participant's application, the amount necessary to satisfy that hardship, which shall be distributed in a single sum (including any Shares, as elected by the Director) as soon as practicable after the Committee's determination. Such a request shall be approved, however, only upon a finding that the Participant has suffered a severe financial hardship which has resulted from an illness or accident of the Participant, the Participant's spouse, or a dependent (as defined in section 152(a) of the Code) of the Participant, loss of the Participant's property due to casualty, or other similar extraordinary and unforeseeable circumstances arising as a result of events beyond the Participant's control, and then only in an amount necessary to eliminate such hardship plus amounts necessary to pay taxes reasonably anticipated as a result of the distribution, after taking into account the extent to which such hardship is or may be relieved through reimbursement or compensation by insurance or by liquidation of the Participant's assets (to the extent the liquidation of such assets would not itself cause severe financial hardship).

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4.3 The Committee may establish rules allowing Participants to make a "second election" to postpone payment of his or her Account, in accordance with section 409A of the Code and the regulations thereunder. In that event, (i) the subsequent election may not take effect unless the Participant is still providing service to an Employer for at least 12 months after the date on which the election is made and (ii) except with respect to an election related to payment upon death, disability or a severe financial hardship, the first payment with respect to which such election is made must be deferred for a period of not less than five years from the date such payment would otherwise have been made.

ARTICLE 5 DEATH BENEFIT

5.1 In the event of the death of a Participant prior to the payment of the full benefit due pursuant to Article 4, the Participant's Beneficiary shall receive a lump sum distribution equal to the balance of the Participant's Account on the date of death; provided, however, in the event of the death of a Participant who was a Director, after payment of annual installments has commenced pursuant to Section 4.1 hereof, the Participant's Beneficiary will continue to receive the remaining annual installment payments due following the Participant's death. The lump sum benefit payment to the Beneficiary will be made as soon as practicable following the completion of the valuation of the deceased Participant's Account.

ARTICLE 6 VESTING

6.1 The balance credited to a Participant's Account attributable to Section 3.2 shall be fully vested at all times.

ARTICLE 7 FUNDING

7.1 The Board may, but shall not be required to, authorize the establishment of a trust by the Employer to serve as the funding vehicle for the benefits described in Article 3 hereof. In any event, the Employer's obligation hereunder shall constitute a general, unsecured obligation, payable solely out of its general assets, and no Participant shall have any right to any specific assets of the Employer. In addition, it is the intention of the Employer that the Plan be unfunded for tax purposes and for purposes of Title I of the Employee Retirement Income Security Act of 1974, as amended.

ARTICLE 8 INVESTMENTS

8.1 The balance credited to a Participant's Account (other than Shares) shall be deemed to be invested in an interest bearing instrument which shall provide for interest to be credited and compounded monthly at an effective rate equal to 100 basis points in excess of the prime commercial lending rate established by Mellon Bank N.A., or such other bank determined by the Committee to be the Company's primary bank as of the beginning of any Plan Year, as in

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effect on the 15th day of each month (or if such day is a non-business day, on the first business day thereafter) during which there is a positive balance in a Participant's Account. Interest shall be applied to the average balance of each Participant's Account during the prior 30-day period. The Committee may determine to make available for Directors, and announce to those Directors the procedure to elect, other deemed forms of investment for the amounts credited to the Accounts. Such other forms of investment shall be set forth in Exhibit A attached to this Plan. A Director's Account, to the extent credited with any Shares, shall be deemed to earn any dividends paid with respect to such Shares and the accumulated dividends, as and when sufficient in amount, shall be deemed invested in additional whole Shares.

ARTICLE 9 ADMINISTRATION

9.1 The Committee shall have full power and authority to interpret the Plan, to prescribe, amend and rescind any rules, forms and procedures as it deems necessary or appropriate for the proper administration of the Plan and to make any other determinations and to take any other such actions as it deems necessary or advisable in carrying out its duties under the Plan. All action taken by the Committee arising out of, or in connection with, the administration of the Plan or any rules adopted thereunder, shall, in each case, lie within its sole discretion, and shall be final, conclusive and binding upon the Employer, the Board, all Employees, all beneficiaries of Employees and all persons and entities having an interest therein.

9.2 Members of the Committee shall serve without compensation for their services unless otherwise determined by the Board. All expenses of administering the Plan shall be paid by the Employer.

9.3 The Company shall indemnify and hold harmless each member of the Committee from any and all claims, losses, damages, expenses (including counsel fees) and liability (including any amounts paid in settlement of any claim or any other matter with the consent of the Board) arising from any act or omission of such member, except when the same is due to gross negligence or willful misconduct.

9.4 Any decisions, actions or interpretations to be made under the Plan by the Company, the Employer or the Committee (other than in the administration of the Plan) shall be made in its sole discretion, not in any fiduciary capacity and need not be uniformly applied to similarly situated individuals and shall be final, binding and conclusive on all persons interested in the Plan.

ARTICLE 10 AMENDMENT

10.1 The Plan may be amended by the Committee at any time and from time to time all without prior notice to any person or entity; provided, however, that no such amendment shall have the effect of divesting a Participant of the benefit which the Participant would otherwise receive hereunder at the time the amendment is adopted. Without limiting the foregoing, the Committee may amend the Plan in any manner that it deems appropriate, including amending

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outstanding deferral elections, if necessary or appropriate to comply with changes to applicable law, without the consent of any Participant.

ARTICLE 11 TERMINATION

11.1 Continuance of the Plan is completely voluntary and is not assumed as a contractual obligation of the Employer. The Committee, acting on behalf of the Employer, shall have the right to terminate the Plan in whole or in part at any time all without prior notice to any person or entity; provided, however, that such termination shall not have the effect of divesting a Participant of the benefit which the Participant would otherwise receive hereunder at the time of the termination. Without limiting the foregoing, the Committee may terminate the Plan or outstanding deferral elections as it deems appropriate, if necessary or appropriate to comply with changes to applicable law, without the consent of any Participant.

ARTICLE 12

MISCELLANEOUS

12.1 Nothing contained herein shall be construed as conferring upon a Director the right to continue in such capacity.

12.2 The rights and obligations created hereunder shall be binding on a Participant's heirs, executors and administrators and on the successors and assigns of the Employer.

12.3 The provisions of the Plan shall be construed and applied under the laws of the Commonwealth of Pennsylvania.

12.4 The rights of any Participant under this Plan are personal and may not be assigned, transferred, pledged or encumbered. Any attempt to do so shall be void. In addition, a Participant's rights hereunder are not subject, in any manner, to anticipation, alienation, sale, transfer, assignment, pledge, encumbrance, attachment or garnishment by creditors of the Participant or the Participant's Beneficiary.

12.5 If any provision of the Plan shall be held invalid or unenforceable, such invalidity or unenforceability shall not effect any other provisions hereof and the Plan shall be construed and enforced as if such provisions had not been included.

12.6 The headings and captions herein are provided for convenience only, and shall not be construed as part of the Plan, and shall not be employed in the construction of the Plan.

12.7 Any benefit payable to or for the benefit of a payee who is a minor, an incompetent person, or is otherwise incapable of receipting therefore shall be deemed paid when paid to such person's guardian or to the party providing, or a reasonably appearing to provide, the care for such person, and such payment shall fully discharge the Employer, the Committee, the Board and all other parties with respect thereto.

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EXHIBIT A

The following additional deemed investments may be elected by a Director.

No additional investments as of January 1, 2005.

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DIRECTORS' COMPENSATION

On December 9, 2004, the Board of Directors approved the following recommendations of the Executive Compensation and Employee Benefits Committee regarding compensation for Aqua America's Non-employee Directors:

Effective January 1, 2005, Non-Employee Director members of the Board of Directors will receive an annual retainer fee of \$12,500, payable quarterly, plus an annual grant of restricted stock with a value of \$25,000 to be issued on the first of the month following the Annual Meeting of Shareholders. The restricted stock vests six months after the date of grant. Non-Employee Directors also receive a fee of \$1,500 for attendance at each meeting of the Board of Directors and a meeting fee for attendance at each committee meeting of \$1,250 for the Audit Committee and \$1,000 for other committees. In addition, each committee Chairman who is a Non-Employee Director receives an annual retainer fee of \$5,000 for the Chairmen of the Audit Committee and Corporate Governance Committee and \$2,500 for the Chairmen of other committees.

All directors are reimbursed for reasonable expenses incurred in connection with attendance at Board or Committee meetings. Directors who are full-time employees of Aqua America do not receive a retainer or fees for service on the Board of Directors or committees of the Board. Directors are eligible to defer part or all of their fees under Aqua America's Director Deferral Plan. Amounts deferred accrue interest at the prime interest rate plus 1.0%. Amounts deferred are not funded.

AQUA AMERICA, INC.

SELECTED PORTIONS OF ANNUAL REPORT TO SHAREHOLDERS FOR THE YEAR ENDED
DECEMBER 31, 2004

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS
(In thousands of dollars, except per share amounts)

FORWARD-LOOKING STATEMENTS

This report by Aqua America, Inc. ("Aqua America," "we" or "us") contains, in addition to historical information, forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements involve risks, uncertainties and other factors, many of which are outside our control, that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. In some cases you can identify forward-looking statements where statements are preceded by, followed by or include the words "believes," "expects," "anticipates," "plans," "future," "potential" or the negative of such terms or similar expressions. Forward-looking statements in this report, include, but are not limited to, statements regarding:

- o recovery of capital expenditures and expenses in rates;
- o projected capital expenditures and related funding requirements;
- o dividend payment projections;
- o future financing plans;
- o future pension contributions;
- o opportunities for future acquisitions, the success of pending acquisitions and the impact of future acquisitions;
- o acquisition-related costs and synergies;
- o the capacity of our water supplies and facilities;
- o general economic conditions;
- o The impact of geographic diversity on our exposure to unusual weather; and
- o The impact of accounting pronouncements.

Because forward-looking statements involve risks and uncertainties, there are important factors that could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including but not limited to:

- o changes in general economic, business and financial market conditions;
- o changes in government regulations and policies, including environmental and public utility regulations and policies;
- o changes in environmental conditions, including those that result in water use restrictions;
- o abnormal weather conditions;
- o changes in capital requirements;

- o changes in our credit rating;
- o our ability to integrate businesses, technologies or services which we may acquire;
- o our ability to manage the expansion of our business;
- o the extent to which we are able to develop and market new and improved services;

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AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)
(In thousands of dollars, except per share amounts)

- o the effect of the loss of major customers;
- o unanticipated capital requirements;
- o our ability to retain the services of key personnel and to hire qualified personnel as we expand;
- o increasing difficulties in obtaining insurance and increased cost of insurance;
- o cost overruns relating to improvements or the expansion of our operations; and
- o civil disturbance or terroristic threats or acts.

Given these uncertainties, you should not place undue reliance on these forward-looking statements. You should read this report with the understanding that our actual future results may be materially different from what we expect. These forward-looking statements represent our estimates and assumptions only as of the date of this report. Except for our ongoing obligations to disclose material information under the federal securities laws, we are not obligated to update these forward-looking statements, even though our situation may change in the future. We qualify all of our forward-looking statements by these cautionary statements.

GENERAL INFORMATION

Name Change

On January 16, 2004, we changed our name to Aqua America, Inc. from Philadelphia Suburban Corporation. In addition, we changed our ticker symbol to WTR from PSC on the New York Stock Exchange and Philadelphia Stock Exchange on January 20, 2004.

Overview

Aqua America, Inc. is the holding company for regulated utilities providing water or wastewater services to more than 2.5 million people in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Florida, Indiana, Virginia, Maine, Missouri, New York and South Carolina. Our largest operating subsidiary, Aqua Pennsylvania, Inc. - formerly Pennsylvania Suburban Water Company, accounts for approximately 57% of our operating revenues and provides water or wastewater services to approximately 1.3 million residents in the suburban areas north and west of the City of Philadelphia and in 21 other counties in Pennsylvania. Our other subsidiaries provide similar services in 12 other states. In addition, we provide water and wastewater service through operating and maintenance contracts with municipal authorities and other parties close to our operating companies' service territories. We are the largest U.S.-based publicly-traded water utility based on number of people served.

The mission of the investor-owned water utility industry is to provide quality and reliable water service at an affordable price for the customer, and provide a fair return to its shareholders. A number of challenges face the industry, including:

- o strict environmental, health and safety standards;

- o the need for substantial capital investment;
- o economic regulation by state, and/or in some cases local, government; and
- o the impact of weather and drought conditions on water sales demand.

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AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)
(In thousands of dollars, except per share amounts)

Aqua America, Inc. strives to achieve the industry mission by effective planning and efficient use of its resources to meet the industry challenges. We maintain a rate case management capability to pursue timely and adequate returns on the capital investments that we make in improving or replacing water mains, treatment plants and other infrastructure. This factor is important in our continued profitability and in providing a fair return to our shareholders, and thus providing access to capital markets to help fund these investments. Often these utility investments are required by a changed federal or state environmental standard, to improve our ability to deliver quality customer service, or to assist in our ability to supply water in sufficient quantities for future demand or when experiencing drought conditions. A strategy to meet the above challenges is to actively explore opportunities to expand our utility operations through acquisitions of water and wastewater utilities either in areas adjacent to our existing service areas or in new service areas. This growth-through-acquisition strategy allows us to operate more efficiently and provides an important source for possible future growth. The ability to successfully execute this strategy and meet the industry challenges is largely due to our qualified and trained workforce, which we strive to retain by treating employees fairly and providing our employees with development and growth opportunities.

We believe that acquisitions will continue to be an important source of growth for us. With more than 50,000 community water systems in the U.S., 84% of which serve less than 3,300 customers, the water industry is the most fragmented of the major utility industries (telephone, natural gas, electric, water and wastewater). In the states where we operate, we believe there are over 22,000 public water systems of widely varying size, with the majority of the population being served by government-owned water systems.

Although not as fragmented as the water industry, the wastewater industry in the U.S. also presents opportunities for consolidation. According to the U.S. Environmental Protection Agency's (EPA) most recent survey of publicly-owned wastewater treatment facilities in 2000, there are approximately 16,000 such facilities in the nation serving approximately 72% of the U.S. population. The remaining population represents individual homeowners with their own treatment facilities; for example, community on-lot disposal systems and septic tank systems. The vast majority of wastewater facilities are government-owned rather than privately-owned. The EPA survey also indicated that there are approximately 6,600 wastewater facilities in operation or planned in the 13 states where we operate.

Because of the fragmented nature of the water and wastewater utility industries, we believe that there are many potential water and wastewater system acquisition candidates throughout the United States. We believe the factors driving the consolidation of these systems are:

- o the benefits of economies of scale;
- o increasingly stringent environmental regulations;
- o the need for capital investment; and
- o the need for technological and managerial expertise.

On June 1, 2004, we acquired the capital stock of Heater Utilities, Inc. for \$48,000 in cash and the assumption of long-term debt of \$19,219 and short-term debt of \$8,500. The acquired operation provides water and wastewater service to over 50,000 water and wastewater customers primarily in the areas of suburban Raleigh, Charlotte, Gastonia and Fayetteville, North Carolina. On June 30, 2004, we acquired certain utility assets of Florida Water Services Corporation, comprised of 63 water and wastewater systems located in central

Florida for \$14,747 in cash. In accordance with Florida procedures, the acquisition remains subject to regulatory approval by the Florida Public Service Commission. This process is not expected to be completed prior to September 2005. The operating results of these acquisitions have been included in our consolidated financial statements beginning on the respective acquisition dates. Under the terms of the purchase agreement, the Commission's review process may result in an adjustment of the final purchase price based on the Commission's determination of plant investment for the systems. The final purchase price is not expected to result in the recognition of goodwill.

AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)
(In thousands of dollars, except per share amounts)

On July 31, 2003, we completed the acquisition of four operating water and wastewater subsidiaries of AquaSource, Inc., a subsidiary of DQE, Inc., including selected, integrated operating and maintenance contracts and related assets, for \$178,428 in cash, as adjusted for a purchase price reduction received in August 2004 of \$12,289 pursuant to the purchase agreement. The acquired operations of AquaSource serve over 130,000 water and wastewater customer accounts in 11 states; including the Connecticut and Kentucky operations which were subsequently sold to other parties. The operating results of AquaSource have been included in our consolidated financial statements beginning August 1, 2003. Please refer to the section captioned "Acquisitions" for an expanded discussion of acquisitions.

We are actively exploring other opportunities to expand our water and wastewater utility operations through acquisitions or otherwise. We intend to continue to pursue acquisitions of municipally-owned and investor-owned water and wastewater systems of all sizes that provide services in areas adjacent to our existing service territories or in new service areas.

Following are our selected five-year financial statistics:

Years ended December 31,	2004 (a)	2003 (b)	2002 (c)	2001	2000 (d)
Operating revenues	\$442,039	\$367,233	\$322,028	\$307,280	\$274,014
Operations and maintenance expense	\$178,345	\$140,602	\$117,735	\$111,885	\$101,741
Net income available to common stock	\$ 80,007	\$ 70,785	\$ 67,154	\$ 60,005	\$ 52,784
Capital expenditures	\$195,736	\$163,320	\$136,164	\$124,088	\$129,740
OPERATING STATISTICS					
Selected operating results as a percentage of operating revenues:					
Operations and maintenance	40.3%	38.3%	36.6%	36.4%	37.1%
Depreciation and amortization	13.3%	14.0%	13.8%	13.1%	12.4%
Taxes other than income taxes	6.2%	5.9%	6.0%	6.8%	8.2%
Interest expense, net	11.0%	12.2%	12.5%	11.9%	12.9%
Net income available to common stock	18.1%	19.3%	20.9%	19.5%	19.3%
Effective tax rates	39.4%	39.3%	38.5%	39.3%	39.2%

(a) Net income available to common stock and net income includes the gain of \$1,522 (\$2,342 pre-tax) realized on the sale of our Geneva, Ohio water system. The gain is reported in the 2004 consolidated statement of income as a reduction to operations and maintenance expense.

(b) 2003 includes five months of financial results for the AquaSource operations acquired in July 2003.

(c) Net income available to common stock and net income includes the gain of \$3,690 (\$5,676 pre-tax) realized on the sale of a portion of our Ashtabula, Ohio water system.

(d) Net income available to common stock and net income includes the gain of \$2,236 (\$4,041 pre-tax) for the partial recovery of the merger costs related to the merger with Consumers Water Company.

We consider the following nonfinancial measure and financial measures to be the fundamental basis by which we evaluate our performance: number of customers, operating revenues, net income and our dividend rate on common stock. In addition, we consider other key financial measures in evaluating our operating results: the ratio of operations and maintenance expense compared to operating revenues (this percentage is termed "operating expense ratio"); return on revenues (net income divided by operating revenues); and earnings before interest, taxes, depreciation and amortization ("EBITDA"). These measurements are reviewed regularly and compared to historical periods as well as our operating budget as approved by the Aqua America, Inc. Board of Directors.

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AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)
(In thousands of dollars, except per share amounts)

Our operating expense ratio is one measure that we use to evaluate our operating efficiency and management effectiveness. As reported in the above table and as anticipated, our operating expense ratio increased for 2004 over 2003, and 2003 as compared to 2002 as a result of the additional operating costs associated with the AquaSource acquisition which closed on July 31, 2003. Our 2004 results reflect a full twelve months of operating results for this acquisition and only five months in 2003. The business model of the acquired AquaSource operations, generally referred to as our Aqua South operations, are different from the rest of the Aqua America operations. The Aqua South operations are comprised of approximately 600 small systems, which are generally clustered in regions to achieve some level of operating efficiency. However, the small, separate systems of the Aqua South operations results in the additional operating revenues generated by the Aqua South operations being accompanied by a higher ratio of operations and maintenance expenses than the level Aqua America experiences in the rest of the Aqua America operations. The Aqua South operations can be characterized as having relatively-higher fixed costs to operate in contrast to the rest of the Aqua America operations which generally consist of larger, interconnected systems resulting in higher fixed capital costs (utility plant investment) and lower operating costs per customer. For the twelve-month period ending June 30, 2003, the last reporting period before the July 31, 2003 closing of AquaSource, our operating expense ratio declined to 36.5%, from 36.6% for the year ended December 31, 2002. We are implementing management systems over time that will allow us to further control costs and improve efficiencies, but the effect of this acquisition will be to increase our overall operating expense ratio from the levels experienced during the preceding five years. Consequently, as anticipated our return on revenues, net income divided by operating revenues, in 2004 was lower than in the previous four years as a result of the impact of the higher cost of Aqua South's operations.

Following are our selected five-year operating and sales statistics:

Years ended December 31,		2004	2003	2002	2001	2000
Customers	Residential water	702,367	624,355	535,506	526,776	512,442
	Commercial water	33,720	33,015	30,355	29,745	29,317
	Industrial water	1,365	1,397	1,423	1,454	1,446
	Other water	15,700	20,483	16,466	9,947	9,500
	Wastewater	82,360	70,241	21,724	19,615	12,441
	Total	835,512	749,491	605,474	587,537	565,146
Operating Revenues (a)	Residential water	\$ 264,910	\$218,487	\$197,190	\$ 188,303	\$ 170,597
	Commercial water	65,605	61,343	55,962	53,103	47,109
	Industrial water	17,377	17,675	17,221	16,141	14,943
	Other water	44,593	40,048	36,255	35,681	29,582
	Wastewater	35,931	17,874	8,210	6,960	5,414
	Other	13,623	11,806	7,190	7,092	6,369
Total	\$ 442,039	\$367,233	\$322,028	\$ 307,280	\$ 274,014	

(a) 2003 includes five months of financial results for the operations acquired in the AquaSource acquisition.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)
(In thousands of dollars, except per share amounts)

RESULTS OF OPERATIONS

Our net income has grown at an annual compound rate of approximately 17.1% during the five-year period ended December 31, 2004. The five year annual compound growth rate is higher than the rate typically experienced due to the base year 1999 results including the after-tax merger costs of \$8,596 associated with the Consumers Water Company merger. As a comparison, our net income for the periods ended December 31, 2004 has grown at annual compound rate of approximately 10.1% during the past six years, 11.0% during the past four years, and 10.0% during the past three years. During the past five years, operating revenues grew at a compound rate of 11.5% and total expenses, exclusive of income taxes, grew at a compound rate of 11.0%.

Operating Revenues

The growth in revenues over the past five years is a result of increases in both the customer base and in water rates. The number of customers increased at an annual compound rate of 8.8% in the past five years primarily as a result of acquisitions of water and wastewater systems, including the mid-year 2004 Heater and Florida Water Services acquisitions, and the AquaSource acquisition completed July 2003. Acquisitions made during the five-year period ended December 31, 2004 have provided water and wastewater revenues of approximately \$90,187 in 2004, \$34,960 in 2003 and \$8,758 in 2002. Excluding the effect of acquisitions, our customer base increased at a five-year annual compound rate of 1.2%. Rate increases implemented during the past three years have provided additional operating revenues of approximately \$15,800 in 2004, \$19,900 in 2003 and \$14,700 in 2002. In addition to regulated water and wastewater operating revenues, we had other non-regulated revenues that were primarily associated with operating and maintenance contracts, and data processing service fees of \$13,623 in 2004, \$11,806 in 2003 and \$7,190 in 2002. The increases in 2004 and 2003 over the previous year resulted primarily from the additional revenues from contract operations associated with the July 2003 AquaSource acquisition.

Economic Regulation - Most of our water and wastewater utility operations are subject to regulation by their respective state regulatory commissions, which have broad administrative power and authority to regulate rates and charges, determine franchise areas and conditions of service, approve acquisitions and authorize the issuance of securities. A small number of our operations are subject to rate regulation by county or city government. The profitability of our utility operations is influenced a great extent by the timeliness and adequacy of rate allowances in the various states in which we operate. Accordingly, we maintain a rate case management capability to provide that the tariffs of the utility operations reflect, to the extent practicable, the timely recovery of increases in costs of operations, capital, taxes, energy, materials and compliance with environmental regulations. In assessing our rate case strategy, we consider the amount of utility plant additions and replacements made since the previous rate decision, the changes in the cost of capital, changes in the capital structure and changes in other costs. Based on these assessments, our utility operations periodically file rate increase requests with their respective state regulatory commissions.

On August 5, 2004, the Pennsylvania Public Utility Commission (PAPUC) granted our Pennsylvania operating subsidiary a \$13,800 base rate increase. The rates in effect at the time of the filing included \$11,200 in Distribution System Improvement Charges ("DSIC") or 5.0% above the prior base rates. Consequently, the total base rates increased by \$25,000 and the DSIC was reset to zero. On August 1, 2002, the PAPUC granted our Pennsylvania operating subsidiary a \$21,226 base rate increase. The rates in effect at the time of the filing included \$9,400 in DSIC at 5.0%. Consequently, the total base rates increased by \$30,626 and the DSIC was reset to zero.

In May 2004, our operating subsidiary in Texas filed an application with the Texas Commission on Environmental Quality to increase rates by \$11,920 over a multi-year period. The application seeks to increase annual revenues in phases and is accompanied by a plan to defer and amortize a portion of our depreciation, operating and other tax expense over a similar multi-year period, such that the annual impact on operating income approximates the requested amount. The application is currently pending before the Commission. We commenced billing for the requested rates and implemented the deferral plan in August 2004, in accordance with authorization from the Texas Commission on

Environmental Quality in July 2004. The additional revenue billed and collected prior to the final ruling are subject to refund based on the outcome of the ruling. The revenue recognized and the expenses deferred by us reflect an estimate of the final outcome of the ruling.

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AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)
(In thousands of dollars, except per share amounts)

Our operating subsidiaries located in other states received rate increases representing estimated annualized revenues of \$6,673 in 2004 resulting from fourteen rate decisions, \$1,275 in 2003 resulting from eight rate decisions and \$3,024 in 2002 resulting from thirteen rate decisions. Revenues from these increases realized in the year of grant were approximately \$3,995 in 2004, \$839 in 2003 and \$1,403 in 2002. These operating subsidiaries currently have eleven rate requests in process requesting a \$6,513 increase in annual revenues. These requests are currently under review by the respective state regulatory commissions. During 2005, we intend to file twenty-two rate requests requesting an aggregate of approximately \$18,682 of increased annual revenues.

Revenue Surcharges - Four states in which we operate permit water utilities, and in some states wastewater utilities, to add a surcharge to their water or wastewater bills to offset the additional depreciation and capital costs associated with certain capital expenditures related to replacing and rehabilitating infrastructure systems. Prior to these mechanisms being approved, water and wastewater utilities absorbed all of the depreciation and capital costs of these projects between base rate increases without the benefit of additional revenues. The gap between the time that a capital project is completed and the recovery of its costs in rates is known as regulatory lag. The infrastructure rehabilitation surcharge mechanism is intended to substantially reduce regulatory lag which often acted as a disincentive to water and wastewater utilities to rehabilitate their infrastructure. In addition, our subsidiaries in certain states use a surcharge or credit on their bill to reflect certain allowable changes in costs until such time as these costs are fully incorporated in base rates.

Currently, Pennsylvania, Illinois, Ohio and Indiana allow for the use of infrastructure rehabilitation surcharges. In Pennsylvania, this mechanism is referred to as a DSIC. These mechanisms typically adjust periodically based on additional qualified capital expenditures completed or anticipated in a future period. The infrastructure rehabilitation surcharge is capped as a percentage of base rates, generally 5% of base rates, and is reset to zero when new base rates that reflect the costs of those additions become effective or when a utility's earnings exceed a regulatory benchmark. Infrastructure rehabilitation surcharges provided revenues of \$7,817 in 2004, \$8,147 in 2003 and \$5,518 in 2002.

Sendout - "Sendout" represents the quantity of treated water delivered to our distribution systems. We use sendout as an indicator of customer demand. Weather conditions tend to impact water consumption, particularly in our northern service territories during the late spring and summer months when nonessential and recreational use of water is at its highest. Consequently, a higher proportion of annual operating revenues is realized in the second and third quarters. In general during this period, an extended period of dry weather increases water consumption, while above average rainfall decreases water consumption. Also, an increase in the average temperature generally causes an increase in water consumption. Conservation efforts, construction codes which require the use of low flow plumbing fixtures, as well as mandated water use restrictions in response to drought conditions, also affect water consumption.

The geographic diversity of our customer base helps reduce our exposure to extreme or unusual weather conditions in any one area of our service territory. Our geographic diversity has continued to widen as a result of the Heater and Florida Water acquisitions which closed in mid-year 2004 and the AquaSource acquisition which closed in July 2003. During the year ended December 31, 2004, which included only the partial year operating revenues from the Heater and Florida Water acquisitions, our operating revenues were derived principally from the following states: 57% in Pennsylvania, 9% in Ohio, 7% in Illinois, 7% in Texas, 5% in New Jersey, and 4% in North Carolina.

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AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)
(In thousands of dollars, except per share amounts)

On occasion, drought warnings and water use restrictions are issued by governmental authorities for portions of our service territories in response to extended periods of dry weather conditions. The timing and duration of the warnings and restrictions can have an impact on our water revenues and net income. In general, water consumption in the summer months is affected by drought warnings and restrictions to a higher degree because nonessential and recreational use of water is highest during the summer months, particularly in our northern service territories. At other times of the year, warnings and restrictions generally have less of an effect on water consumption. During the period from November 2001 to December 2002, at various times in specific counties and to varying degrees, drought warnings or drought emergencies were declared by the Commonwealth of Pennsylvania for substantial portions of our Pennsylvania service territories. A drought warning calls for a 10 to 15 percent voluntary reduction of water use, particularly non-essential uses of water. A drought emergency imposes a ban on nonessential water use. Water use restrictions were also imposed and relaxed at various times during 2002 in our service territories in New Jersey. Currently there are no drought warnings or restrictions in any of the areas we serve.

Operations and Maintenance Expenses

Operations and maintenance expenses totaled \$178,345 in 2004, \$140,602 in 2003 and \$117,735 in 2002. Most elements of operating costs are subject to the effects of inflation, and changes in the number of customers served, and several elements are subject to the effects of changes in water consumption, weather and the degree of water treatment required due to variations in the quality of the raw water. The principal elements of operating costs are labor and employee benefits, electricity, chemicals, maintenance expenses and insurance costs. Electricity and chemical expenses vary in relationship to water consumption, raw water quality, and to a lesser extent the competitive electric market in some of the states in which we operate. Maintenance expenses are sensitive to extremely cold weather, which can cause water mains to rupture. Operations and maintenance expenses increased in 2004 as compared to 2003 by \$37,743 or 26.8% due to added operating costs associated with acquisitions of \$36,123, additional postretirement costs of \$2,110, increased accounting expense of \$1,496 for assessing internal control effectiveness under the Sarbanes-Oxley Act and higher water production expenses. Partially offsetting these increases were lower insurance costs due to the favorable settlement of insurance claims during 2004, and the gain on the sale of the Geneva, Ohio water system of \$2,342. In the consolidated statement of income for 2004, the gain on the sale of the Geneva water system is reported as a component of the line titled operations and maintenance expense. The impact of acquisitions is primarily the result of the effect of AquaSource for the full twelve-month period versus five months in 2003, and the mid-year 2004 acquisitions of Heater and the Florida Water Services systems.

Operations and maintenance expenses increased in 2003 as compared to 2002 by \$22,867 or 19.4% due to additional operating costs associated with acquisitions of \$18,526, primarily from AquaSource, higher postretirement costs, and additional maintenance costs, offset in part by reduced bad debt expense. The postretirement benefits expense increase resulted principally from higher pension costs and increased retiree medical costs. The increased maintenance expenses are primarily a result of additional main break repairs resulting from the relatively harsh winter weather experienced in early 2003 in our northern service territory.

Depreciation and Amortization Expenses

Depreciation expense was \$54,564 in 2004, \$48,522 in 2003 and \$41,424 in 2002, and has increased principally as a result of the significant capital expenditures made to expand and improve our utility facilities, and as a result of acquisitions of water systems.

Amortization expense was \$4,300 in 2004, \$2,941 in 2003 and \$2,898 in 2002. The increase in 2004 and 2003 is due to the amortization of the costs associated with, and other costs being recovered in, various rate filings. Expenses associated with filing rate cases are deferred and amortized over periods that generally range from one to three years.

AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
 FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)
 (In thousands of dollars, except per share amounts)

Taxes Other than Income Taxes

Taxes other than income taxes increased by \$5,989 or 27.7% in 2004 as compared to 2003 and \$2,140 or 11.0% in 2003 as compared to 2002. The increase in both 2004 and 2003 is due to additional taxes associated with acquisitions and increases in state taxes. The other taxes associated with acquisitions resulted from the effect of the July 2003 AquaSource acquisition for a twelve-month period in 2004 as compared to the five-month period in 2003, and the mid-year 2004 acquisitions of Heater Utilities and the systems of Florida Water.

Interest Expense, net

Net interest expense was \$48,679 in 2004, \$44,662 in 2003 and \$40,396 in 2002. Interest income of \$1,762 in 2004, \$395 in 2003 and \$287 in 2002 was netted against interest expense. Interest expense increased in 2004 and in 2003 primarily as a result of higher levels of borrowings, offset partially by the effects of decreased interest rates on borrowings. The higher level of average borrowings in 2004 and 2003 was used to finance the acquisition of AquaSource in July 2003, the Heater and Florida Water acquisitions in mid-year 2004, and capital expenditures. Interest income increased in 2004 due to \$532 of interest income in connection with the arbitration award related to the final purchase price for the AquaSource acquisition received in 2004 and additional interest income associated with acquisitions. Interest expense during 2004 was favorably impacted by a reduction in the weighted cost of long-term debt from 6.19% at December 31, 2003 to 6.00% at December 31, 2004.

Allowance for Funds Used During Construction

The allowance for funds used during construction (AFUDC) was \$2,304 in 2004, \$2,127 in 2003 and \$1,389 in 2002 and has varied over the years as a result of changes in the average balance of utility plant construction work in progress (CWIP), to which AFUDC is applied, and to changes in the AFUDC rate. The increase in 2004 is due to an increase in the average balance of CWIP to which AFUDC is applied. The increase in 2003 is due to an increase in the AFUDC rate as a result of tax-exempt borrowings for our multi-year infrastructure rehabilitation plan and an increase in the average balance of CWIP.

Gain on Sale of Water System

Gain on sale of water system represents the gain realized on the December 2002 sale of a portion of the Ashtabula, Ohio water system to the county government. The sale provided \$12,118 of net proceeds and resulted in 2002 pre-tax gain of \$5,676. The gain realized on the December 2004 sale of the Geneva, Ohio water system to the City of Geneva of \$2,342 is reported in the consolidated statement of income as a component of the line titled operations and maintenance expense.

Gain on Sale of Other Assets

Gain on sale of other assets totaled \$1,272 in 2004, \$5,692 in 2003 and \$2,079 in 2002 and consisted of gains on land and marketable securities sales. Gain on sale of land totaled \$869 in 2004, \$5,153 in 2003 and \$900 in 2002. Gain on sale of marketable securities totaled \$403 in 2004, \$539 in 2003 and \$1,179 in 2002.

Income Taxes

Our effective income tax rate was 39.4% in 2004, 39.3% in 2003 and 38.5% in 2002. The changes in the effective tax rates in 2004 and 2003 are due to differences between tax deductible expenses and book expenses.

FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)
(In thousands of dollars, except per share amounts)

Summary

Operating income was \$177,234 in 2004, \$153,561 in 2003 and \$140,504 in 2002 and net income available to common stock was \$80,007 in 2004, \$70,785 in 2003 and \$67,154 in 2002. Diluted income per share was \$0.85 in 2004, \$0.79 in 2003 and \$0.78 in 2002. The changes in the per share income in 2004 and 2003 over the previous years were due to the aforementioned changes in income and impacted by a 5.6% increase in the average number of common shares outstanding during 2004 and a 3.1% increase in the average number of common shares outstanding during 2003, respectively. The increase in the number of shares outstanding in 2004 and 2003 is primarily a result of the additional shares issued in common share offerings and through our dividend reinvestment plan, employee stock purchase plan and equity compensation plan.

Although we have experienced increased income in the recent past, continued adequate rate increases reflecting increased operating costs and new capital investments are important to the future realization of improved profitability.

Fourth Quarter Results

Net income available to common stock was \$22,474 in the fourth quarter of 2004 and \$18,606 in the same period of 2003. The change in net income is due to a \$14,230 increase in operating revenues, offset by increased operations and maintenance expense of \$3,373, increased interest expense of \$1,418, a lower gain on sales of other assets of \$973 and increased amortization expense of \$514. The increase in operating revenues was a result of additional revenues of \$9,006 resulting from an increase in water rates granted to our operating subsidiaries, and the additional revenues from acquisitions, offset partially by reduced infrastructure rehabilitation surcharge revenue of \$2,036. The reduction in infrastructure rehabilitation surcharge revenues is due to the August 2004 Pennsylvania rate increase which resulted in the DSIC being reset to zero concurrent with the increase in base water rates. The higher operations and maintenance expense is due primarily to the additional operating costs associated with acquisitions, offset partially by the gain on the December 2004 sale of the Geneva water system of \$2,342, and reduced insurance costs.

Effects of Inflation

As a regulated enterprise, our rates are established to provide recovery of costs and a return on our investment. Recovery of the effects of inflation through higher water rates is dependent upon receiving adequate and timely rate increases. However, rate increases are not retroactive and often lag increases in costs caused by inflation. During periods of moderate to low inflation, as has been experienced for the past several years, the effects of inflation on our operating results are not significant.

Security

In light of concerns regarding security in the wake of the September 11, 2001 terrorist attacks, we have increased security measures at our facilities. These increased security measures were not made in response to any specific threat. We are in contact with federal, state and local authorities and industry trade associations regarding information on possible threats and security measures for water utility operations. The cost of the increased security measures, including capital expenditures, is expected to be recoverable in water rates and is not expected to have a material impact on our results from operations or financial condition.

Net operating cash flow, dividends paid on common stock, capital expenditures, including allowances for funds used during construction, and expenditures for acquiring water and wastewater systems for the five years ended December 31, 2004 were as follows:

	Net Operating Cash Flow	Common Dividends	Capital Expenditures	Acquisitions of Utility Systems
2000	\$ 86,972	\$ 30,406	\$ 129,740	\$ 3,546
2001	102,165	34,234	124,088	9,517
2002	121,560	36,789	136,164	8,914
2003	143,373	39,917	163,320	192,331
2004	173,603	45,807	195,736	54,300
	\$ 627,673	\$ 187,153	\$ 749,048	\$ 268,608

Included in capital expenditures for the five-year period are: expenditures for the modernization and replacement of existing treatment plants, new water mains and customer service lines, rehabilitation of existing water mains and hydrants, and water meters. During this five-year period, we received \$45,494 of customer advances and contributions in aid of construction to finance new water mains and related facilities which are not included in the capital expenditures presented in the above table. In addition, during this period, we have made sinking fund contributions and retired debt in the amount of \$163,689, retired \$1,760 of preferred stock, and have refunded \$23,550 of customer advances for construction. Common dividends increased during the past five years as a result of an annual increase in the common dividends declared and paid and an increase in the shares outstanding during the period.

Our planned 2005 capital program, exclusive of the costs of new mains financed by advances and contributions in aid of construction, is estimated to be \$262,400 of which \$66,400 is for infrastructure rehabilitation surcharge-qualified projects. We have increased our capital spending for infrastructure rehabilitation in response to the infrastructure rehabilitation surcharge mechanisms, and should these mechanisms be discontinued for any reason, which is not anticipated, we would re-evaluate the magnitude our capital program. Our 2005 capital program, along with \$50,195 of sinking fund obligations and debt maturities, and \$33,444 of other contractual cash obligations, as reported in the section captioned "Contractual Obligations", is expected to be financed through internally-generated funds, our revolving credit facilities, the issuance of equity and the issuance of new long-term debt.

Future utility construction in the period 2006 through 2009, including recurring programs, such as the ongoing replacement of water meters, water treatment plant upgrades, storage facility renovations, the rehabilitation of water mains and additional transmission mains to meet customer demands, exclusive of the costs of new mains financed by advances and contributions in aid of construction, is estimated to require aggregate expenditures of approximately \$700,000. We anticipate that less than one-half of these expenditures will require external financing of debt and the additional issuance of common stock through our dividend reinvestment and stock purchase plans and possible future public equity offerings. We expect to refinance \$86,263 of sinking fund obligations and debt maturities during this period as they become due with new issues of long-term debt. The estimates discussed above do not include any amounts for possible future acquisitions of water systems or the financing necessary to support them.

AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)
(In thousands of dollars, except per share amounts)

Our primary source of liquidity is cash flows from operations, borrowings under various short-term lines of credit and other credit facilities, and customer advances and contributions in aid of construction. Our cash flow from operations, or internally-generated funds, is impacted by the timing of rate relief and water consumption. We fund our capital and acquisition programs through internally-generated funds, supplemented by short-term borrowings. Over time, we refinance our short-term borrowings with long-term debt and proceeds

from the issuance of common stock. The ability to finance our future construction programs, as well as our acquisition activities, depends on our ability to attract the necessary external financing and maintain internally-generated funds. Rate orders permitting compensatory rates of return on invested capital and timely rate adjustments will be required by our operating subsidiaries to achieve an adequate level of earnings and cash flow to enable them to secure the capital they will need and to maintain satisfactory debt coverage ratios.

Acquisitions

During the past five years, we have expended cash of \$268,608 and issued 1,317,017 shares of common stock, valued at \$16,400 at the time of the acquisition, related to the acquisitions of utility systems, primarily water utilities and some wastewater utilities. The operating results of these acquisitions have been included in our consolidated financial statements beginning on the respective acquisition date.

Pursuant to our strategy to grow through acquisitions, on June 1, 2004, we acquired the capital stock of Heater Utilities, Inc. for \$48,000 in cash and the assumption of long-term debt of \$19,219 and short-term debt of \$8,500. The acquired operation provides water and wastewater service to over 50,000 water and wastewater customers primarily in the areas of suburban Raleigh, Charlotte, Gastonia and Fayetteville, North Carolina. For the fiscal year ended December 31, 2003, Heater had operating revenues of \$19,489. The acquisition was accounted for as a purchase and accordingly, we recorded goodwill of \$18,842. In 2004, as part of the North Carolina Utilities Commission approval process for this acquisition, the Commission approved a mechanism through which we could recover up to two-thirds of the goodwill through customer rates in the future upon achieving certain objectives. We intend to pursue these objectives to facilitate recognition of this premium in customer rates. However, there can be no assurance that we will be able to achieve these objectives and recover such amount of goodwill, if any.

On June 30, 2004, we acquired certain utility assets of Florida Water Services Corporation, comprised of 63 water and wastewater systems located in central Florida for \$14,747 in cash, which is less than the depreciated original cost of these assets. In accordance with Florida procedures, the acquisition remains subject to regulatory approval by the Florida Public Service Commission and this process is not expected to be completed prior to September 2005. Under the terms of the purchase agreement, the Commission's review process may result in an adjustment of the final purchase price, which would be settled in cash, based on the Commission's determination of plant investment for the systems. Since the purchase price adjusts by the change in the determined plant investment or rate base, effectively the rate base adjustment is directly offset by the change in purchase price. The final purchase price is not expected to result in the recognition of goodwill.

The acquisition of Heater and the Florida Water Systems were initially funded by a portion of the proceeds from the issuance by Aqua America of an unsecured short-term note in May 2004. A portion of the short-term note was subsequently repaid by Aqua America with the proceeds from a November 2004 secondary equity offering, and a portion of the short-term note was refinanced through the February 2005 issuance of \$30,000 of unsecured notes. In November 2004, we sold 1,955,000 shares of common stock in a public offering for proceeds of \$42,600, net of expenses. In February 2005, Aqua America issued \$18,000 of notes due in 2015 with an interest rate of 5.01% and \$12,000 of notes due in 2020 with an interest rate of 5.20%.

AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued) (In thousands of dollars, except per share amounts)

Pursuant to our growth strategy, on July 31, 2003, we completed the acquisition of four operating water and wastewater subsidiaries of AquaSource, Inc., a subsidiary of DQE, Inc., including selected, integrated operating and maintenance contracts and related assets (individually and collectively the acquisition is referred to as "AquaSource") for \$190,717 in cash, as adjusted pursuant to the purchase agreement based on working capital at closing. On August 27, 2004, we were awarded and received \$12,289 plus interest in an

arbitration related to the calculation of the final purchase price under the terms of the purchase agreement, which resulted in a final purchase price of \$178,428. In the consolidated statement of cash flow for 2004, the \$12,289 award has been reported as proceeds on the line titled acquisitions of water and wastewater systems, net. The acquisition was initially funded by a portion of the proceeds from the July 2003 issuance of \$135,000 of unsecured notes due 2023, with an interest rate of 4.87%, and the issuance of a \$90,000 unsecured note by Aqua America. In August 2003, the \$90,000 unsecured note was repaid with the proceeds from the issuance of 5,000,000 shares of common stock through a shelf registration. The acquired operations of AquaSource serve over 130,000 water and wastewater customer accounts in 11 states (including the Connecticut and Kentucky operations which were subsequently sold to other parties). Please refer to the section captioned "Dispositions" for a discussion of the AquaSource operations located in Connecticut, Kentucky and New York. The acquisition provides an expanded platform from which to extend our growth-through-acquisition strategy of acquiring water and wastewater systems that are near or adjacent to our existing service territories. The AquaSource operations are comprised of approximately 600 small systems, which are generally clustered in regions to achieve some level of operating efficiency.

We continue to hold acquisition discussions with several water and wastewater systems. Generally acquisitions are expected to be financed through the issuance of equity (for the acquisition of some investor-owned systems) or funded initially with short-term debt with subsequent repayment from the proceeds of long-term debt or proceeds from equity offerings.

Dispositions

In December 2004, as a result of the settlement of a condemnation action, our Ohio operating subsidiary sold its water utility assets within the municipal boundaries of the City of Geneva in Ashtabula County, Ohio for net proceeds of approximately \$4,716, which was in excess of the book value for these assets. The proceeds were used to pay-down short-term debt and the sale resulted in the recognition in the fourth quarter of 2004 of a gain on the sale of these assets, net of expenses, of \$2,342. The gain is reported in the 2004 consolidated statement of income as a reduction to operations and maintenance expense. We continue to operate this water system for the City of Geneva under an operating contract that began upon the closing of the sale for a period through December 2006. The operating contract provides for an annual base operating fee of \$135 and allows for additional fees to be earned commensurate with the services provided. These water utility assets represent less than 1% of Aqua America's total assets, and the total number of customers included in the water system sold represents less than 1% of our total customer base.

We continue to review and evaluate for possible sale selected areas of our business and operating divisions that were acquired in July 2003 with the AquaSource operations. To date, we have completed the following sale transactions of operating divisions acquired as part of the AquaSource transaction:

- o In July 2004, we sold our only operation in Kentucky. The sale price approximates our investment in this operation. The operation represented approximately 0.2% of the operations acquired from AquaSource, Inc.
- o In October 2003, we completed the sale of our only operation in Connecticut. The sale price of \$4,000 approximates our investment in this operation. The operation represented approximately 2% of the operations acquired from AquaSource, Inc.

In May 2003, we announced an agreement for the sale of the AquaSource regulated operation located in New York to a New England-based water company. In January 2005, after the expiration of the sale agreement, we did not renew the sale agreement. The New York operations represented approximately 1% of the operations acquired from AquaSource, Inc.

In December 2002, as a result of the settlement of a condemnation action, our Ohio operating subsidiary sold to Ashtabula County, Ohio the water utility assets in the unincorporated areas of Ashtabula County and the area

within the Village of Geneva on the Lake for net proceeds of \$12,118, which was in excess of the book value for these assets. The proceeds were used to pay down short-term debt, and the sale resulted in the recognition in the fourth quarter of 2002 of a gain on the sale of these assets, net of expenses, of \$5,676. We continue to operate this water system for Ashtabula County, beginning after the closing of the sale, under a multi-year operating contract. The water utility assets sold represented less than 1% of our total assets, and the total number of customers included in the water system sold represented less than 1% of our total customer base.

The City of Fort Wayne, Indiana has authorized the acquisition, by eminent domain or otherwise, of a portion of the utility assets of one of the operating subsidiaries that we acquired in connection with the AquaSource acquisition in 2003. We have challenged whether the City is following the correct legal procedures in connection with the City's attempted condemnation and we have challenged the City's valuation of this portion of our system. The portion of the system under consideration represents approximately 1% of our total customer base. While we continue to discuss this matter with officials from the City of Fort Wayne, we continue to protect our interests in this proceeding. We believe that we will be entitled to fair market value for our assets if they are condemned, and that the fair market value will be in excess of the book value for such assets.

Despite these transactions, our strategy continues to be to acquire additional water and wastewater systems, to maintain our existing systems where there is a business or a strategic benefit, and to actively oppose unilateral efforts by municipal governments to acquire any of our operations.

Sources of Capital

Since net operating cash flow plus advances and contributions in aid of construction have not been sufficient to fully fund cash requirements, we issued approximately \$564,000 of long-term debt and obtained other short-term borrowings during the past five years. At December 31, 2004, we had short-term lines of credit and other credit facilities of \$198,000, of which \$159,190 was available. Our short-term lines of credit and other credit facilities are either payable on demand or have a 364-day term.

In April 2003, we filed a universal shelf registration with the SEC to allow for the sale, over time, of up to \$250,000 of various debt and equity securities, including common stock. To date, we have completed three issuances under the universal shelf registration:

- o In November 2004, we sold 1,955,000 shares of common stock in a public offering for proceeds of \$42,600, net of expenses. The net proceeds were used to repay a portion of our short-term debt. The short-term debt was incurred by Aqua America in connection with the Heater and Florida Water acquisitions.
- o In August 2003, we sold 5,000,000 shares of common stock in a public offering for proceeds of \$90,100, net of expenses. The net proceeds were used to repay an unsecured note of \$90,000. The indebtedness was incurred by Aqua America in connection with the acquisition of the operations that were purchased from AquaSource, Inc.
- o In May 2003, we sold 1,868,750 shares of common stock in a public offering for proceeds of \$33,100, net of expenses. The net proceeds were used to repay short-term debt, including the repayment of \$22,000 of indebtedness incurred in connection with our repurchase of 1,513,275 shares of our common stock from affiliates of Veolia Environnement, S.A., formerly Vivendi Environnement, S.A., in October 2002.

AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued) (In thousands of dollars, except per share amounts)

The balance remaining available for use under the universal shelf registration as of December 31, 2004 is \$77,517. In addition, we have a shelf registration statement filed with the SEC to permit the offering from time to time of shares of common stock and shares of preferred stock for acquisitions. During 2004 and 2003, no shares were issued from the acquisition shelf registration. During 2002, 178,664 shares of common stock totaling \$2,745, were issued to acquire water and wastewater systems. The balance remaining available

for use under the acquisition shelf registration as of December 31, 2004 is 2,218,947 shares. The form and terms of such securities shall be determined when and if these securities are issued under these shelf registrations.

In September 2000, we sold 2,583,008 shares of common stock in a public offering for net proceeds of \$29,689. The proceeds of this offering were used to make an equity contribution to our Pennsylvania operating subsidiary.

We offer a Dividend Reinvestment and Direct Stock Purchase Plan (Plan) that provides a convenient and economical way to purchase shares of Aqua America, Inc. Under the direct stock purchase portion of the Plan, shares are sold throughout the year. The dividend reinvestment portion of the Plan offers a 5% discount on the purchase of shares of common stock with reinvested dividends. As of the December 2004 dividend payment, holders of 16.9% of the common shares outstanding participated in the dividend reinvestment portion of the Plan. The shares issued under the Plan are either original issue shares or shares purchased by the Company's transfer agent in the open-market. During the past five years, we have sold 2,086,736 original issue shares of common stock for net proceeds of \$32,677 through the dividend reinvestment portion of the Plan and the proceeds were used to invest in our operating subsidiaries, to repay short-term debt, and for general corporate purposes.

Other Capital Transactions

In May 2002, Veolia Environnement, S.A., formerly Vivendi Environnement, S.A., which through its affiliates (collectively "VE") owned approximately 16.8% of our outstanding common stock, advised us of its decision to sell its investment in Aqua America. VE announced that its decision was part of its overall strategy to divest non-core assets and focus on other business strategies. In September 2002, in order to facilitate the orderly re-distribution of the shares held by VE into the market, we completed a secondary offering of 12,356,570 shares of Aqua America common stock held by VE. The number of outstanding shares of common stock was not changed and we did not receive any proceeds as a result of this secondary offering. In addition, in October 2002 we repurchased 1,513,275 shares of Aqua America common stock representing the remainder of the shares of Aqua America common stock held by VE. The repurchase of shares was funded with proceeds of \$22,000 from a short-term credit facility. In May 2003, this \$22,000 short-term credit facility was repaid with funds from the issuance of 1,868,750 shares of common stock through a shelf registration, providing proceeds of approximately \$33,100, net of expenses. The balance of the net proceeds were used to repay other short-term debt.

The Board of Directors has authorized us to purchase our common stock, from time to time, in the open market or through privately negotiated transactions. We have not purchased any shares under this authorization since 2000. As of December 31, 2004, 411,209 shares remain available for repurchase. Funding for future stock purchases, if any, is not expected to have a material impact on our financial position.

AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued) (In thousands of dollars, except per share amounts)

Contractual Obligations

The following table summarizes our contractual cash obligations as of December 31, 2004:

	Payments Due By Period						Total
	2005	2006	2007	2008	2009	Thereafter	
Long-term debt (a)	\$ 50,195	\$ 24,623	\$ 31,068	\$ 23,756	\$ 6,816	\$ 698,198	\$ 834,656
Operating leases (b)	2,926	2,309	1,669	1,336	969	15,907	25,116
Unconditional purchase obligations (c)	10,840	10,760	11,325	11,103	10,594	82,388	137,010
Other purchase obligations (d)	6,244	-	-	-	-	-	6,244
Postretirement benefit plans' obligations (e)	10,082	-	-	-	-	-	10,082
Other obligations (f)	3,352	400	400	267	130	-	4,549

Total	\$ 83,639	\$ 38,092	\$ 44,462	\$ 36,462	\$ 18,509	\$ 796,493	\$ 1,017,657
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- (a) Represents sinking fund obligations and debt maturities.
- (b) Represents operating leases that are noncancelable, before expiration, for the lease of motor vehicles, buildings, land and other equipment.
- (c) Represents our commitment to purchase minimum quantities of water as stipulated in agreements with other water purveyors. We use purchased water to supplement our water supply, particularly during periods of peak customer demand.
- (d) Represents an approximation of the open purchase orders as of the period end for goods and services purchased in the ordinary course of business.
- (e) Represents contributions expected to be made to postretirement benefit plans. The amount of required contributions in 2006 and thereafter is not determinable.
- (f) Represents capital expenditures estimated to be required under legal and binding contractual obligations.

In addition to these obligations, we make refunds on Customers' Advances for Construction over a specific period of time based on operating revenues related to developer-installed water mains or as new customers are connected to and take service from such mains. After all refunds are made, any remaining balance is transferred to Contributions in Aid of Construction. The refund amounts are not included in the above table because the refund amounts and timing 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 refund amounts are payable annually through 2017 and amounts not paid by the contract expiration dates become non-refundable.

These contractual obligations will be funded from cash flows from operations and liquidity sources held by or available to Aqua America.

Market Risk

We are subject to market risks in the normal course of business, including changes in interest rates and equity prices. The exposure to changes in interest rates is a result of financings through the issuance of fixed-rate, long-term debt. Such exposure is typically related to financings between utility rate increases, because generally our rate increases provide a revenue level to allow recovery of our current cost of capital.

AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued) (In thousands of dollars, except per share amounts)

Interest rate risk is managed through the use of a combination of long-term debt, which is at fixed interest rates and short-term debt, which is at floating interest rates. As of December 31, 2004, the debt maturities by period and the weighted average interest rate for fixed-rate, long-term debt are as follows:

	2005	2006	2007	2008	2009	Thereafter	Total	Fair Value
Long-term debt (fixed rate)	\$ 50,195	\$ 24,623	\$ 31,068	\$ 23,756	\$ 6,816	\$ 698,198	\$ 834,656	\$ 863,247
Weighted average interest rate	7.19%	5.69%	5.10%	6.66%	4.89%	5.93%	6.00%	

From time to time, we make investments in marketable equity securities. As a result, we are exposed to the risk of changes in equity prices for the "available for sale" marketable equity securities. As of December 31, 2004, we owned no marketable equity securities as we sold the balance of our securities during 2004. As a result, the market risks to which we are exposed are less than the risks to which we were exposed in the prior year.

Capitalization

The following table summarizes our capitalization during the past five years:

December 31,	2004	2003	2002	2001	2000
Long-term debt*	52.8%	52.8%	55.6%	52.9%	52.4%
Preferred stock	0.0%	0.0%	0.0%	0.1%	0.2%
Common stockholders' equity	47.2%	47.2%	44.4%	47.0%	47.4%
	100.0%	100.0%	100.0%	100.0%	100.0%

*Includes current portion.

The changes in the capitalization ratios primarily result from the issuance of common stock over the past five years, and the issuance of debt to finance our acquisitions and capital program and the previously mentioned repurchase of common stock from Veolia Environnement (formerly Vivendi, S.A.) in 2002. It is our goal to maintain an equity ratio adequate to support our current Standard and Poors corporate credit rating of "A+" and its senior secured debt rating of "AA-" for Aqua Pennsylvania, our largest operating subsidiary.

Dividends on Common Stock

We have paid common dividends consecutively for 60 years. Effective December 1, 2004, our Board of Directors authorized an increase of 8.3% in the dividend rate over the amount we paid in the previous quarter. As a result of this authorization, beginning with the dividend payment in December 2004, the annual dividend rate increased to \$0.52 per share. We presently intend to pay quarterly cash dividends in the future, on March 1, June 1, September 1 and December 1, subject to our earnings and financial condition, regulatory requirements and such other factors as our Board of Directors may deem relevant. During the past five years, our common dividends paid have averaged 56.6% of net income.

AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued) (In thousands of dollars, except per share amounts)

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our financial condition and results of operations are impacted by the methods, assumptions, and estimates used in the application of critical accounting policies. The following accounting policies are particularly important to our financial condition or results of operations, and require estimates or other judgements of matters of uncertainty. Changes in the estimates or other judgements included within these accounting policies could result in a significant change to the financial statements. We believe our most critical accounting policies include revenue recognition, the use of regulatory assets and liabilities as permitted by Statement of Financial Accounting Standards ("SFAS") No. 71, "Accounting for the Effects of Certain Types of Regulation," the review for impairment of our long-lived assets which consist primarily of Utility Plant in Service and regulatory assets, and our accounting for pensions and other postretirement benefits.

Revenue Recognition - Our utility revenues recognized in an accounting period include amounts billed to customers on a cycle basis and unbilled amounts based on estimated usage from the last billing to the end of the accounting period. The estimated usage is based on our judgement and assumptions; our actual results could differ from these estimates which would result in operating revenues being adjusted in the period that the revision to our estimates are determined.

Regulatory Assets and Liabilities - SFAS No. 71 stipulates generally accepted accounting principles for companies whose rates are established by or are subject to approval by an independent third-party regulator. In accordance with SFAS No. 71, we defer costs and credits on the balance sheet as regulatory assets and liabilities when it is probable that these costs and credits will be recognized in the rate-making process in a period different from when the costs and credits were incurred. These deferred amounts, both assets and liabilities, are then recognized in the income statement in the same period that they are

reflected in our rates charged for water and wastewater service. In the event that our assessment as to the probability of the inclusion in the rate-making process is incorrect, the associated regulatory asset or liability would be adjusted to reflect the change in our assessment or change in regulatory approval.

Impairment of Long-Lived Assets - In accordance with the requirements of SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", we review for impairment of our long-lived assets, including Utility Plant in Service. We also review regulatory assets for the continued application of SFAS No. 71. Our review determines whether there have been changes in circumstances or events that have occurred that require adjustments to the carrying value of these assets. In accordance with SFAS No. 71, adjustments to the carrying value of these assets would be made in instances where the inclusion in the rate-making process is unlikely.

Accounting for Postretirement Benefits - We maintain a qualified defined benefit pension plan and plans that provide for certain postretirement benefits other than pensions. Accounting for pensions and other postretirement benefits requires an extensive use of assumptions about the discount rate, expected return on plan assets, the rate of future compensation increases received by our employees, mortality, turnover and medical costs. Each assumption is reviewed annually with assistance from our actuarial consultant who provides guidance in establishing the assumptions. The assumptions are selected to represent the average expected experience over time and may differ in any one year from actual experience due to changes in capital markets and the overall economy. These differences will impact the amount of pension and other postretirement benefit expense that we recognize.

Our discount rate is based on a market rate for a recognized-rating agency's high-quality long-term bond portfolio with durations matching the expected payouts under our retirement plans. Our pension expense and liability (benefit obligations) increases as the discount rate is reduced. A 25 basis-point reduction in this assumption would have increased 2004 pension expense by \$550 and the pension liabilities by \$6,500. The present values of Aqua America's future pension and other postretirement obligations were determined using discount rates of 5.75% at December 31, 2004 and 6.25% at December 31, 2003. Our expense under these plans is determined using the discount rate as of the beginning of the year, which was 6.25% for 2004, and will be 5.75% for 2005.

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AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued)
(In thousands of dollars, except per share amounts)

Our expected return on assets is determined by evaluating the asset class return expectations with our advisors as well as actual, long-term, historical results of our asset returns. Our pension expense increases as the expected return on assets decreases. A 25 basis-point reduction in this assumption would have increased 2004 pension expense by \$270. For 2004, we used an 8.5% expected return on assets assumption which will remain unchanged for 2005. The expected return on assets is based on a targeted allocation of 65% equities and 35% fixed income. We believe that our actual long-term asset allocation on average will approximate the targeted allocation. Our targeted allocation is driven by the investment strategy to earn a reasonable rate of return while maintaining risk at acceptable levels through the diversification of investments across and with various asset categories.

As of December 31, 2004, we have an additional minimum liability of \$6,820 associated with our defined benefit pension plans. The additional minimum liability is a result of the accumulated benefit obligation exceeding the fair value of plan assets. The portion of the additional minimum liability related to our employees in one of our rate jurisdictions results in the establishment of a regulatory asset of \$4,140, as we expect recovery of the future, increased pension expense through customer rates. Since the balance of the additional minimum liability of \$2,680 may not be recovered through rates, the accounting requirements for recording a regulatory asset are not met and as a result this amount is recorded as an other comprehensive loss for 2004 through a charge to accumulated other comprehensive income, net of income tax benefits of \$938. The change in the additional minimum liability from December 31, 2003 of \$41 to December 31, 2004 of \$6,820 resulted from the effect of a decreased discount

rate, offset partially by an increase in the pension plan assets during 2004 due to positive equity market performance and pension contributions. Although additional minimum liability does not directly impact net income or cash flow, in future years, our pension expense and cash funding requirements are anticipated to increase as a result of the decline in the plans' funded status. Funding requirements for qualified defined benefit pension plans are determined by government regulations and not by accounting pronouncements. In accordance with our funding policy, during 2005 our required pension contribution is expected to be approximately \$7,278. We expect future changes in the amount of contributions and expense recognized will be generally included in customer rates.

IMPACT OF RECENT ACCOUNTING PRONOUNCEMENTS

In May 2004, the Financial Accounting Standards Board ("FASB") issued FASB Staff Position ("FSP") No. 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003." FSP 106-2 supersedes FSP 106-1, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003," which was issued in January 2004 and permitted a sponsor of a postretirement health care plan that provides a prescription drug benefit to make a one-time election to defer accounting for the effects of the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the "Act") until more authoritative guidance on the accounting for the federal subsidy was issued. We had elected the one-time deferral allowed under FSP 106-1 and as a result we adopted FSP 106-2 as required in the third quarter of 2004 and it did not have a material impact on our results of operation or financial position.

In November 2004, the FASB approved Statement of Financial Accounting Standards ("SFAS") No. 151, "Inventory Costs - An Amendment of ARB No. 43, Chapter 4." SFAS No. 151 requires the exclusion of certain costs from inventories and the allocation of fixed production overheads to inventories to be based on the normal capacity of the production facilities. The standard is effective for Aqua America for costs incurred after December 31, 2005. We believe this statement will not have a material impact on our results of operations or financial position.

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AQUA AMERICA, INC. AND SUBSIDIARIES

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (continued) (In thousands of dollars, except per share amounts)

In November 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets - An Amendment of APB Opinion No. 29." SFAS No. 153 eliminates the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. SFAS No. 153 specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. SFAS No. 153 is effective for fiscal periods beginning after June 15, 2005. We believe this statement will not have a material impact on our results of operations or financial position.

On October 22, 2004, the American Jobs Creation Act ("AJCA") was signed into law. Among other provisions, the AJCA creates a new deduction for qualified domestic production activities. Certain of our activities, such as our water treatment activity, are considered as qualifying production activities for purposes of determining the deduction for qualified production activities. In December 2004, the FASB issued FSP 109-1, "Application of FASB Statement No. 109, Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004." In accordance with FSP 109-1, we will treat the deduction for qualified domestic production activities as a reduction of the income tax provision in future years as realized. The AJCA and FSP 109-1 did not impact our 2004 consolidated financial statements. We are currently assessing the impact, if any, of the AJCA and FSP 109-1 on our consolidated financial statements in future periods. We believe the deduction could impact our future effective income tax rate and it is not expected to have a material impact on our results of operations or financial position.

In December 2004, the FASB issued SFAS No. 123R, "Share-Based Payment," which is effective for reporting periods beginning after June 15, 2005 (our

third quarter 2005 period). This standard revises SFAS No. 123, "Accounting for Stock-based Compensation," and supersedes APB No. 25, "Accounting for Stock Issued to Employees." As noted in the footnotes to our consolidated financial statements, we currently provide pro forma disclosure of compensation costs associated with the fair value of stock options that have been granted. We currently account for stock-based compensation associated with stock options using the intrinsic method, and accordingly, no compensation costs have been recognized in our consolidated financial statements. SFAS 123R generally requires that we measure the cost of employee services received in exchange for stock-based awards on the grant-date fair value and this cost will be recognized over the period during which an employee provides service in exchange for the award. The fair value of the option grant will be estimated using an option-pricing model. We are currently evaluating this standard to determine the impact on our consolidated financial statements, including the selection of an appropriate option-pricing model as permitted under SFAS No. 123R, and the method by which we will adopt SFAS No. 123R. We are currently evaluating the requirements of SFAS No. 123R and we expect the adoption of this standard will have a material impact on our results of operations and earnings per share.

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AQUA AMERICA, INC. AND SUBSIDIARIES

Management's Report On Internal Control Over Financial Reporting

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

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

In assessing the effectiveness of internal control over financial reporting, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control-Integrated Framework. As a result of management's assessment and based on the criteria in the framework, management has concluded that, as of December 31, 2004, the Company's internal control over financial reporting was effective.

Management evaluated the Company's internal control over financial reporting as of December 31, 2004. In conducting this assessment, management has excluded Heater Utilities, Inc. from its assessment because it was acquired by the Company in a purchase business combination during 2004. Heater Utilities, Inc., is a wholly-owned subsidiary, whose total assets and total revenues represent approximately 5% and 3%, respectively, of the related consolidated financial statement amounts as of and for the year ended December 31, 2004.

The Company's independent registered public accounting firm, PricewaterhouseCoopers LLP, has audited management's assessment of the effectiveness of the Company's internal control over financial reporting, as stated in their report which appears herein.

NICHOLAS DEBENEDICTIS

DAVID P. SMELTZER

Nicholas DeBenedictis
Chairman &
President

David P. Smeltzer
Senior Vice President - Finance

March 14, 2005

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of
Aqua America, Inc.:

We have completed an integrated audit of Aqua America, Inc.'s 2004 consolidated financial statements and of its internal control over financial reporting as of December 31, 2004 and audits of its 2003 and 2002 financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Our opinions, based on our audits, are presented below.

Consolidated financial statements

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of income and comprehensive income, of capitalization and of cash flows present fairly, in all material respects, the financial position of Aqua America, Inc. and its subsidiaries at December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2004 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Internal control over financial reporting

Also, in our opinion, management's assessment, included in Management's Report on Internal Control Over Financial Reporting, appearing in the 2004 Annual Report to Shareholders, that the Company maintained effective internal control over financial reporting as of December 31, 2004 based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), is fairly stated, in all material respects, based on those criteria. Furthermore, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control - Integrated Framework issued by the COSO. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express opinions on management's assessment and on the effectiveness of the Company's internal control over financial reporting based on our audit. We conducted our audit of internal control over financial reporting in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. An audit of internal control over financial reporting includes obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we consider necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to

permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

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

As described in Management's Report on Internal Control Over Financial Reporting, management has excluded Heater Utilities, Inc. from its assessment of internal control over financial reporting as of December 31, 2004 because it was acquired by the Company in a purchase business combination during 2004. We have also excluded Heater Utilities, Inc. from our audit of internal control over financial reporting. Heater Utilities, Inc., is a wholly-owned subsidiary, whose total assets and total revenues represent approximately 5% and 3%, respectively, of the related consolidated financial statement amounts as of and for the year ended December 31, 2004.

PRICEWATERHOUSECOOPERS LLP

PricewaterhouseCoopers LLP
Philadelphia, PA
March 14, 2005

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AQUA AMERICA, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(In thousands, except per share amounts)
Years ended December 31, 2004, 2003 and 2002

	2004	2003	2002

Operating revenues	\$ 442,039	\$ 367,233	\$ 322,028
Costs and expenses:			
Operations and maintenance	178,345	140,602	117,735
Depreciation	54,564	48,522	41,424
Amortization	4,300	2,941	2,898
Taxes other than income taxes	27,596	21,607	19,467

	264,805	213,672	181,524
Operating income	177,234	153,561	140,504
Other expense (income):			
Interest expense, net	48,679	44,662	40,396
Allowance for funds used during construction	(2,304)	(2,127)	(1,389)
Gain on sale of water system	-	-	(5,676)
Gain on sale of other assets	(1,272)	(5,692)	(2,079)

Income before income taxes	132,131	116,718	109,252
Provision for income taxes	52,124	45,923	42,046

Net income	80,007	70,795	67,206
Dividends on preferred stock	-	10	52

Net income available to common stock	\$ 80,007	\$ 70,785	\$ 67,154
	=====		
Net income	\$ 80,007	\$ 70,795	\$ 67,206
Other comprehensive income (loss), net of tax:			
Minimum pension liability adjustment	(1,742)	-	-
Unrealized gains on securities	59	455	104
Reclassification adjustment for gains reported in net income	(230)	(347)	(767)

	(1,913)	108	(663)

Comprehensive income	\$ 78,094	\$ 70,903	\$ 66,543
	=====		
Net income per common share:			
Basic	\$ 0.86	\$ 0.80	\$ 0.78
Diluted	\$ 0.85	\$ 0.79	\$ 0.78
	=====		
Average common shares outstanding during the period:			
Basic	93,247	88,275	85,674

Diluted

94,282	89,244	86,538
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See accompanying notes to consolidated financial statements.

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AQUA AMERICA, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands of dollars, except per share amounts)
December 31, 2004 and 2003

	2004	2003
Assets		
Property, plant and equipment, at cost	\$ 2,626,151	\$ 2,302,304
Less accumulated depreciation	556,339	478,013
Net property, plant and equipment	2,069,812	1,824,291
Current assets:		
Cash and cash equivalents	13,116	10,757
Accounts receivable and unbilled revenues, net	64,538	62,320
Inventory, materials and supplies	6,903	5,841
Prepayments and other current assets	5,570	5,051
Total current assets	90,127	83,969
Regulatory assets	110,993	98,761
Deferred charges and other assets, net	31,998	34,277
Funds restricted for construction activity	17,196	28,438
Goodwill	20,122	-
	\$ 2,340,248	\$ 2,069,736
Liabilities and Stockholders' Equity		
Stockholders' equity:		
Common stock at \$.50 par value, authorized 300,000,000 shares, issued 96,071,580 and 93,270,424 in 2004 and 2003	\$ 48,036	\$ 46,635
Capital in excess of par value	468,524	413,008
Retained earnings	245,115	210,915
Minority interest	1,237	912
Treasury stock, at cost, 686,747 and 681,384 shares in 2004 and 2003	(12,702)	(12,611)
Accumulated other comprehensive income	(1,742)	171
Total stockholders' equity	748,468	659,030
Long-term debt, excluding current portion	784,461	696,666
Commitments	-	-
Current liabilities:		
Current portion of long-term debt	50,195	39,386
Loans payable	85,115	96,459
Accounts payable	23,534	32,321
Accrued interest	12,029	11,126
Accrued taxes	8,975	16,779
Other accrued liabilities	37,534	35,930
Total current liabilities	217,382	232,001
Deferred credits and other liabilities:		
Deferred income taxes and investment tax credits	223,887	190,395
Customers' advances for construction	73,095	72,500
Other	15,147	9,419
Total deferred credits and other liabilities	312,129	272,314
Contributions in aid of construction	277,808	209,725
	\$ 2,340,248	\$ 2,069,736

See accompanying notes to consolidated financial statements.

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AQUA AMERICA, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CAPITALIZATION
(In thousands of dollars, except per share amounts)
December 31, 2004 and 2003

2004

2003

Stockholders' equity:		
Common stock, \$.50 par value	\$ 48,036	\$ 46,635
Capital in excess of par value	468,524	413,008
Retained earnings	245,115	210,916
Minority interest	1,237	912
Treasury stock, at cost	(12,702)	(12,612)
Accumulated other comprehensive income	(1,742)	171
Total stockholders' equity	748,468	659,030
Long-term debt:		
Long-term debt of subsidiaries (substantially secured by utility plant):		
Interest Rate Range		
0.00% to 2.49%	20,051	16,868
2.50% to 2.99%	29,924	18,913
3.00% to 3.49%	17,546	5,618
3.50% to 3.99%	7,123	2,800
4.00% to 4.99%	9,435	8,135
5.00% to 5.49%	165,615	110,875
5.50% to 5.99%	89,260	76,260
6.00% to 6.49%	110,360	119,360
6.50% to 6.99%	42,000	42,000
7.00% to 7.49%	45,105	46,716
7.50% to 7.99%	25,231	23,000
8.00% to 8.49%	26,714	17,500
8.50% to 8.99%	9,000	9,000
9.00% to 9.49%	53,244	53,805
9.50% to 9.99%	42,088	43,242
10.00% to 10.50%	6,000	6,000
	698,696	600,092
Note payable, 6.05%, due 2006	960	960
Unsecured notes payable, 4.87%, due 2023	135,000	135,000
	834,656	736,052
Current portion of long-term debt	50,195	39,386
Long-term debt, excluding current portion	784,461	696,666
Total capitalization	\$ 1,532,929	\$ 1,355,696

See accompanying notes to consolidated financial statements.

AQUA AMERICA, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMMON STOCKHOLDERS' EQUITY
(In thousands of dollars, except per share amounts)

	Common Stock	Capital in excess of par value	Retained earnings	Treasury Stock	Accumulated Other Comprehensive Income	Total
Balance at December 31, 2001	\$ 34,650	\$ 304,039	\$ 149,682	\$ (17,167)	\$ 726	\$ 471,930
Net income	-	-	67,154	-	-	67,154
Other comprehensive income: unrealized						
gains on securities, net of income tax of \$56	-	-	-	-	104	104
Reclassification adjustment for gains reported						
in net income, net of income tax of \$412	-	-	-	-	(767)	(767)
Dividends	-	-	(36,789)	-	-	(36,789)
Stock issued for acquisitions (178,864 shares)	71	2,674	-	-	-	2,745
Sale of stock (448,593 shares)	161	6,220	-	855	-	7,236
Repurchase of stock (1,274,680 shares)	-	-	-	(24,109)	-	(24,109)
Equity Compensation Plan (37,031 shares)	15	598	-	-	-	613
Exercise of stock options (339,178 shares)	137	3,237	-	-	-	3,374
Employee stock plan tax benefits	-	1,103	-	-	-	1,103
Balance at December 31, 2002	35,034	317,871	180,047	(40,421)	63	492,594
Net income	-	-	70,785	-	-	70,785
Other comprehensive income: unrealized						
gains on securities, net of income tax of \$244	-	-	-	-	455	455
Reclassification adjustment for gains reported						
in net income, net of income tax of \$186	-	-	-	-	(347)	(347)
Dividends	-	-	(39,917)	-	-	(39,917)
Stock split	9,244	(9,244)	-	-	-	-
Sale of stock (7,308,870 shares)	2,168	99,031	-	29,163	-	130,362
Repurchase of stock (60,646 shares)	-	-	-	(1,353)	-	(1,353)
Equity Compensation Plan (20,156 shares)	8	344	-	-	-	352
Exercise of stock options (434,833 shares)	181	4,283	-	-	-	4,464

Employee stock plan tax benefits	-	723	-	-	-	723
Balance at December 31, 2003	46,635	413,008	210,915	(12,611)	171	658,118
Net income	-	-	80,007	-	-	80,007
Other comprehensive income (loss):						
Minimum pension liability adjustment, net of income tax of \$938	-	-	-	-	(1,742)	(1,742)
Unrealized gain on securities, net of income tax of \$32	-	-	-	-	59	59
Less: Reclassification adjustment for gains reported in net income, net of income tax of \$173	-	-	-	-	(230)	(230)
Dividends	-	-	(45,807)	-	-	(45,807)
Sale of stock (2,385,902 shares)	1,170	48,971	-	991	-	51,132
Repurchase of stock (51,808 shares)	-	-	-	(1,082)	-	(1,082)
Equity Compensation Plan (34,151 shares)	17	692	-	-	-	709
Exercise of stock options (427,548 shares)	214	4,847	-	-	-	5,061
Employee stock plan tax benefits	-	1,006	-	-	-	1,006
Balance at December 31, 2004	\$ 48,036	\$ 468,524	\$ 245,115	\$ (12,702)	\$ (1,742)	\$ 747,231

See accompanying notes to consolidated financial statements.

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AQUA AMERICA, INC. AND SUBSIDIARIES
CONSOLIDATED CASH FLOW STATEMENTS
(In thousands of dollars)
Years ended December 31, 2004, 2003 and 2002

	2004	2003	2002
Cash flows from operating activities:			
Net income	\$ 80,007	\$ 70,795	\$ 67,206
Adjustments to reconcile net income to net cash flows from operating activities:			
Depreciation and amortization	58,864	51,463	44,322
Deferred income taxes	40,577	26,741	18,470
Gain on sale of water system	(2,342)	-	(5,676)
Gain on sale of other assets	(1,272)	(5,692)	(2,079)
Net increase in receivables, inventory and prepayments	(2,766)	(314)	(742)
Net increase in payables, accrued interest, accrued taxes and other accrued liabilities	863	7,777	1,346
Other	(328)	(7,397)	(1,287)
Net cash flows from operating activities	173,603	143,373	121,560
Cash flows from investing activities:			
Property, plant and equipment additions, including allowance for funds used during construction of \$2,304, \$2,127 and \$1,389	(195,736)	(163,320)	(136,164)
Acquisitions of water and wastewater systems, net	(54,300)	(192,331)	(8,914)
Net decrease (increase) in funds restricted for construction activity	11,243	15,314	(23,986)
Net proceeds from the sale of water systems	4,716	4,000	12,118
Net proceeds from the sale of other assets	2,098	6,496	6,258
Other	(517)	(312)	(362)
Net cash flows used in investing activities	(232,496)	(330,153)	(151,050)
Cash flows from financing activities:			
Customers' advances and contributions in aid of construction	14,269	8,181	10,266
Repayments of customers' advances	(4,930)	(4,257)	(5,070)
Net proceeds (repayments) of short-term debt	(31,900)	(18,654)	5,445
Proceeds from long-term debt	130,258	154,537	119,350
Repayments of long-term debt	(55,928)	(44,204)	(43,279)
Redemption of preferred stock	-	(172)	(944)
Proceeds from issuing common stock	56,193	134,826	10,611
Repurchase of common stock	(1,082)	(1,353)	(24,109)
Dividends paid on preferred stock	-	(10)	(52)
Dividends paid on common stock	(45,807)	(39,917)	(36,789)
Other	179	2,645	(1,034)
Net cash flows from financing activities	61,252	191,622	34,395
Net increase in cash and cash equivalents	2,359	4,842	4,905
Cash and cash equivalents at beginning of year	10,757	5,915	1,010
Cash and cash equivalents at end of year	\$ 13,116	\$ 10,757	\$ 5,915
Cash paid during the year for:			
Interest, net of amounts capitalized	\$ 45,261	\$ 40,572	\$ 38,040
Income taxes	\$ 22,322	\$ 19,168	\$ 24,165

See Summary of Significant Accounting Policies-Customers' Advances for Construction, Acquisitions and Employee Stock and Incentive Plans footnotes for description of non-cash activities.

See accompanying notes to consolidated financial statements.

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Notes to Consolidated Financial Statements (continued)
(In thousands of dollars, except per share amounts)

Summary of Significant Accounting Policies

Name Change - On January 16, 2004, Philadelphia Suburban Corporation changed its corporate name to Aqua America, Inc. In addition, we changed our ticker symbol from PSC to WTR on the New York Stock Exchange and Philadelphia Stock Exchange effective on January 20, 2004.

Nature of Operations - Aqua America, Inc. ("Aqua America" or the "Company") is the holding company for regulated utilities providing water or wastewater services in Pennsylvania, Ohio, North Carolina, Illinois, Texas, New Jersey, Florida, Indiana, Virginia, Maine, Missouri, New York and South Carolina. Our largest operating subsidiary, Aqua Pennsylvania, Inc. - formerly Pennsylvania Suburban Water Company, accounts for approximately 57% of our operating revenues and provides water or wastewater service to customers in the suburban areas north and west of the City of Philadelphia and in 21 other counties in Pennsylvania. The Company's other subsidiaries provide similar services in 12 other states. In addition, the Company provides water and wastewater service through operating and maintenance contracts with municipal authorities and other parties close to our operating companies' service territories.

Regulation - Most of the operating companies that are regulated public utilities are subject to regulation by the public utility commissions of the states in which they operate. The respective public utility commissions have jurisdiction with respect to rates, service, accounting procedures, issuance of securities, acquisitions and other matters. Some of the operating companies that are regulated public utilities are subject to rate regulation by county or city government. Regulated public utilities follow Statement of Financial Accounting Standards ("SFAS") No. 71, "Accounting for the Effects of Certain Types of Regulation." SFAS No. 71 provides for the recognition of regulatory assets and liabilities as allowed by regulators for costs or credits that are reflected in current rates or are considered probable of being included in future rates. The regulatory assets or liabilities are then relieved as the cost or credit is reflected in rates.

Consolidation - The consolidated financial statements include the accounts of the Company and its subsidiaries. All material intercompany accounts and transactions have been eliminated where appropriate.

Recognition of Revenues - Revenues include amounts billed to customers on a cycle basis and unbilled amounts based on estimated usage from the latest billing to the end of the accounting period. Nonregulated revenues are recognized when services are performed and are primarily associated with operating and maintenance contracts and data processing service fees. Nonregulated revenues totaled \$13,623 in 2004, \$11,806 in 2003 and \$7,190 in 2002.

Property, Plant and Equipment and Depreciation - Property, plant and equipment consist primarily of utility plant. The cost of additions includes contracted cost, direct labor and fringe benefits, materials, overheads and, for certain utility plant, allowance for funds used during construction. Water systems acquired are recorded at estimated original cost of utility plant when first devoted to utility service and the applicable depreciation is recorded to accumulated depreciation. The difference between the estimated original cost, less applicable accumulated depreciation, and the purchase price is recorded as an acquisition adjustment within utility plant. At December 31, 2004, utility plant includes a net credit acquisition adjustment of \$63,347, which is generally being amortized from 0 to 20 years. Amortization of the acquisition adjustments totaled \$3,961 in 2004, \$1,649 in 2003 and \$633 during 2002.

Utility expenditures for maintenance and repairs, including major maintenance projects and minor renewals and betterments, are charged to operating expenses when incurred in accordance with the system of accounts prescribed by the public utility commissions of the states in which the company operates. The cost of new units of property and betterments are capitalized.

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

When units of utility property are replaced, retired or abandoned, the recorded value thereof is credited to the asset account and such value, together with the net cost of removal, is charged to accumulated depreciation. To the extent the Company recovers cost of removal or other retirement costs through rates after the retirement costs are incurred, a regulatory asset is recorded. In some cases, the Company recovers retirement costs through rates during the life of the associated asset and before the costs are incurred. These amounts result in a regulatory liability being reported based on the amounts previously recovered through customer rates.

The straight-line remaining life method is used to compute depreciation on utility plant. Generally, the straight-line method is used with respect to transportation and mechanical equipment, office equipment and laboratory equipment.

In accordance with the requirements of Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", the long-lived assets of the Company, which consist primarily of Utility Plant in Service and regulatory assets, are reviewed for impairment when changes in circumstances or events occur. There has been no change in circumstances or events that have occurred that require adjustments to the carrying values of these assets.

Allowance for Funds Used During Construction - The allowance for funds used during construction ("AFUDC") is a non-cash credit which represents the estimated cost of funds used to finance the construction of utility plant. In general, AFUDC is applied to construction projects requiring more than one month to complete. No AFUDC is applied to projects funded by customer advances for construction or contributions in aid of construction. AFUDC includes the net cost of borrowed funds and a rate of return on other funds when used, and is recovered through water rates as the utility plant is depreciated. The amount of AFUDC related to equity funds in 2002 was \$9. There was no AFUDC related to equity funds in 2004 and 2003. No interest was capitalized by our nonregulated businesses.

Cash and Cash Equivalents - The Company considers all highly liquid investments with an original maturity of three months or less, which are not restricted for construction activity, to be cash equivalents.

Accounts Receivable - Accounts receivable are recorded at the invoiced amounts. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in our existing accounts receivable, and is determined based on historical write-off experience. The Company reviews the allowance for doubtful accounts quarterly. Account balances are written off against the allowance when it is probable the receivable will not be recovered.

Deferred Charges and Other Assets - Deferred charges and other assets consist of financing expenses, other costs and marketable securities. Deferred bond issuance expenses are amortized by the straight-line method over the life of the related issues. Call premiums related to the early redemption of long-term debt, along with the unamortized balance of the related issuance expense, are deferred and amortized over the life of the long-term debt used to fund the redemption. Other costs, for which the Company has received or expects to receive prospective rate recovery, are deferred and amortized over the period of rate recovery in accordance with SFAS No. 71.

Marketable securities are considered "available-for-sale" and accordingly, are carried on the balance sheet at fair market value. Unrecognized gains are included in other comprehensive income.

Goodwill - Goodwill represents the excess cost over the fair value of net tangible and identifiable intangible assets acquired, and a substantial portion of the goodwill balance is associated with the acquisition of Heater Utilities, Inc. in June 2004. Goodwill is not amortized but is tested for impairment annually, or more often, if certain circumstances indicate a possible impairment may exist. In accordance with the requirements of SFAS No. 142, "Goodwill and Other Intangible Assets," the Company tested the goodwill attributable to each of our reporting units for impairment as of June 30, 2004, in conjunction with the timing of our annual strategic business plan. Based on the Company's comparison of the estimated fair value of each reporting unit to their respective carrying amounts, the impairment test concluded that none of its goodwill was impaired.

AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

Income Taxes - The Company accounts for certain income and expense items in different time periods for financial reporting than for tax reporting purposes. Deferred income taxes are provided on the temporary differences between the tax basis of the assets and liabilities, and the amounts at which they are carried in the consolidated financial statements. The income tax effect of temporary differences not allowed currently in rates is recorded as deferred taxes with an offsetting regulatory asset or liability. These deferred income taxes are based on the enacted tax rates expected to be in effect when such temporary differences are projected to reverse. Investment tax credits are deferred and amortized over the estimated useful lives of the related properties.

Customers' Advances for Construction - Water mains or, in some instances, cash advances to reimburse the Company for its costs to construct water mains, are contributed to the Company by customers, real estate developers and builders in order to extend water service to their properties. The value of these contributions is recorded as Customers' Advances for Construction. The Company makes refunds on these advances over a specific period of time based on operating revenues related to the main or as new customers are connected to and take service from the main. After all refunds are made, any remaining balance is transferred to Contributions in Aid of Construction. Non-cash property, in the form of water mains, has been received, generally from developers, as advances or contributions of \$9,273, \$9,991 and \$17,271 in 2004, 2003 and 2002, respectively.

Contributions in Aid of Construction - Contributions in aid of construction include direct non-refundable contributions and the portion of customers' advances for construction that become non-refundable.

Inventories, Materials and Supplies - Inventories are stated at cost. Cost is principally determined using the first-in, first-out method.

Stock-Based Compensation - The Company currently accounts for stock-based compensation using the intrinsic value method in accordance with APB Opinion No. 25, "Accounting for Stock Issued to Employees". Accordingly, no compensation expense related to granting of stock options has been recognized in the financial statements for stock options that have been granted. Please refer to the Recent Accounting Pronouncements section of this footnote for information concerning changes to the Company's accounting for stock-based compensation. Pursuant to the current disclosure requirements of SFAS No. 123, "Accounting for Stock-Based Compensation," as amended by SFAS No. 148, pro forma net income available to common stock and earnings per share are presented in the following table as if compensation cost for stock options was determined as of the grant date under the fair value method:

	Years Ended December 31,		
	2004	2003	2002
Net income available to common stock, as reported	\$ 80,007	\$ 70,785	\$ 67,154
Add: stock-based employee compensation expense included in reported net income, net of tax	266	224	473
Less: pro forma expense related to stock options granted, net of tax effects	(1,990)	(1,793)	(1,741)
Pro forma	\$ 78,283	\$ 69,216	\$ 65,886
Basic net income per share:			
As reported	\$ 0.86	\$ 0.80	\$ 0.78
Pro forma	0.84	0.78	0.77
Diluted net income per share:			
As reported	\$ 0.85	\$ 0.79	\$ 0.78
Pro forma	0.83	0.78	0.76

AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

The per share weighted-average fair value at the date of grant for stock options granted during 2004, 2003 and 2002 was \$5.43, \$4.67 and \$5.15 per option, respectively. The fair value of options at the date of grant was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions:

	2004	2003	2002
	-----	-----	-----
Expected life (years)	4.5	5.6	5.5
Interest rate	4.0%	3.7%	4.9%
Volatility	29.9%	32.4%	34.2%
Dividend yield	2.2%	2.6%	2.6%

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

Recent Accounting Pronouncements - In May 2004, the Financial Accounting Standards Board ("FASB") issued FASB Staff Position ("FSP") No. 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003." FSP 106-2 supersedes FSP 106-1, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003," which was issued in January 2004 and permitted a sponsor of a postretirement health care plan that provides a prescription drug benefit to make a one-time election to defer accounting for the effects of the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the "Act") until more authoritative guidance on the accounting for the federal subsidy was issued. The Company had elected the one-time deferral allowed under FSP 106-1 and as a result adopted FSP 106-2 as required in the third quarter of 2004 and it did not have a material impact on our results of operations or financial position.

In November 2004, the FASB approved Statement of Financial Accounting Standards ("SFAS") No. 151, "Inventory Costs - An Amendment of ARB No. 43, Chapter 4." SFAS No. 151 requires the exclusion of certain costs from inventories and the allocation of fixed production overheads to inventories to be based on the normal capacity of the production facilities. The standard is effective for the Company for costs incurred after December 31, 2005. The Company believes this statement will not have a material impact on its results of operations or financial position.

In November 2004, the FASB issued SFAS No. 153, "Exchanges of Nonmonetary Assets - An Amendment of APB Opinion No. 29." SFAS No. 153 eliminates the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. SFAS No. 153 specifies that a nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. SFAS No. 153 is effective for fiscal periods beginning after June 15, 2005. The Company believes this statement will not have a material impact on its results of operations or financial position.

On October 22, 2004, the American Jobs Creation Act ("AJCA") was signed into law. Among other provisions, the AJCA creates a new deduction for qualified domestic production activities. Certain activities of the Company, such as our water treatment activity, are considered as qualifying production activities for purposes of determining the deduction for qualified production activities. In December 2004, the FASB issued FSP 109-1, "Application of FASB Statement No. 109, Accounting for Income Taxes, to the Tax Deduction on Qualified Production Activities Provided by the American Jobs Creation Act of 2004." In accordance with FSP 109-1, the Company will treat the deduction for qualified domestic production activities as a reduction of the income tax provision in future years as realized. The AJCA and FSP 109-1 did not impact the Company's 2004 consolidated financial statements. Thus, the Company is currently assessing the impact, if any, of the AJCA and FSP 109-1 on its consolidated financial

statements in future periods. The Company believes the deduction could impact the Company's future effective income tax rate and it is not expected to have a material impact on its results of operations or financial position.

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AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

In December 2004, the FASB issued SFAS No. 123R, "Share-Based Payment," which is effective for reporting periods beginning after June 15, 2005 (our third quarter 2005 period). This standard revises SFAS No. 123, "Accounting for Stock-based Compensation," and supersedes APB No. 25, "Accounting for Stock Issued to Employees." As noted in the section captioned "Stock-based Compensation" in the Summary of Significant Accounting Policies footnote, the Company currently provides pro forma disclosure of its compensation costs associated with the fair value of stock options that have been granted. The Company currently accounts for stock-based compensation associated with stock options using the intrinsic method, and accordingly, no compensation costs have been recognized in its consolidated financial statements. SFAS 123R generally requires that we measure the cost of employee services received in exchange for stock-based awards on the grant-date fair value and this cost will be recognized over the period during which an employee provides service in exchange for the award. The fair value of the option grant will be estimated using an option-pricing model. The Company is currently evaluating this standard to determine the impact on its consolidated financial statements, including the selection of an appropriate option-pricing model as permitted under SFAS No. 123R, and the method by which we will adopt SFAS No. 123R. The Company is currently evaluating the requirements of SFAS No. 123R and it expects that the adoption of this standard will have a material impact on its results of operations and earnings per share.

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AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

Acquisitions

Heater - Pursuant to our strategy to grow through acquisitions, on June 1, 2004 the Company acquired the capital stock of Heater Utilities, Inc. for \$48,000 in cash and the assumption of long-term debt of \$19,219 and short-term debt of \$8,500. The acquired operation provides water and wastewater service to over 50,000 water and wastewater customers primarily in the areas of suburban Raleigh, Charlotte, Gastonia and Fayetteville, North Carolina. For the fiscal year ended December 31, 2003, Heater had operating revenues of \$19,489. The acquisition was accounted for as a purchase and accordingly, the purchase price is allocated to the net tangible and intangible assets based upon their estimated fair values at the date of the acquisition. The Company obtained a third-party valuation of these assets and liabilities, and it resulted in the recording of a purchase accounting fair value adjustment of \$3,141 to increase the carrying-value of long-term debt assumed. The purchase price allocation is as follows:

	June 1, 2004

Property, plant and equipment, net	\$ 96,779
Current assets	4,133
Other long-term assets	6,005
Goodwill	18,842

Total assets acquired	125,759

Current liabilities	3,063
Loans payable	8,500
Long-term debt	22,360
Other long-term liabilities	43,836

Total liabilities assumed	----- 77,759 -----
Net assets acquired	\$ 48,000 =====

The Company has recorded goodwill of \$18,842, and a substantial portion of the goodwill is expected to be deductible for tax purposes. The purchase price was arrived at through arms-length negotiations with the seller and is consistent with the multiples paid in other comparable transactions. Aqua America considered important regulatory, strategic and valuation considerations in arriving at the final purchase price. During 2004, through the North Carolina Utilities Commission approval process, a mechanism has been developed through which the Company could recover up to two-thirds of the goodwill through customer rates in the future upon achieving certain objectives. The Company intends to pursue these objectives to facilitate recognition of this premium in customer rates. However, there can be no assurance that the Company will be able to achieve these objectives and recover such amount of goodwill, if any.

Florida Water - On June 30, 2004, the Company acquired certain utility assets of Florida Water Services Corporation, comprised of 63 water and wastewater systems located in central Florida for \$14,747 in cash, which is less than the depreciated original cost of these assets. In accordance with Florida procedures, the acquisition remains subject to regulatory approval by the Florida Public Service Commission. This process is not expected to be completed prior to September 2005. Under the terms of the purchase agreement, the Commission's review process may result in an adjustment of the final purchase price, which would be settled in cash, based on the Commission's determination of plant investment for the systems. Since the purchase price adjusts by the change in the determined plant investment or rate base, effectively the rate base adjustment is directly offset by the change in purchase price. The final purchase price is not expected to result in the recognition of goodwill.

AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

AquaSource - Pursuant to our strategy to grow through acquisitions, on July 31, 2003, the Company completed its acquisition of four operating water and wastewater subsidiaries of AquaSource, Inc. (a subsidiary of DQE, Inc.), including selected, integrated operating and maintenance contracts and related assets (individually and collectively the acquisition is referred to as "AquaSource") for \$190,717 in cash, as adjusted pursuant to the purchase agreement based on working capital at closing. On August 27, 2004, we were awarded and received \$12,289 plus interest in an arbitration related to the calculation of the final purchase price under the terms of the purchase agreement, which resulted in a final purchase price of \$178,428. In the consolidated statement of cash flow for 2004, the \$12,289 award has been reported as proceeds on the line titled acquisitions of water and wastewater systems, net.

The results of AquaSource have been included in the Company's consolidated financial statements beginning August 1, 2003. The acquired operations of AquaSource serve over 130,000 water and wastewater customer accounts in 11 states (including the Connecticut and Kentucky operations which were subsequently sold to other parties). Please refer to the Dispositions footnote for a discussion of the AquaSource operations located in Connecticut, Kentucky and New York. The AquaSource acquisition was initially funded by a portion of the proceeds from the July 2003 issuance of \$135,000 of unsecured notes due 2023, with an interest rate of 4.87%, and the issuance of a \$90,000 unsecured note by Aqua America. In August 2003, the \$90,000 unsecured note was repaid with the proceeds from the issuance of 5,000,000 shares of common stock through a shelf registration.

Under the purchase method of accounting, the purchase price is allocated to AquaSource's net tangible and intangible assets based upon their estimated fair values at the date of the acquisition. The purchase price allocation, which reflects the effects of the August 2004 purchase price arbitration proceeding, is as follows:

	July 31, 2003

Property, plant and equipment, net	\$197,719
Current assets	9,687
Other long-term assets	14,204
Assets held for sale, net	4,096

Total assets acquired	225,706

Current liabilities	8,214
Long-term debt	7,170
Other long-term liabilities	31,894

Total liabilities assumed	47,278

Net assets acquired	\$178,428
	=====

The following supplemental pro forma information is presented to illustrate the effects of the AquaSource acquisition, which was completed on July 31, 2003, on the historical operating results for the year ended December 31, 2003 and 2002 as if the acquisition had occurred at the beginning of the respective periods (unaudited):

	Years Ended December 31,	

	2003	2002

Operating revenues	\$ 407,628	\$ 391,569
Net income	\$ 74,436	\$ 72,420
Net income per common share:		
Basic	\$ 0.81	\$ 0.80
Diluted	\$ 0.81	\$ 0.79

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The supplemental information is not necessarily representative of the actual results that may have occurred for these periods or of the results that may occur in the future. This information does not reflect the effects of recent rate increases or cost savings that may result from the acquisition, such as the effects of a reduction in administrative costs. This information is based upon the historical operating results of AquaSource for periods prior to the acquisition date of July 31, 2003 as provided to the Company by AquaSource, Inc. and DQE, Inc. management.

Other Acquisitions - During 2004, in addition to the Heater and Florida Water acquisitions, the Company completed 27 acquisitions or other growth ventures in the various states in which the Company operates for an aggregate purchase price of \$3,842 in cash. The operating revenues included in the consolidated financial statements of the Company during the period owned by the Company were \$617.

During 2003, in addition to the AquaSource acquisition, the Company completed 17 acquisitions or other growth ventures in the various states in which the Company operates for an aggregate purchase price of \$1,614 in cash. Operating revenues included in the consolidated financial statements of the Company related to these systems were \$860 in 2004 and \$312 in 2003.

During 2002, the Company completed 25 acquisitions or other growth ventures in various states. The total purchase price of \$11,659 for the systems acquired in 2002 consisted of \$8,914 in cash and the issuance of 178,864 shares of the Company's common stock. Operating revenues included in the consolidated financial statements of the Company related to the systems acquired in 2002 were \$2,932 in 2004, \$2,920 in 2003 and \$1,341 in 2002.

Dispositions

In December 2004, as a result of the settlement of a condemnation action, the Company's Ohio operating subsidiary sold its water utility assets within the municipal boundaries of the City of Geneva in Ashtabula County, Ohio for net proceeds of approximately \$4,716, which was in excess of the book value for these assets. The proceeds were used to pay-down short-term debt and the sale resulted in the recognition in the fourth quarter of 2004 of a gain on the sale of these assets, net of expenses, of \$2,342. The gain is reported in the 2004 consolidated statement of income as a reduction to operations and maintenance expense. We continue to operate this water system for the City of Geneva under an operating contract that began upon the closing of the sale for a period through December 2006. The operating contract provides for an annual base operating fee of \$135 and allows for additional fees to be earned commensurate with the services provided. These water utility assets represent less than 1% of Aqua America's total assets, and the total number of customers included in the water system sold represents less than 1% of our total customer base.

In July 2004, the Company sold its only operations in Kentucky. The sale price approximates our investment in this operation. The operation represented approximately 0.2% of the operations acquired from AquaSource, Inc. In October 2003, the Company sold its only operation in Connecticut. The sale price of \$4,000 approximates our investment in this operation. The operation represented approximately 2% of the operations acquired from AquaSource, Inc. In May 2003, the Company announced an agreement for the sale of the AquaSource regulated operation located in New York to a New England-based water company. In January 2005, after the expiration of the sale agreement, the Company did not renew the sale agreement. The New York operations represented approximately 1% of the operations acquired from AquaSource, Inc.

In December 2002, as a result of the settlement of a condemnation action, the Company's Ohio operating subsidiary sold to Ashtabula County, Ohio the water utility assets in the unincorporated areas of Ashtabula County and the area within the Village of Geneva on the Lake for \$12,118, net of certain closing costs. The sale was in excess of the book value for these assets and the sale generated a gain of \$5,676 (or an after-tax

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gain of \$3,690 and \$0.04 per share) recorded in the fourth quarter of 2002. We continue to operate this water system for Ashtabula County, beginning after the closing of the sale, under a multi-year operating contract. The water utility assets sold represent less than 1% of our total assets, and the total number of customers included in the water system sold represents less than 1% of our total customer base.

The City of Fort Wayne, Indiana has authorized the acquisition, by eminent domain or otherwise, of a portion of the utility assets of one of the operating subsidiaries that the Company acquired in connection with the AquaSource acquisition in 2003. The Company has challenged whether the City is following the correct legal procedures in connection with the City's attempted condemnation and the Company has challenged the City's valuation of this portion of its system. The portion of the system under consideration represents approximately 1% of the Company's total customer base. While the Company continues to discuss this matter with officials from the City of Fort Wayne, the Company continues to protect its interests in this proceeding. The Company believes that it will be entitled to fair market value for its assets if they are condemned, and it is believed that the fair market value will be in excess of the book value for such assets.

Property, Plant and Equipment

December 31,		Approximate range of remaining lives
2004	2003	
-----		-----

Utility plant and equipment:

Mains and accessories	\$1,087,712	\$ 962,439	15 to 85 years
Services, hydrants, treatment plants and reservoirs	607,331	547,622	5 to 56 years
Operations structures and water tanks	218,888	175,663	15 to 61 years
Miscellaneous pumping and purification equipment	342,985	259,468	10 to 50 years
Meters, data processing, transportation and operating equipment	298,015	251,721	5 to 50 years
Land and other non-depreciable assets	67,260	58,223	-
	-----	-----	
Utility Plant and equipment	2,622,191	2,255,136	
Utility construction work in progress	63,754	92,106	-
Net utility plant acquisition adjustment	(63,347)	(48,054)	0 to 20 years
Non-utility plant and equipment	3,553	3,116	2 to 40 years
	-----	-----	
Total property, plant and equipment	\$2,626,151	\$2,302,304	
	=====	=====	

Accounts Receivable

	December 31,	
	-----	-----
	2004	2003
	-----	-----
Billed utility revenue	\$ 39,783	\$ 41,843
Unbilled utility revenue	27,927	23,876
Other	1,677	2,452
	-----	-----
	69,387	68,171
Less allowance for doubtful accounts	4,849	5,851
	-----	-----
Net accounts receivable	\$ 64,538	\$ 62,320
	=====	=====

The Company's customers are located principally in the following states: 49% in Pennsylvania, 10% in Ohio, 8% in North Carolina, 8% in Illinois, 6% in Texas, 5% in New Jersey, 4% in Florida, and 4% in Indiana. No single

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customer accounted for more than one percent of the Company's operating revenues during the years ended December 31, 2004, 2003 or 2002. The following table summarizes the changes in the Company's allowance for doubtful accounts:

	2004	2003	2002
	-----	-----	-----
Balance at January 1,	\$ 5,851	\$ 3,580	\$ 2,482
Amounts charged to expense	2,621	2,643	3,182
Accounts written off	(4,255)	(2,715)	(2,375)
Recoveries of accounts written off	556	253	291
Allowance acquired through acquisitions	76	2,090	-
	-----	-----	-----
Balance at December 31,	\$ 4,849	\$ 5,851	\$ 3,580
	=====	=====	=====

Regulatory Assets and Liabilities

The regulatory assets represent costs that are expected to be fully recovered from customers in future rates while regulatory liabilities represent amounts that are expected to be refunded to customers in future rates or amounts recovered from customers in advance of incurring the costs. Except for income taxes and the competitive transition charge payment, regulatory assets and regulatory liabilities are excluded from the Company's rate base and do not earn a return. The components of regulatory assets and (liabilities) are as follows:

	December 31,	
	-----	-----
	2004	2003

Income taxes, asset	\$ 68,990	\$ 68,917
Income taxes, liability	(3,283)	(3,434)
CTC payment	6,879	8,026
Postretirement benefits	11,403	6,698
Merger costs	2,170	2,700
Water tank painting	4,593	3,240
Utility plant retirement costs, asset	14,729	13,699
Utility plant retirement costs, liability	(8,184)	(7,484)
Rate case filing expenses & other	13,696	6,399
	-----	-----
	\$110,993	\$ 98,761
	=====	=====

Items giving rise to deferred state income taxes, as well as a portion of deferred Federal income taxes related to certain differences between tax and book depreciation expense, are recognized in the rate setting process on a cash or flow-through basis and will be recovered as they reverse. The regulatory asset associated with the Competitive Transition Charge ("CTC") payment represents the full payoff in 2001, net of amortization, of the allocable share of a CTC as negotiated by Aqua Pennsylvania, Inc. from its electric distribution company, PECO Energy Company. The Pennsylvania Electricity Generation Customer Choice and Competition Act permitted electric distribution utilities to recover their stranded costs from its customers in the form of a CTC. Rate recovery of the \$11,465 CTC payment began in 2000 and is expected to conclude in 2010.

Postretirement benefits include pension and other postretirement benefits. The pension costs include deferred net pension expense in excess of amounts funded which the Company believes will be recoverable in future years as pension funding is required, and in addition includes an additional minimum liability for pensions as a result of a decline in the discount rate assumed for pension obligations and a change in the fair market value of plan assets. The additional minimum liability equals the excess of the accumulated benefit obligation over the fair value of plan assets. The regulatory asset related to postretirement benefits other than pensions represents costs that were deferred between the time that the accrual method of accounting for these benefits was adopted in 1993 and the recognition of the accrual method in the Company's rates as prescribed in subsequent rate filings. Amortization of the amount deferred for postretirement benefits other than pensions began in 1994 and is currently being recovered in rates.

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The regulatory asset related to the recovery of merger costs represents the portion of the Consumers Water Company merger costs that will be recovered in rates as a result of a rate settlement in 2000 and is being amortized over the recovery period. Expenses associated with water tank painting are deferred and amortized over a period of time as approved in the regulatory process. The regulatory asset for utility plant retirement costs, including cost of removal, represents costs already incurred that are expected to be recovered in future rates over a five year recovery period. The regulatory liability for utility plant retirement costs represents amounts recovered through rates during the life of the associated asset and before the costs are incurred. The regulatory asset related to rate case filing expenses represents the costs associated with filing for rate increases that are deferred and amortized over periods that generally range from one to five years.

Income Taxes

The provision for income taxes consists of:

	Years Ended December 31,		
	2004	2003	2002
	-----	-----	-----
Current:			
Federal	\$ 2,042	\$ 11,933	\$ 16,619
State	7,553	7,249	6,647
	-----	-----	-----

	9,595	19,182	23,266
Deferred:			
Federal	41,414	25,521	17,921
State	1,115	1,220	859
	42,529	26,741	18,780
Total tax expense	\$ 52,124	\$ 45,923	\$ 42,046

The statutory Federal tax rate is 35% and for states with a corporate net income tax, the state corporate net income tax rates range from 5.00% to 9.99% for all years presented. The Company's Federal income tax returns for all years through 2000 have been closed, and 2002 was closed as a result of the conclusion of a tax audit.

The reasons for the differences between amounts computed by applying the statutory Federal income tax rate to income before income tax expense are as follows:

	Years Ended December 31,		
	2004	2003	2002
Computed Federal tax expense at statutory rate	\$ 46,245	\$ 40,852	\$ 38,238
Increase in tax expense for depreciation expense to be recovered in future rates	1,376	1,125	558
Merger transaction costs	(24)	(96)	(680)
Charitable contribution	-	(424)	(98)
Deduction for Aqua America common dividends paid under employee benefit plan	(245)	(241)	(207)
Amortization of deferred investment tax credits	(285)	(285)	(283)
Prior year rate reductions	(538)	(431)	(315)
State income taxes, net of federal tax benefit	5,634	5,505	4,879
Other, net	(39)	(82)	(46)
Actual income tax expense	\$ 52,124	\$ 45,923	\$ 42,046

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The tax effects of temporary differences between book and tax accounting that give rise to the deferred tax assets and deferred tax liabilities are as follows:

	December 31,	
	2004	2003
Deferred tax assets:		
Customers' advances for construction	\$ 17,057	\$ 17,133
Costs expensed for book not deducted for tax, principally accrued expenses	1,989	6,525
Utility plant acquisition adjustment basis differences	30,920	21,784
Minimum pension liability adjustment	938	-
Total gross deferred tax assets	50,904	45,442
Deferred tax liabilities:		
Utility plant, principally due to depreciation and differences in the basis of fixed assets due to variation in tax and book accounting	243,953	203,706

Deferred taxes associated with the gross-up of revenues necessary to recover, in rates, the effect of temporary differences	23,670	24,634
Deferred investment tax credit	6,328	6,618
Unrealized gain on marketable securities	-	141
Other	840	738
	-----	-----
Total gross deferred tax liabilities	274,791	235,837
	-----	-----
Net deferred tax liability	\$223,887	\$190,395
	=====	=====

On October 22, 2004, the American Jobs Creation Act ("AJCA") was signed into law. Among other provisions, the AJCA creates a new deduction for qualified domestic production activities. Certain activities of the Company, such as our water treatment activity, are considered as qualifying production activities for purposes of determining the deduction for qualified production activities. The AJCA did not impact the Company's 2004 consolidated financial statements. Thus, the Company is currently assessing the impact, if any, of the AJCA on its consolidated financial statements in future periods. See Summary of Significant Accounting Policies - Recent Accounting Pronouncements for a discussion of the AJCA.

Commitments

The Company maintains agreements with other water purveyors for the purchase of water to supplement its water supply, particularly during periods of peak demand. The agreements stipulate purchases of minimum quantities of water to the year 2026. The estimated annual commitments related to such purchases are expected to approximate \$10,924 through 2009 and \$82,388 thereafter. The Company purchased approximately \$8,724, \$8,014 and \$7,079 of water under these agreements during the years ended December 31, 2004, 2003 and 2002, respectively.

The Company leases motor vehicles, buildings and other equipment under operating leases that are noncancelable. The future annual minimum lease payments due are: \$2,452 in 2005, \$1,833 in 2006, \$1,192 in 2007, \$857 in 2008, \$488 in 2009 and \$692 thereafter. The Company leases parcels of land on which treatment plants and other facilities are situated and adjacent parcels that are used for watershed protection. The operating leases are noncancelable, expire between 2012 and 2052 and contain certain renewal provisions. Certain leases are subject to an adjustment every five years based on changes in the Consumer Price Index. Subject to the aforesaid adjustment, during each of the next five years, approximately \$477 of annual lease payments for land are due, and \$15,215 thereafter. The Company leases treatment plants to other parties under lease agreements that require payments to the Company of \$567 in 2005, \$567 in 2006, \$267 in 2007, \$308 in 2008, \$246 in 2009 and \$3,676 thereafter.

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Rent expense was \$3,267, \$2,993 and \$2,182 for the years ended December 31, 2004, 2003 and 2002, respectively.

Long-term Debt and Loans Payable

The Consolidated Statements of Capitalization provides a summary of long-term debt and loans outstanding as of December 31, 2004 and 2003. The supplemental indentures with respect to certain issues of the First Mortgage Bonds restrict the ability of Aqua Pennsylvania, Inc. and certain other operating subsidiaries of the Company to declare dividends, in cash or property, or repurchase or otherwise acquire the stock of these companies. As of December 31, 2004, approximately \$249,000 of Aqua Pennsylvania's retained earnings and \$62,000 of the retained earnings of certain other subsidiaries were free of these restrictions. Certain supplemental indentures also prohibit Aqua Pennsylvania and certain other subsidiaries of the Company from making loans to, or purchasing the stock of, the Company.

Annual sinking fund payments are required for certain issues of First Mortgage Bonds by the supplemental indentures. The future sinking fund payments

and debt maturities of the Company's long-term debt are as follows:

Interest Rate Range	2005	2006	2007	2008	2009	Thereafter
0.00% to 2.49%	\$ 1,267	\$ 1,337	\$ 1,351	\$ 1,364	\$ 1,388	\$ 13,344
2.50% to 2.99%	1,453	6,495	1,529	1,572	1,619	17,256
3.00% to 3.49%	267	266	12,273	280	290	4,170
3.50% to 3.99%	679	689	700	710	722	3,623
4.00% to 4.99%	-	50	50	50	55	144,230
5.00% to 5.49%	-	-	-	-	-	165,615
5.50% to 5.99%	-	-	-	-	-	89,260
6.00% to 6.49%	-	144	644	10,172	-	100,360
6.50% to 6.99%	10,000	10,000	10,000	-	-	12,000
7.00% to 7.49%	28,500	2,539	2,580	2,625	714	8,147
7.50% to 7.99%	180	194	210	227	245	24,175
8.00% to 8.49%	126	138	152	167	184	25,947
8.50% to 8.99%	-	-	-	-	-	9,000
9.00% to 9.49%	6,568	576	584	594	604	44,318
9.50% to 9.99%	1,155	2,195	995	5,995	995	30,753
10.00% to 10.50%	-	-	-	-	-	6,000
Total	\$ 50,195	\$ 24,623	\$ 31,068	\$ 23,756	\$ 6,816	\$ 698,198

Aqua Pennsylvania had a five-year \$300,000 medium-term note program that expired in December 2004 that provided for the issuance of long-term debt with maturities ranging between one and 35 years at fixed rates of interest, as determined at the time of issuance. The bonds issued under this program were secured by the Thirty-Third Supplement to the trust indenture relating to Aqua Pennsylvania's First Mortgage Bonds. In May 2004, Aqua Pennsylvania issued \$87,000 of First Mortgage Bonds through the program with a weighted-average interest rate of approximately 5.1% and a weighted-average maturity of 13.7 years. The proceeds from this issuance were used to refinance short-term debt and to fund long-term debt maturities.

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In May 2004, an unsecured note of \$70,000 was issued by the Company. Interest under this note is based, at the borrower's option, on either a defined base rate or an adjusted London Interbank Offered Rate corresponding to the interest period selected. The proceeds of this financing were used to fund acquisitions and to refinance existing debt. In November 2004, \$34,000 of the \$70,000 unsecured note was repaid with the proceeds from an equity offering. The remaining balance of the note of \$36,000 is classified as loans payable. In connection with the acquisition of Heater Utilities, Inc. in June 2004, the Company assumed \$22,360 of long-term debt at interest rates ranging from 7.05% to 8.24% due 2012 to 2025, which includes the purchase accounting fair value adjustment of \$3,141, increasing the carrying-value of long-term debt. In November 2004, Aqua Pennsylvania issued \$14,000 tax-exempt bonds due 2039 at a rate of 5.05% and secured by a supplement to the trust indenture relating to Aqua Pennsylvania's First Mortgage Bonds. The proceeds from the bonds issued were used to retire previously issued tax-exempt bonds. At various times during 2004, Aqua Pennsylvania and other operating subsidiaries issued other notes payable and first mortgage bonds in aggregate of \$31,239 at a weighted-average interest rate of 3.76% due at various times ranging from 2006 to 2037. The proceeds from these issuances were used to reduce a portion of the balance of the short-term debt at each of the respective operating subsidiaries and to redeem \$6,000 of first mortgage bonds with a weighted-average interest rate of 9.19%. As of December 31, 2004, the Trustees for eight issues held \$17,196 pending completion of the projects financed with the issues and are reported in the consolidated balance sheet as funds restricted for construction activity.

In July 2003, the Company issued \$135,000 of unsecured notes due 2023 and with an interest rate of 4.87%. The proceeds of this financing were used to fund the acquisition of the AquaSource operations and to refinance existing debt. In July 2003, the Company also issued a \$90,000 unsecured note payable and the proceeds were also used to fund the acquisition of the AquaSource operations. In August 2003, the \$90,000 note payable was repaid with the

proceeds from an equity offering. At various times during 2003, Aqua Pennsylvania, other operating subsidiaries and the Company issued other notes payable and first mortgage bonds in aggregate of \$27,894 at a weighted average interest rate of 4.50% due at various times ranging from 2013 to 2032. The proceeds from these issuances were used to reduce a portion of the balance of the short-term debt at each of the respective operating subsidiaries, to redeem \$7,000 of first mortgage bonds of operating subsidiaries with a weighted average interest rate of 6.35% and redeem the Company's preferred stock of \$172. In connection with the acquisition of the AquaSource operations in July 2003, the Company assumed \$8,131 of long-term debt of which \$7,415 was retired during 2003. The weighted average cost of long-term debt at December 31, 2004 and 2003 was 6.00% and 6.19%, respectively.

Aqua Pennsylvania has a \$70,000 364-day revolving credit facility with four banks and the Company has a \$20,000 364-day bank revolving credit facility. Funds borrowed under these agreements are classified as loans payable and are used to provide working capital. As of December 31, 2004 and 2003, funds borrowed under the Aqua Pennsylvania revolving credit agreements were \$29,000 and \$52,068, respectively, and \$0 and \$19,801 were borrowed under the Company's revolving credit agreement, respectively. Interest under these facilities is based, at the borrower's option, on the prime rate, an adjusted federal funds rate, an adjusted London Interbank Offered Rate corresponding to the interest period selected, an adjusted Euro-Rate corresponding to the interest period selected or at rates offered by the banks. These agreements restrict the total amount of short-term borrowings of Aqua Pennsylvania and the Company. A commitment fee ranging from 1/4 to 1/10 of 1% is charged on the unused portion of the revolving credit agreements. The average cost of borrowing under these facilities was 1.4% and 1.6%, and the average borrowing was \$50,115 and \$62,528, during 2004 and 2003, respectively. The maximum amount outstanding at the end of any one month was \$89,519 in 2004 and \$73,079 in 2003.

At December 31, 2004 and 2003, the Company had combined short-term lines of credit of \$108,000 and \$88,000, respectively. Funds borrowed under these lines are classified as loans payable and are used to provide working capital. As of December 31, 2004 and 2003, funds borrowed under the short-term lines of credit were \$9,810 and \$24,590, respectively. The average borrowing under the lines was \$34,711 and \$50,353 during 2004 and 2003, respectively. The maximum amount outstanding at the end of any one month was \$51,288 in 2004 and \$73,700 in 2003. Interest under the lines is based at the Company's option, depending on the line, on the prime rate, an adjusted Euro-Rate, an adjusted federal funds rate or at rates offered by the banks. The average cost of borrowings under all lines during 2004 and 2003 was 2.3% and 2.4%, respectively.

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Interest income of \$1,762, \$395 and \$287 was netted against interest expense on the consolidated statements of income for the years ended December 31, 2004, 2003 and 2002, respectively. The total interest cost was \$50,441, \$45,057 and \$40,683 in 2004, 2003 and 2002, including amounts capitalized of \$2,304, \$2,127 and \$1,389, respectively.

Fair Value of Financial Instruments

The carrying amount of current assets and liabilities that are considered financial instruments approximates their fair value as of the dates presented. The carrying amount and estimated fair value of the Company's long-term debt are as follows:

	December 31,	
	2004	2003
Carrying amount	\$834,656	\$736,052
Estimated fair value	863,247	781,502

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. The Company's customers' advances for construction and related tax deposits have a carrying value of \$73,095 and

\$72,500 at December 31, 2004 and 2003, respectively. 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 2017 and amounts not paid by the 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.

Preferred Stock

At December 31, 2004, the Company had 1,770,819 shares of Series Preferred Stock with a \$1.00 par value authorized, of which 100,000 shares are designated as Series A Preferred Stock. During 1996, the Company designated and issued in connection with an acquisition 32,200 shares as Series B Preferred Stock, \$1.00 par value. The Series B Preferred Stock was recorded on the consolidated balance sheet at its liquidation value of \$100 per share. In December 2003, the remaining shares of Series B Preferred Stock were redeemed as provided under the provisions of the issue through the issuance of debt of \$960 with a five-year maturity at an interest rate of 6.05% per annum. The Series A Preferred Stock, as well as the undesignated shares of Series Preferred Stock, remains unissued. As of December 31, 2004, the Company did not have any preferred stock outstanding.

Stockholders' Equity

At December 31, 2004, the Company had 300,000,000 shares of common stock authorized; par value \$0.50. Shares outstanding at December 31, 2004, 2003 and 2002 were 95,384,833, 92,589,040 and 84,895,543, respectively. Treasury shares held at December 31, 2004, 2003 and 2002 were 686,747, 681,384 and 2,151,350, respectively.

The Company has a universal shelf registration with the Securities and Exchange Commission to allow for the sale, over time, of up to \$250,000 of various debt and equity securities, including common stock. The Company has issued common stock in these transactions under the universal shelf registration:

- o In November 2004, the Company issued 1,955,000 shares of common stock in a public offering for proceeds of \$42,600, net of expenses. The net proceeds were used to repay a portion of our short-term debt. The indebtedness was incurred by Aqua America in connection with acquisitions.

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- o In August 2003, the Company issued 5,000,000 shares of common stock in a public offering for proceeds of \$90,100, net of expenses. The net proceeds were used to repay an unsecured note of \$90,000. The indebtedness was incurred by Aqua America in connection with the acquisition of the operations that were purchased from AquaSource, Inc.
- o In May 2003, the Company issued 1,868,750 shares of common stock in a public offering for proceeds of \$33,100, net of expenses. The net proceeds were used to repay short-term debt, including the repayment of \$22,000 of indebtedness incurred in connection with the Company's repurchase of 1,513,275 shares of common stock from affiliates of Veolia Environnement, S.A. (formerly Vivendi Environnement, S.A.) in October 2002.

The balance remaining available for use under the universal shelf registration as of December 31, 2004 is \$77,517. In addition, the Company has a shelf registration statement filed with the Securities and Exchange Commission to permit the offering from time to time of shares of common stock and shares of preferred stock for acquisitions. During 2002, 178,664 shares of common stock totaling \$2,745 were issued by the Company to acquire water and wastewater systems. The balance remaining available for use under the acquisition shelf registration as of December 31, 2004 is 2,218,947 shares. The form and terms of such securities shall be determined when and if these securities are issued under these shelf registrations.

In May 2002, Veolia Environnement, S.A. which through its affiliates (collectively "VE") owned approximately 16.8% of our outstanding common stock,

advised the Company of their decision to sell its investment in Aqua America, Inc. VE announced that its decision was part of its overall strategy to divest non-core assets and focus on other business strategies. In September 2002, in order to facilitate the orderly re-distribution of the shares held by VE into the market, the Company completed a secondary offering of 12,356,570 shares of Aqua America common stock held by VE. The number of outstanding shares of common stock was not changed and the Company did not receive any proceeds as a result of this secondary offering. In addition, in October 2002 the Company repurchased 1,513,275 shares of Aqua America, Inc. common stock representing the remainder of the shares of Aqua America, Inc. common stock held by VE. The repurchase of shares was funded with proceeds of \$22,000 from a short-term credit facility. In May 2003, this \$22,000 short-term credit facility was repaid with a portion of the funds from the issuance of 1,868,750 shares of common stock through a shelf registration as described above.

In addition, the Board of Directors has authorized the Company to purchase its common stock, from time to time, in the open market or through privately negotiated transactions. The Company has not repurchased any shares under this authorization since 2000. As of December 31, 2004, 411,209 shares remain available for purchase by the Company.

The Company has a Dividend Reinvestment and Direct Stock Purchase Plan ("Plan") that allows reinvested dividends to be used to purchase shares of common stock at a five percent discount from the current market value. Under the direct stock purchase program, shares are purchased by investors at market price. The shares issued under the Plan are either original issue shares or shares purchased by the Company's transfer agent in the open-market. During 2004, 2003 and 2002, under the dividend reinvestment portion of the Plan, 384,457, 395,605 and 402,084 original issue shares of common stock were sold providing the Company with proceeds of \$7,808, \$7,000 and \$6,407, respectively.

The Company reports comprehensive income in accordance with SFAS No. 130, "Reporting Comprehensive Income." Accordingly, the Company's accumulated other comprehensive income is reported in the Stockholders' Equity section of the Consolidated Balance Sheets, the Consolidated Statements of Stockholders' Equity and the related other comprehensive income is reported in the Consolidated Statements of Income and Comprehensive Income. The Company reports its unrealized gains on securities and minimum pension liability adjustments as other comprehensive income or loss and accumulated other comprehensive income or loss.

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AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

Net Income per Common Share and Equity per Common Share

Basic net income per share is based on the weighted average number of common shares outstanding. Diluted net income per share is based on the weighted average number of common shares outstanding and potentially dilutive shares. The dilutive effect of employee stock options is included in the computation of Diluted net income per share. The following table summarizes the shares, in thousands, used in computing Basic and Diluted net income per share:

	Years ended December 31,		
	2004	2003	2002
Average common shares outstanding during the period for Basic computation	93,247	88,275	85,674
Dilutive effect of employee stock options	1,035	969	864
Average common shares outstanding during the period for Diluted computation	94,282	89,244	86,538

For the year ended December 31, 2004, employee stock options outstanding to purchase 569,900 shares of common stock were excluded from the calculation of diluted net income per share as the options' exercise price was greater than the average market price of the Company's common stock. For the years ended December 31, 2003 and 2002, there were no outstanding employee stock options excluded from the calculation of diluted net income per share as the

average market price of the Company's common stock was greater than the options' exercise price.

Equity per common share was \$7.83 and \$7.11 at December 31, 2004 and 2003, respectively. These amounts were computed by dividing common stockholders' equity by the number of shares of common stock outstanding at the end of each year.

Shareholder Rights Plan

The Company has a Shareholder Rights Plan designed to protect the Company's shareholders in the event of an unsolicited unfair offer to acquire the Company. Each outstanding common share is entitled to one Right which is evidenced by the common share certificate. In the event that any person acquires 20% or more of the outstanding common shares or commences a tender or exchange offer which, if consummated, would result in a person or corporation owning at least 20% of the outstanding common shares of the Company, the Rights will begin to trade independently from the common shares and, if certain circumstances occur, including the acquisition by a person of 20% or more of the outstanding common shares, each Right would then entitle its holder to purchase a number of common shares of the Company at a substantial discount. If the Company is involved in a merger or other business combination at any time after the Rights become exercisable, the Rights will entitle the holder to acquire a certain number of shares of common stock of the acquiring company at a substantial discount. The Rights are redeemable by the Company at a redemption price of \$.01 per Right at any time before the Rights become exercisable. The Rights will expire on March 1, 2008, unless previously redeemed.

Employee Stock and Incentive Plan

In May 2004, the 2004 Equity Compensation Plan ("the 2004 Plan") was approved by the shareholders to replace the 1994 Equity Compensation Plan ("the 1994 Plan"), the Company may grant qualified and non-qualified stock options to officers, key employees and consultants. Officers and key employees may also be granted dividend equivalents and restricted stock. Restricted stock may also be granted to non-employee members of the Board of Directors ("Board"). The 2004 Plan authorizes 3,675,000 shares for issuance under the Plan. A maximum of 50% of the shares available for issuance under the 2004 Plan may be issued as restricted stock and the maximum number of shares that may be subject to grants under the plans to any one individual in any one year is 150,000. Awards under the 2004 Plan are, and awards under the 1994 plan were, made by a committee of the Board of Directors.

AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements (In thousands of dollars, except per share amounts)

Options under the plans were issued at the market price of the stock on the day of the grant. Options are exercisable in installments of 33% annually, starting one year from the date of the grant and expire 10 years from the date of the grant. The following table summarizes stock option transactions for the plans:

	As of or For the Years Ended December 31,					
	2004		2003		2002	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Options:						
Outstanding, beginning of year	2,993,421	\$ 13.31	2,830,133	\$ 12.06	2,559,763	\$ 10.66
Granted	582,650	21.53	613,654	16.98	617,813	16.64
Terminated	(98,286)	16.63	(15,533)	14.78	(8,265)	12.99
Exercised	(427,548)	11.95	(434,833)	10.28	(339,178)	9.82
Outstanding, end of year	3,050,237	\$ 14.96	2,993,421	\$ 13.31	2,830,133	\$ 12.06
Exercisable, end of year	1,911,805	\$ 12.43	1,756,300	\$ 11.01	1,555,483	\$ 9.70

Options exercised during 2004 ranged in price from \$4.56 per

share to \$21.53 per share. At December 31, 2004, 3,678,584 options under the 2004 Plan were still available for grant, although under the terms of the 2004 Plan, terminated, expired or forfeited grants under the 1994 Plan and shares withheld to satisfy tax withholding requirements under the 1994 Plan may be re-issued under the 2004 Plan. The following table summarizes the price ranges of the options outstanding and options exercisable as of December 31, 2004:

	Options Outstanding			Options Exercisable	
	Shares	Weighted Average Remaining Life (years)	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Range of prices:					
\$ 4.56 - 7.99	342,302	1.4	\$ 6.25	342,302	\$ 6.25
\$ 8.00 - 9.99	245,471	5.3	9.39	245,471	9.39
\$10.00 - 12.99	396,510	3.9	11.10	396,510	11.10
\$13.00 - 15.99	433,175	6.3	15.28	433,175	15.28
\$16.00 - 16.99	941,578	7.9	16.65	454,295	16.65
\$17.00 - 21.53	691,201	9.1	20.97	40,052	18.33
	3,050,237	6.5	\$ 14.96	1,911,805	\$ 12.43

Under SFAS No. 123 "Accounting for Stock-Based Compensation" and SFAS No. 148 "Accounting for Stock-Based Compensation - Transition and Disclosure", the Company currently applies the provisions of APB Opinion No. 25 and provides the pro forma disclosure provisions of this statement. Accordingly, no compensation cost has been recognized in the financial statements for stock options that have been granted. Pursuant to the disclosure requirements of SFAS No. 123, "Accounting for Stock-Based Compensation," as amended by SFAS No. 148, pro forma net income available to common stock and earnings per share are presented in the Summary of Significant Accounting Policies - Stock-Based Compensation as if compensation cost for stock options was determined as of the grant date under the fair value method. In December 2004, the FASB issued SFAS No. 123R, "Share-Based Payment" which will change the Company's accounting for the compensation costs for its stock options granted as described in the Summary of Significant Accounting Policies - Recent Accounting Pronouncements.

AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

Restricted stock awards provide the grantee with the rights of a shareholder, including the right to receive dividends and to vote such shares, but not the right to sell or otherwise transfer the shares during the restriction period. During 2004, 2003 and 2002, 34,151, 20,156 and 37,031 shares of restricted stock were granted with a restriction period ranging from six to 36 months. The value of restricted stock awards, which are "compensatory", is equal to the fair market value of the stock on the date of the grant and is amortized ratably over the restriction period. The company recorded compensation expense related to restricted stock awards of \$439, \$369 and \$769 during 2004, 2003 and 2002, respectively.

Pension Plans and Other Postretirement Benefits

The Company maintains a qualified, defined benefit pension plan that covers a majority of its full-time employees who were hired prior to April 1, 2003. Retirement benefits under the plan are generally based on the employee's total years of service and compensation during the last five years of employment. The Company's policy is to fund the plan annually at a level which is deductible for income tax purposes and which provides assets sufficient to meet its pension obligations. To offset certain limitations imposed by the Internal Revenue Code with respect to payments under qualified plans, the Company has a non-qualified Excess Benefit Plan for Salaried Employees in order to prevent certain employees from being penalized by these limitations. The Company also has non-qualified Supplemental Executive Retirement Plans for certain current and retired employees. The net pension costs and obligations of the qualified and non-qualified plans are included in the tables which follow.

Employees hired after April 1, 2003 may participate in a defined contribution plan that provides a Company matching contribution on amounts contributed by participants and an annual profit-sharing contribution based upon a percentage of the eligible participants' compensation.

In addition to providing pension benefits, the Company offers certain Postretirement Benefits other than Pensions ("PBOPs") to employees hired before April 1, 2003 and retiring with a minimum level of service. These PBOPs include continuation of medical and prescription drug benefits for eligible retirees and life insurance benefits for certain eligible retirees. The Company funds its gross PBOP cost through various trust accounts. The benefits of retired officers and certain other retirees are paid by the Company and not from plan assets due to limitations imposed by the Internal Revenue Code.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid in the years indicated:

Years:	Pension Benefits	Other Postretirement Benefits
	-----	-----
2005	\$ 6,453	\$ 1,852
2006	6,541	1,950
2007	6,747	2,047
2008	7,129	2,176
2009	7,452	2,310
2010 - 2014	47,220	14,012

In May 2004, the FASB issued FASB Staff Position ("FSP") No. 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003." FSP 106-2 supersedes FSP 106-1, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003," which was issued in January 2004 and permitted a sponsor of a postretirement health care plan that provides a prescription drug benefit to make a one-time election to defer accounting for the effects of the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the "Act") until more authoritative guidance on the accounting for the federal subsidy was issued. The Company had elected the one-time deferral allowed under FSP 106-1 and as a result adopted FSP 106-2 as required in the third quarter of 2004 and it did not have a material impact on our results of operations or financial position.

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AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

The changes in the benefit obligation and fair value of plan assets, the funded status of the plans and the assumptions used in the measurement of the company's benefit obligation are as follows:

	Pension Benefits		Other Postretirement Benefits	
	2004	2003	2004	2003
	-----	-----	-----	-----
Change in benefit obligation:				
Benefit obligation at January 1,	\$150,098	\$131,059	\$29,134	\$25,436
Service cost	4,312	3,627	1,112	987
Interest cost	9,512	8,999	1,825	1,703
Plan amendments	567	-	6	-
Actuarial loss	12,742	12,222	1,676	1,978
Plan participants' contributions	-	-	631	513
Benefits paid	(6,155)	(5,809)	(1,580)	(1,483)
	-----	-----	-----	-----
Benefit obligation at December 31,	171,076	150,098	32,804	29,134
	-----	-----	-----	-----
Change in plan assets:				
Fair value of plan assets at January 1,	108,731	94,438	14,391	12,200
Actual return on plan assets	8,535	20,021	641	816
Employer contributions	4,181	81	2,522	2,345
Benefits paid	(6,155)	(5,809)	(948)	(970)
	-----	-----	-----	-----
Fair value of plan assets at December 31,	115,292	108,731	16,606	14,391
	-----	-----	-----	-----

Funded status of plan:				
Funded status at December 31,	55,784	41,367	16,198	14,743
Unrecognized actuarial loss	(41,531)	(29,164)	(6,853)	(4,857)
Unrecognized prior service cost	(2,090)	(1,942)	527	590
Unrecognized net transition obligation	1,017	1,227	(6,428)	(7,231)
	-----	-----	-----	-----
Net amount recognized	\$ 13,180	\$ 11,488	\$ 3,444	\$ 3,245
	=====	=====	=====	=====

The Company's pension plans had an accumulated benefit obligation of \$136,851 and \$121,521 at December 31, 2004 and 2003, respectively. The following table provides the net liability recognized on the Consolidated Balance Sheets at December 31,:

	Pension Benefits		Other Postretirement Benefits	
	2004	2003	2004	2003
Prepaid benefits cost	\$ -	\$ -	\$ 762	\$ 937
Accrued benefit cost	(13,180)	(11,488)	(4,206)	(4,182)
Additional minimum liability	(8,928)	(2,003)	-	-
Intangible assets	2,108	1,962	-	-
Regulatory asset	4,140	41	-	-
Accumulated other comprehensive loss	2,680	-	-	-
	-----	-----	-----	-----
Net liability recognized	\$ (13,180)	\$ (11,488)	\$ (3,444)	\$ (3,245)
	=====	=====	=====	=====

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AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

At December 31, 2004 and 2003, the Company's pension plans had benefit obligations in excess of its plan assets. The following tables provide the projected benefit obligation, the accumulated benefit obligation and fair market value of the plan assets as of December, 31:

	Projected Benefit Obligation Exceeds the Fair Value of Plan Assets	
	2004	2003
Projected benefit obligation	\$ 171,076	\$ 150,098
Fair value of plan assets	115,292	108,731
	-----	-----
	Accumulated Benefit Obligation Exceeds the Fair Value of Plan Assets	
	2004	2003
Accumulated benefit obligation	\$ 136,851	\$ 121,521
Fair value of plan assets	115,292	108,731

The following table provides the components of net periodic benefit costs for the years ended December 31,:

	Pension Benefits			Other Postretirement Benefits		
	2004	2003	2002	2004	2003	2002
Service cost	\$ 4,312	\$ 3,627	\$ 3,205	\$ 1,112	\$ 987	\$ 840
Interest cost	9,512	8,999	8,501	1,825	1,703	1,620
Expected return on plan assets	(9,169)	(7,775)	(9,945)	(1,086)	(917)	(953)
Amortization of transition obligation (asset)	(209)	(209)	(209)	803	803	803

Amortization of prior service cost	419	395	414	(57)	(57)	(57)
Amortization of actuarial (gain) loss	1,009	1,282	(2)	125	62	(5)
Amortization of regulatory asset	-	-	-	144	136	136
Capitalized costs	(1,021)	(205)	(66)	(629)	(598)	(520)
Net periodic benefit cost	\$ 4,853	\$ 6,114	\$ 1,898	\$ 2,237	\$ 2,119	\$ 1,864

Accounting for pensions and other postretirement benefits requires 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. Each assumption is reviewed annually with assistance from the Company's actuarial consultant who provides guidance in establishing the assumptions. The assumptions are selected to represent the average expected experience over time and may differ in any one year from actual experience due to changes in capital markets and the overall economy. These differences will impact the amount of pension and other postretirement benefit expense that the Company recognizes.

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AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

The significant assumptions related to the Company's pension and other postretirement benefit plans are as follows:

	Pension Benefits		Other Postretirement Benefits	
	2004	2003	2004	2003
Weighted-average Assumptions Used to Determine Benefit Obligations as of December 31,				
Discount rate	5.75%	6.25%	5.75%	6.25%
Rate of compensation increase	4.0-5.0%	4.0-5.0%	4.0%	4.0%
Assumed Health Care Cost Trend Rates Used to Determine Benefit Obligations as of December 31,				
Health care cost trend rate	n/a	n/a	10%	10%
Rate to which the cost trend is assumed to decline (the ultimate trend rate)	n/a	n/a	5%	5%
Year that the rate reaches the ultimate trend rate	n/a	n/a	2010	2009
Weighted-average Assumptions Used to Determine Net Periodic Benefit Costs for Years Ended December 31,				
Discount rate	6.25%	6.75%	6.25%	6.75%
Expected return on plan assets	8.50%	8.50%	6.0-9.0%	6.0-9.0%
Rate of compensation increase	4.0-5.0%	4.0-5.0%	4.0%	4.0%
Assumed Health Care Cost Trend Rates Used to Determine Net Periodic Benefit Costs for Years Ended December 31,				
Health care cost trend rate	n/a	n/a	10%	10%
Rate to which the cost trend is assumed to decline (the ultimate trend rate)	n/a	n/a	5%	5%
Year that the rate reaches the ultimate trend rate	n/a	n/a	2009	2006

n/a - Assumption is not applicable to pension benefits.

Assumed health-care trend rates have a significant effect on the expense and liabilities for other postretirement benefit plans. The health care trend rate is based on historical rates and expected market conditions. A one-percentage point change in the expected health-care cost trend rates would have the following effects:

1-Percentage- 1-Percentage-

	Point Increase -----	Point Decrease -----
Effect on the health-care component of the accrued other postretirement benefit obligation	\$ 863 =====	\$ (910) =====
Effect on total service and interest cost components of net periodic postretirement health-care benefit cost	\$ 92 =====	\$ (102) =====

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AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

The discount rate is based on a market rate for a recognized-rating agency's high-quality long-term bond portfolio with durations matching the expected payouts under our retirement plans. The Company's pension expense and liability (benefit obligations) increases as the discount rate is reduced.

The Company's expected return on assets is determined by evaluating the asset class return expectations with its advisors as well as actual, long-term, historical results of our asset returns. The Company's pension expense increases as the expected return on assets decreases. The Company believes its actual long-term asset allocation on average will approximate the targeted allocation. The Company's investment strategy is to earn a reasonable rate of return while maintaining risk at acceptable levels through the diversification of investments across and within various asset categories. Investment returns are compared to benchmarks that include the S&P 500 Index, the Lehman Brothers Intermediate Government/Credit Index, and a combination of the two indices. The Pension Committee meets semi-annually to review plan investments and management monitors investment performance quarterly through a performance report prepared by an external consulting firm.

The Company's pension plan asset allocation and the target allocation by asset category are as follows:

	2005 Target Allocation -----	Percentage of Plan Assets at December 31, -----	
		2004 -----	2003 -----
Asset Category:			
Equity securities	65%	62%	66%
Debt securities	35%	27%	32%
Cash	0%	11%	2%
Total	100% =====	100% =====	100% =====

Equity securities include Aqua America, Inc. common stock in the amounts of \$7,373 or 6.4% of total plan assets and \$6,469 or 5.9% of total plan assets as of December 31, 2004 and 2003, respectively.

The asset allocation for the Company's other postretirement benefit plans and the target allocation by asset category are as follows:

	2005 Target Allocation -----	Percentage of Plan Assets at December 31, -----	
		2004 -----	2003 -----
Asset Category:			
Cash	65%	60%	64%
Equity securities	35%	40%	36%
Total	100% =====	100% =====	100% =====

Minimum funding requirements for qualified defined benefit pension plans are determined by government regulations and not by accounting

pronouncements. In accordance with funding rules and the Company's funding policy, during 2005 our pension contribution is expected to be \$7,278. The Company's funding of its PBOP cost during 2005 is expected to approximate \$2,804.

As of December 31, 2004, the Company has an additional minimum liability of \$6,820 associated with our defined benefit plan. The additional minimum liability is a result of the accumulated benefit obligation exceeding the fair value of plan assets. The portion of the additional minimum liability related to our employees in one of our rate jurisdictions results in the establishment of a regulatory asset of \$4,140, as the Company expects recovery of the future, increased pension expense through customer rates. Since the balance of the additional minimum liability of \$2,680 may not be recovered through rates, the accounting requirements for recording a regulatory asset are not met and as a result this amount is recorded as an other comprehensive loss for 2004 through a charge to accumulated other comprehensive income, net of income tax benefits of \$938. The change in the additional minimum liability from December 31, 2003 to December 31, 2004 resulted from the effect of a decreased discount rate, offset partially by an increase in the pension plan assets during 2004 due to positive equity market performance and pension contributions.

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AQUA AMERICA, INC. AND SUBSIDIARIES

Notes to Consolidated Financial Statements
(In thousands of dollars, except per share amounts)

The Company has 401(k) savings plans that cover substantially all employees. The Company makes matching contributions that are invested in Aqua America, Inc. common stock based on a percentage of an employee's contribution, subject to certain limitations. The Company's matching contribution, recorded as compensation expense, was \$1,160, \$921 and \$859 for the years ended December 31, 2004, 2003 and 2002, respectively.

Water and Wastewater Rates

On August 5, 2004, the Pennsylvania Public Utility Commission ("PAPUC") granted Aqua Pennsylvania, Inc. a \$13,800 base rate increase. The rates in effect at the time of the filing included \$11,200 in Distribution System Improvement Charges ("DSIC") or 5.0% above the prior base rates. Consequently, the total base rates increased by \$25,000 and the DSIC was reset to zero. On August 1, 2002, the PAPUC granted Aqua Pennsylvania, Inc. a \$21,226 or 10.2% base rate increase. The rates in effect at the time of the filing included \$9,400 in DSIC at 5.0%. Consequently, the total base rates increased by \$30,626 and the DSIC was reset to zero.

In May 2004, the Company's operating subsidiary in Texas filed an application with the Texas Commission on Environmental Quality to increase rates by \$11,920 over a multi-year period. The application seeks to increase annual revenues in phases and is accompanied by a plan to defer and amortize a portion of the Company's depreciation, operating and other tax expense over a similar multi-year period, such that the annual impact on operating income approximates the requested amount. The application is currently pending before the Commission. The Company commenced billing for the requested rates and implemented the deferral plan in August 2004, in accordance with authorization from the Texas Commission on Environmental Quality in July 2004. The additional revenue billed and collected prior to the final ruling are subject to refund based on the outcome of the ruling. The revenue recognized and the expenses deferred by the Company reflect an estimate of the final outcome of the ruling.

The Company's other operating subsidiaries were allowed annual rate increases of \$6,673 in 2004, \$1,275 in 2003 and \$3,024 in 2002, represented by fourteen, eight and thirteen rate decisions, respectively. Revenues from these increases realized in the year of grant were approximately \$3,995, \$839 and \$1,403 in 2004, 2003 and 2002, respectively.

Four states in which the Company operates permit water utilities, and in some states wastewater utilities, to add a surcharge to their water or wastewater bills to offset the additional depreciation and capital costs related to infrastructure system replacement and rehabilitation projects completed and placed into service between base rate filings. Currently, Pennsylvania, Illinois, Ohio and Indiana allow for the use of infrastructure rehabilitation surcharges. These mechanisms typically adjust periodically based on additional qualified capital expenditures completed or anticipated in a future period. The

infrastructure rehabilitation surcharge is capped as a percentage of base rates, generally 5% of base rates, and is reset to zero when new base rates that reflect the costs of those additions become effective or when a utility's earnings exceed a regulatory benchmark. Infrastructure rehabilitation surcharges provided revenues in 2004, 2003 and 2002 of \$7,817, \$8,147 and \$5,518, respectively.

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Selected Quarterly Financial Data (Unaudited) Aqua America, Inc. and Subsidiaries
(in thousands of dollars, except per share amounts)

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
2004					
Operating revenues	\$ 99,768	\$ 106,524	\$ 120,305	\$ 115,442	\$ 442,039
Operations and maintenance expense	41,831	44,483	46,526	45,505	178,345
Operating income	36,444	40,473	50,997	49,320	177,234
Net income available to common stock	15,575	17,871	24,087	22,474	80,007
Basic net income per common share	0.17	0.19	0.26	0.24	0.86
Diluted net income per common share	0.17	0.19	0.26	0.24	0.85
Dividend paid per common share	0.12	0.12	0.12	0.13	0.49
Dividend declared per common share	0.12	0.12	0.25	-	0.49
Price range of common stock					
- high	22.85	21.96	22.22	24.64	24.64
- low	20.00	18.98	18.90	20.77	18.90
2003					
Operating revenues	\$ 80,489	\$ 83,379	\$ 102,153	\$ 101,212	\$ 367,233
Operations and maintenance expense	30,664	31,029	36,777	42,132	140,602
Operating income	32,446	35,290	46,302	39,523	153,561
Net income available to common stock	13,324	15,235	23,620	18,606	70,785
Basic net income per common share	0.16	0.18	0.26	0.20	0.80
Diluted net income per common share	0.16	0.18	0.26	0.20	0.79
Dividend paid per common share	0.112	0.112	0.112	0.120	0.456
Dividend declared per common share	0.112	0.112	0.232	-	0.456
Price range of common stock					
- high	17.83	19.85	20.07	22.40	22.40
- low	15.77	17.22	18.28	18.71	15.77

High and low prices of the Company's common stock are as reported on the New York Stock Exchange Composite Tape. The cash dividends paid in December 2004 of \$0.13 and December 2003 of \$0.12 were declared in August 2004 and August 2003, respectively.

Beginning August 1, 2003, the financial results for the operations acquired in the AquaSource acquisition have been included in the Company's consolidated financial statements.

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Summary of Selected Financial Data Aqua America, Inc. and Subsidiaries
(in thousands of dollars, except per share amounts)

Years ended December 31,	2004	2003 (a)	2002	2001	2000
PER COMMON SHARE:					
Net income					
Basic	\$ 0.86	0.80	0.78	0.71	0.65
Diluted	0.85	0.79	0.78	0.70	0.65
Cash dividends declared and paid	0.49	0.46	0.43	0.40	0.38
Return on average stockholders' equity	11.4%	12.3%	13.9%	13.3%	13.2%
Book value at year end	\$ 7.83	\$ 7.11	\$ 5.80	\$ 5.52	\$ 5.10
Market value at year end	24.59	22.10	16.48	18.04	15.68
INCOME STATEMENT HIGHLIGHTS:					
Operating revenues	\$ 442,039	\$ 367,233	\$ 322,028	\$ 307,280	\$ 274,014
Depreciation and amortization	58,864	51,463	44,322	40,168	34,100
Interest expense, net (b)	46,375	42,535	39,007	38,637	37,775
Income before income taxes	132,131	116,718	109,252	99,087	86,995
Provision for income taxes	52,124	45,923	42,046	38,976	34,105
Net income available to common stock	80,007	70,785	67,154	60,005	52,784
BALANCE SHEET HIGHLIGHTS:					
Total assets	\$2,340,248	\$2,069,736	\$1,717,069	\$1,555,108	\$1,413,723
Property, plant and equipment, net	2,069,812	1,824,291	1,486,703	1,364,282	1,249,652
Stockholders' equity	748,468	659,030	493,097	472,717	430,587
Long-term debt, including current portion	834,656	736,052	617,175	531,455	472,712
Total debt	919,771	832,511	732,288	641,123	573,706
ADDITIONAL INFORMATION:					
Net cash flows from operating activities	\$ 173,603	\$ 143,373	\$ 121,560	\$ 102,165	\$ 86,972

Capital additions	195,736	163,320	136,164	124,088	129,740
Net cash expended for acquisitions					
of utility systems	54,300	192,331	8,914	9,517	3,546
Dividends on common stock	45,807	39,917	36,789	34,234	30,406
Number of customers served	835,512	749,491	605,474	587,537	565,146
Number of shareholders of common stock	24,082	22,726	21,389	20,920	20,978
Common shares outstanding (000)	95,385	92,589	84,896	85,483	83,869
Employees (full-time)	1,442	1,260	971	951	943

- (a) Beginning August 1, 2003, the financial results for the operations acquired in the AquaSource acquisition have been included in Aqua America's consolidated financial statements.
- (b) Includes dividends on preferred stock of subsidiary and minority interest, net of allowance for funds used during construction.

AQUA AMERICA, INC. AND SUBSIDIARIES

The following table lists the significant subsidiaries and other active subsidiaries of Aqua America, Inc. at December 31, 2004:

Aqua Pennsylvania, Inc. (Pennsylvania)
Aqua Resources, Inc. (Pennsylvania)
Aqua Services, Inc. (Delaware)
Aqua Ohio, Inc. (Ohio)
Aqua Illinois, Inc. (Illinois)
Aqua New Jersey, Inc. (New Jersey)
Aqua Maine, Inc. (Maine)
Aqua North Carolina, Inc. (North Carolina)
Aqua Texas, Inc. (Texas)
Aqua Indiana, Inc. (Indiana)
Aqua Utilities, Inc. (Texas)
Aqua Virginia, Inc. (Virginia)
Aqua Utilities Florida, Inc. (Florida)
Aqua Missouri, Inc. (Missouri)
Aqua South Carolina, Inc. (South Carolina)
Heater Utilities, Inc. (North Carolina)

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We hereby consent to the incorporation by reference in the Registration Statements on Form S-3 (Nos. 333-61772, 333-42275, 333-104290 and 333-122900), on Form S-4 (No. 333-93243), and on Form S-8 (Nos. 333-61768, 333-70859, 033-52557, 333-81085, 333-107673, 333-113502 and 333-116776) of Aqua America, Inc. of our report dated March 14, 2005 relating to the consolidated financial statements, management's assessment of the effectiveness of internal controls over financial reporting and the effectiveness of internal control over financial reporting, which appears in the Annual Report to Shareholders, which is incorporated in this Annual Report on Form 10-K.

PRICEWATERHOUSECOOPERS LLP

Philadelphia, Pennsylvania
March 14, 2005

CERTIFICATION

I, Nicholas DeBenedictis, Chairman, President and Chief Executive Officer of Aqua America, Inc., certify that:

1. I have reviewed this annual report on Form 10-K of Aqua America, Inc.;
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and we have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures, and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 14, 2005

NICHOLAS DEBENEDICTIS

Nicholas DeBenedictis
Chairman, President and Chief Executive Officer

CERTIFICATION

I, David P. Smeltzer, Senior Vice President - Finance and Chief Financial Officer of Aqua America, Inc., certify that:

1. I have reviewed this annual report on Form 10-K of Aqua America, Inc.;
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and we have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures, and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 14, 2005

DAVID P. SMELTZER

David P. Smeltzer

Senior Vice President - Finance and Chief Financial Officer

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350

In connection with the Annual Report on Form 10-K for the year ended December 31, 2004 of Aqua America, Inc. (the "Company") as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Nicholas DeBenedictis, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. Section 78m(a) or Section 78o(d)); and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

NICHOLAS DEBENEDICTIS

Nicholas DeBenedictis
Chairman, President and Chief Executive Officer
March 14, 2005

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350

In connection with the Annual Report on Form 10-K for the year ended December 31, 2004 of Aqua America, Inc. (the "Company") as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, David P. Smeltzer, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. Section 78m(a) or Section 78o(d)); and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

DAVID P. SMELTZER

David P. Smeltzer
Senior Vice President - Finance and Chief Financial Officer
March 14, 2005