

THE YORK WATER COMPANY

2010 Annual Report



Providing **VALUE** for 195 Years
through

CUSTOMER SERVICE
Growth
PERFORMANCE



195th YEAR

TABLE OF CONTENTS

President and CEO's Letter

<i>Dear Shareholders.....</i>	2
-------------------------------	----------

Financials

<i>Highlights of Our 195th Year</i>	5
---	----------

<i>Shareholder Information.....</i>	6
-------------------------------------	----------

<i>Management's Discussion and Analysis.....</i>	8
--	----------

<i>Management's Report on Internal Control Over Financial Reporting</i>	18
---	-----------

<i>Report of Independent Registered Public Accounting Firm on Internal Control Over Financial Reporting</i>	19
---	-----------

<i>Report of Independent Registered Public Accounting Firm.....</i>	20
---	-----------

<i>Balance Sheets</i>	21
-----------------------------	-----------

<i>Statements of Income</i>	22
-----------------------------------	-----------

<i>Statements of Common Stockholders' Equity and Comprehensive Income.....</i>	23
--	-----------

<i>Statements of Cash Flows</i>	24
---------------------------------------	-----------

<i>Notes to Financial Statements</i>	25
--	-----------

Additional Information

<i>Supplemental Information</i>	44
---------------------------------------	-----------

<i>Directors.....</i>	46
-----------------------	-----------

<i>Officers and Key Employees.....</i>	47
--	-----------

<i>Transfer Agent and Registrar</i>	47
---	-----------

<i>Stock Exchange Listing</i>	47
-------------------------------------	-----------

<i>Independent Auditors</i>	47
-----------------------------------	-----------

<i>Chartered Territory Distribution and Supply System</i>	48
---	-----------



Front Cover: The original directors and employees of The York Water Company insert the first tap into the wooden water main, in 1816. "Hydran Water" by Folk Artist, Lewis Miller (1796-1882) is from the collection of the York County Heritage Trust, York, PA.

Providing **VALUE** for 195 Years
through

**CUSTOMER SERVICE
Growth
PERFORMANCE**



Almost 200 years have gone by since York's first water was supplied from a spring located on Peter Small's tract of land to customers through bored out "wooden maines". Those first water mains were constructed to provide a growing community with protection against fires. Over the years the mission has grown to also provide drinking water and economic development.

Ten years have gone by since The York Water Company was listed on NASDAQ – celebrated in 2010 with the ceremonial ringing of the closing bell on October 25 in New York City. Through two centuries of dedicated service, consistent growth, and excellent performance, America's oldest investor owned water company continues to provide exceptional **VALUE TO CUSTOMERS, SHAREHOLDERS, AND THE COMMUNITIES WE SERVE.**

Through acquisition of existing water systems in new areas, and servicing new regional manufacturing/ distribution facilities, both Residential and Commercial customer bases were expanded in 2010. At less than a penny per gallon – some of the lowest regulated water rates in Pennsylvania, The York Water Company provides exceptional **VALUE TO ITS CUSTOMERS.**

Despite the continuation of an uncertain economic climate throughout 2010, The York Water Company continued to thrive and achieved a Record Year of financial growth and provided dividend payments for the 195th consecutive year - a remarkable **VALUE FOR OUR SHAREHOLDERS.**

Planned capital expenditures continued for infrastructure replacement, facility expansion, and distribution system improvements to insure that there is a safe, reliable, and abundant supply of water available to current and future customers - an investment with **VALUE FOR THE COMMUNITIES WE SERVE.**

With strong leadership and dedicated experienced employees, The York Water Company is well positioned to continue this long-standing tradition of providing **VALUE THROUGH CUSTOMER SERVICE, GROWTH, AND PERFORMANCE** for many years to come - doing whatever is required to provide "That good York water" for our growing communities.



Jeffrey R. Hines, P.E.

President and
Chief Executive Officer

Dear Shareholders,

I am pleased to report a record year for The York Water Company which continues its 195 year tradition of service, growth, and performance.

Record Financial Performance

Due to our continued growth, 2010 results were the best in our history.

Operating revenues grew by 5.3% to \$39.0 million in 2010. Operating income increased 13.7% to \$19.8 million. Our net income increased by 18.9% to \$8.9 million in 2010. Earnings per share increased 10.9% to \$0.71 per share.

Continued Growth, Acquisitions, and Expansion

The average number of customers served grew by 0.9% during 2010 to 62,474. The percent of customer growth in 2010 was below our five year average of 3% due to a slowdown in the housing market due to the economy. The Company is now authorized to serve in 46 municipalities in Adams and York Counties. Population served grew by 1.1% in 2010 to approximately 182,000.

In 2010, The York Water Company continued its long tradition of acquiring troubled water systems and providing water service into new areas. In 2010, the customers of the Evergreen Lane Water System in York County became customers of York Water. Evergreen Lane, which served approximately 50 people, is now a part of York Water's service population of over 182,000.

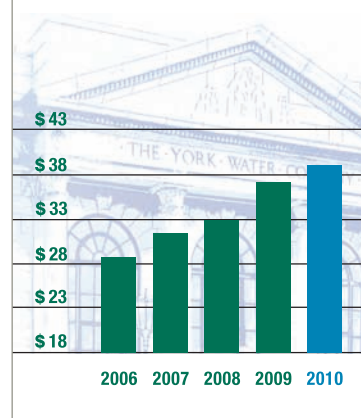
Church & Dwight Expands Major Facility in York

In 2010, Church & Dwight Co, Inc. expanded operations at their recently completed Arm & Hammer detergent manufacturing and distribution facility in York. They are currently our fourth largest customer. At full production it is anticipated that this facility will be our second largest customer. One of the major reasons that Church & Dwight expanded the facility in York was a reasonable cost structure and an abundant supply of high quality water.

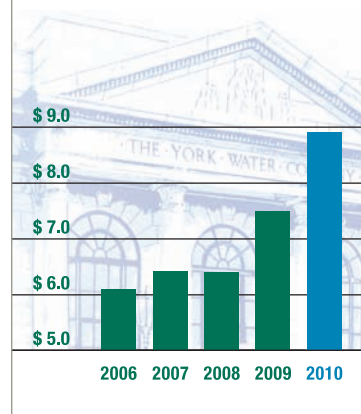
Debt Issue

In the fall of 2010, the Company issued \$15,000,000 of 5.00% senior notes due in 2040. The debt proceeds were used to pay off short-term borrowings used for acquisitions, to retire maturing long-term debt issues, and for construction expenditures including: replacements and expansion at the filter plant and pumping station, and a continuing water main replacement and distribution system improvement program.

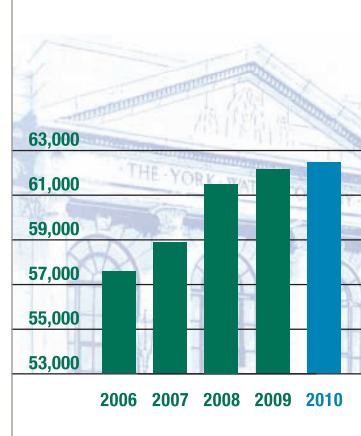
Operating Revenue
(millions)



Net Income
(millions)



Customers





The York Water Company celebrated its 195th Business Anniversary and 10 Year Listing on NASDAQ by ringing the NASDAQ Stock Market Closing Bell.

Dividends and Shareholder Value

In line with our objective to maintain regular dividend increases, we raised the quarterly dividend rate by 2.3% during the year. This is the fourteenth consecutive year we have raised our dividend and the 195th consecutive year of dividend payments. We believe this to be the longest consecutive dividend record of any public corporation in America.

Our financial position continued to excel in 2010. The market price of our common stock increased \$2.78 per share to \$17.29, or a 19.2% increase. In addition, the dividend was increased in 2010 by 1.8% to \$0.515 per share, for a yield on December 31, 2010 of about 3.0%. If a share of stock were purchased on December 31, 2009, the total return for the year would be 22.2%. If a share of stock were purchased at the market's low point of the year: May 26, 2010, at \$13.01, the total return for the year would have been above 35%.

Continued Success of a Direct Stock Purchase Plan

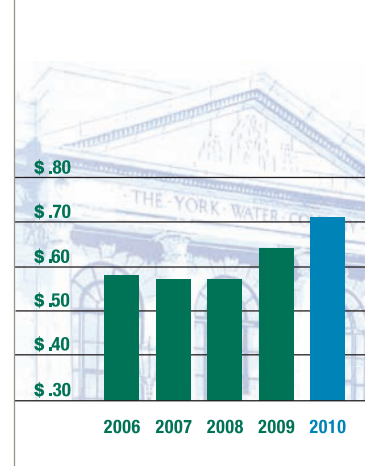
In 2010 the Company continued its Direct Stock Purchase Plan that allows for the purchase of up to \$40,000 per year directly from the company at market price without any fees. Dividends can then be reinvested automatically at a 5% discount, again with no fees. Interested investors should go to www.yorkwater.com and review the prospectus for additional information and to participate in the program.

Rate Increase Approved, Water Still Costs Less than One Cent per Gallon

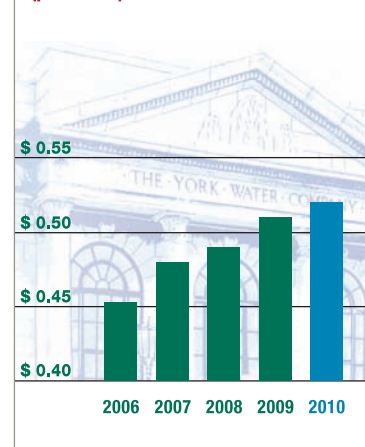
On November 4, 2010 the Pennsylvania Public Utility Commission approved a \$3.4 million per year increase in revenue. Although it was a difficult time to raise customers' rates, it was necessary to pay for \$30 million in capital improvements that have been completed since the last rate increase. Much of this investment was required to replace critical infrastructure and to insure our customers have a safe, reliable, and abundant supply of water now and into the future.

The York Water Company continues to maintain the lowest customer complaint rate in the state and York Water's rates remain among the lowest in the state.

Earnings Per Share



Common Stock Dividends (per share)



Customers/Employee

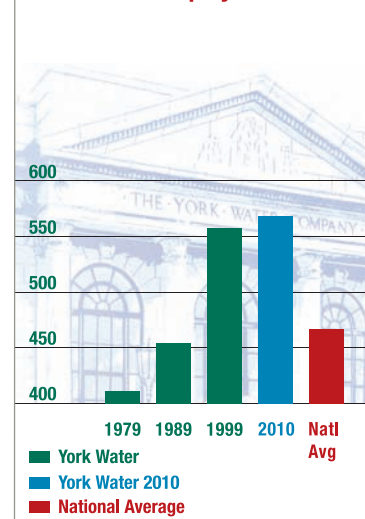




Photo above: Jeffrey R. Hines, P.E. (on right) expresses appreciation to William T. Morris (on left) for 43 years of service to The York Water Company.



Photo on right: Filter Plant operators understand the value of a clean and consistent water supply. In 2010 the Operators celebrated the accomplishment of maintaining filtered water turbidity below .10 NTUs for ten straight years, well below the .30 NTU requirement. Filter Plant operators (front row) Dave Zarfoss, Dale Barnhart (Asst. Superintendent), John Poklembo (Superintendent), John Gunnet; (back row) Mike Spilman, George Roundtree, Tom Bailey, and Sharon Markey. (Not shown: Sam Napier).

Personal Service and “green” Electronic Billing

Although we are a 195 year old company, we continue to make technological advances to assist our customers. However we still strive to provide that personal touch. When you call our office, one of our friendly customer service representatives will answer the phone and assist you. In 2010 we initiated electronic billing. Now, instead of receiving a paper bill, customers have the option of getting it delivered to their email account each month with directions on how they can pay their bill on-line. Of course, our historic office in downtown York remains open for walk-in or phone-in customer support.

Dedicated and Experienced Employees

A Company that continues to thrive and grow, and improve service to its customers for 195 years, can only be possible due to the dedication, loyalty, and hard work of its talented employees. We thank all of the York Water family for their commitment to make this Company the most efficient water utility in the nation.

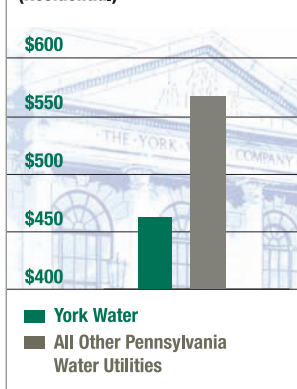
William T. Morris Retires After 43 Years of Service

William T. Morris has been a leader of The York Water Company as General Manager and President for 30 years, Chairman of the Board for 7 years, and as a Director for 32 years. During his long tenure, Bill demonstrated a resolute dedication to the Company and helped transform it into its preeminent position in the community and in the water profession. Bill will continue to serve the Company as a Director Emeritus.

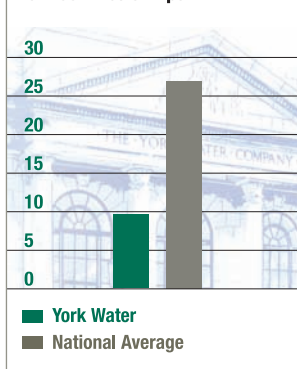
Outlook

We continue our efforts to grow our business and serve our communities. We monitor our operating region for opportunities to acquire new franchise territories and enter into non-regulated business activities so that we may provide our rich history, experience, and know-how to communities that realize the importance of a high quality, drought-resistant supply of water for domestic, commercial, industrial, and fire protection uses. In 2011 we will enter into our first wastewater contract and provide billing and customer service to area wastewater authorities, starting with the Jefferson-Codorus Joint Sewer Authority. We will continue to anticipate our communities’ growth so that wherever and whenever “That good York water” is needed, it will be available in plentiful supply.

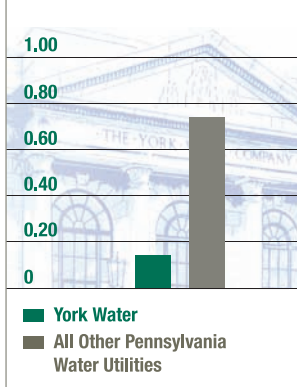
Average Annual Cost for Water (Residential)



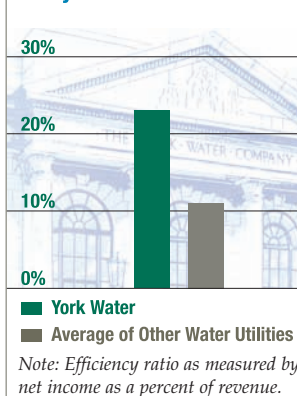
Main Breaks Per 100 Miles of Pipe



Complaint Rate Per 1000 Customers



Most Efficient Water Utility in America



Highlights of Our 195th Year

(In thousands of dollars, except per share amounts)

For the Year	Summary of Operations				
	2010	2009	2008	2007	2006
Water operating revenues	\$ 39,005	\$ 37,043	\$ 32,838	\$ 31,433	\$ 28,658
Operating expenses	19,238	19,655	18,158	17,333	15,754
Operating income	19,767	17,388	14,680	14,100	12,904
Interest expense	4,795	4,780	4,112	3,916	3,727
Other income (expenses), net	(465)	(517)	(509)	(78)	110
Income before income taxes	14,507	12,091	10,059	10,106	9,287
Income taxes	5,578	4,579	3,628	3,692	3,196
Net income	\$ 8,929	\$ 7,512	\$ 6,431	\$ 6,414	\$ 6,091

Per Share of Common Stock

Book value	\$ 7.19	\$ 6.92	\$ 6.14	\$ 5.97	\$ 5.84
Basic earnings per share	0.71	0.64	0.57	0.57	0.58
Cash dividends declared per share	0.515	0.506	0.489	0.475	0.454
Weighted average number of shares outstanding during the year	12,626,660	11,695,155	11,298,215	11,225,822	10,475,173

Utility Plant

Original cost, net of acquisition adjustments	\$ 269,856	\$ 259,839	\$ 245,249	\$ 222,354	\$ 202,020
Construction expenditures	10,541	12,535	24,438	18,154	20,678

Other

Total assets	\$ 259,931	\$ 248,837	\$ 240,442	\$ 210,969	\$ 196,064
Long-term debt including current portion	85,173	77,568	86,353	70,505	62,335

For Management's Discussion and Analysis of Financial Condition and Results of Operations, please refer to page 8.

Shareholder Information

Market for Common Stock and Dividends

The common stock of The York Water Company is traded on the NASDAQ Global Select Market (Symbol "YORW").

Quarterly price ranges and cash dividends per share for the last two years follow:

	2010			2009		
	High	Low	Dividend*	High	Low	Dividend*
1st Quarter	\$15.00	\$13.04	\$0.128	\$13.50	\$9.74	\$0.126
2nd Quarter	15.60	12.83	0.128	16.26	11.75	0.126
3rd Quarter	16.40	13.42	0.128	17.95	13.75	0.126
4th Quarter	18.00	15.52	0.131	15.24	13.65	0.128

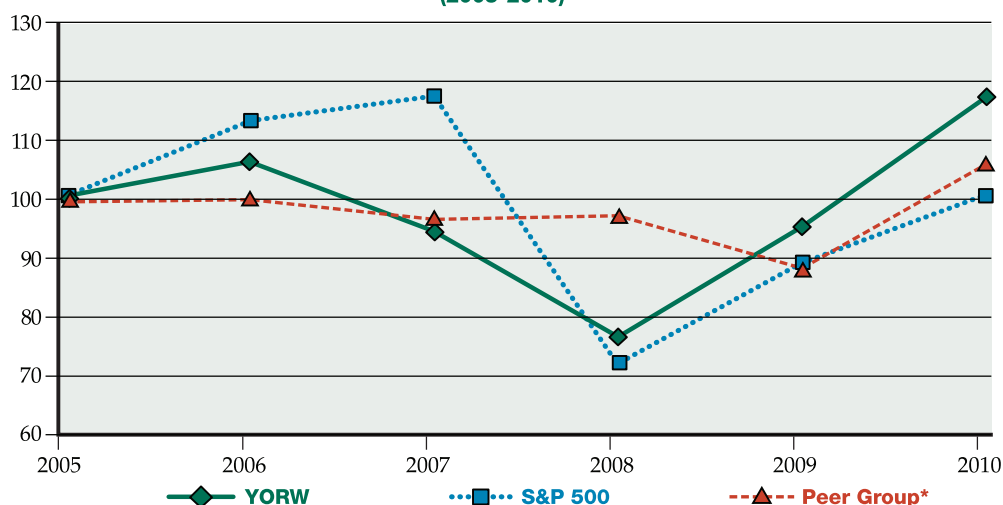
*Cash dividends per share reflect dividends declared at each dividend date.

Prices listed in the above table are sales prices as listed on the NASDAQ Global Select Market. Shareholders of record (excluding individual participants in securities positions listings) as of December 31, 2010 numbered approximately 1,649.

Performance Graph

The following line graph presents the annual and cumulative total shareholder return for The York Water Company Common Stock over a five-year period from 2005 through 2010, based on the market price of the Common Stock and assuming reinvestment of dividends, compared with the cumulative total shareholder return of companies in the S&P 500 Index and a peer group made up of publicly traded water utilities, also assuming reinvestment of dividends. The peer group companies include: American States, Aqua America, Artesian Resources, California Water Service, Connecticut Water Service, Middlesex Water, Pennichuck Corporation and San Jose Water.

**The York Water Company: Price Performance
(2005-2010)**



	2005	2006	2007	2008	2009	2010
The York Water Company	100.00	106.37	94.84	76.67	95.34	117.43
S&P 500 Index	100.00	113.62	117.63	72.36	89.33	100.75
Peer Group*	100.00	100.19	96.79	97.25	88.32	106.26

*ARTNA, AWR, CTWS, CWT, MSEX, PNNW, SJW, WTR
Source: FactSet Research Systems Inc.

Shareholder Information

Dividend Policy

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

The dividend paid on the Company's common stock on January 14, 2011 was the 560th consecutive dividend paid by the Company. The Company has paid consecutive dividends for its entire history, since 1816. The policy of our Board of Directors is currently to pay cash dividends on a quarterly basis. The dividend rate has been increased annually for fourteen consecutive years. The Company's Board of Directors declared dividend number 561 in the amount of \$0.131 per share at its January 2011 meeting. The dividend is payable on April 15, 2011 to shareholders of record as of February 28, 2011. Future cash dividends will be dependent upon the Company's earnings, financial condition, capital demands and other factors and will be determined by the Company's Board of Directors. See Note 4 to the Company's financial statements included herein for restrictions on dividend payments.

Financial Reports and Investor Relations

Shareholders may request, without charge, copies of the Company's financial reports, including Annual Reports, and Forms 8-K, 10-K and 10-Q filed with the Securities and Exchange Commission (SEC). Such requests, as well as other investor relations inquiries, should be addressed to:

Kathleen M. Miller — Chief Financial Officer

The York Water Company
P.O. Box 15089, York, PA 17405-7089

(717) 845-3601
(800) 750-5561
kathym@yorkwater.com

The Annual Report as well as reports filed with the SEC and other information about the Company can also be found on the Company's website at: www.yorkwater.com.

Management's Discussion & Analysis of Financial Condition & Results of Operations

(In thousands of dollars, except per share amounts)

FORWARD-LOOKING STATEMENTS

This Annual Report contains certain matters which are not historical facts, but which are forward-looking statements. Words such as "may," "should," "believe," "anticipate," "estimate," "expect," "intend," "plan" and similar expressions are intended to identify forward-looking statements. The Company intends these forward-looking statements to qualify for safe harbor from liability established by the Private Securities Litigation Reform Act of 1995. These forward-looking statements include certain information relating to the Company's business strategy; statements including, but not limited to:

- expected profitability and results of operations;
- goals, priorities and plans for, and cost of, growth and expansion;
- strategic initiatives;
- availability of water supply;
- water usage by customers; and
- ability to pay dividends on common stock and the rate of those dividends.

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

- changes in weather, including drought conditions;
- levels of rate relief granted;
- the level of commercial and industrial business activity within the Company's service territory;
- construction of new housing within the Company's service territory and increases in population;
- changes in government policies or regulations;
- the ability to obtain permits for expansion projects;
- material changes in demand from customers, including the impact of conservation efforts which may impact the demand of customers for water;
- changes in economic and business conditions, including interest rates, which are less favorable than expected;
- changes in, or unanticipated, capital requirements;
- changes in accounting pronouncements;
- changes in our credit rating or the market price of our common stock;
- the ability to obtain financing; and
- other matters set forth in Item 1A, "Risk Factors," of the Company's Annual Report on Form 10-K for the year ended December 31, 2010.

OVERVIEW

The Company is the oldest investor-owned water utility in the United States and is duly organized under the laws of the Commonwealth of Pennsylvania. The Company has operated continuously since 1816. The business of the Company is to impound, purify to meet or exceed safe drinking water standards and distribute water. The Company operates within its franchised territory, which covers 39 municipalities within York County, Pennsylvania and seven municipalities within Adams County, Pennsylvania. The Company is regulated by the Pennsylvania Public Utility Commission, or PPUC, in the areas of billing, payment procedures, dispute processing, terminations, service territory, debt and equity financing and rate setting.

Management's Discussion & Analysis of Financial Condition & Results of Operations

(In thousands of dollars, except per share amounts)

The Company must obtain PPUC approval before changing any practices associated with the aforementioned areas. Water service is supplied through the Company's own distribution system. The Company obtains its water supply from both the South Branch and East Branch of the Codorus Creek, which together have an average daily flow of 73.0 million gallons per day. This combined watershed area is approximately 117 square miles. The Company has two reservoirs, Lake Williams and Lake Redman, which together hold up to approximately 2.2 billion gallons of water. The Company has a 15-mile pipeline from the Susquehanna River to Lake Redman which provides access to an additional supply of 12.0 million gallons of untreated water per day. As of December 31, 2010, the Company's average daily availability was 35.0 million gallons, and daily consumption was approximately 18.9 million gallons. The Company's service territory had an estimated population of 182,000 as of December 31, 2010. Industry within the Company's service territory is diversified, manufacturing such items as fixtures and furniture, electrical machinery, food products, paper, ordnance units, textile products, air conditioning systems, laundry detergent, barbells and motorcycles.

The Company's business is somewhat dependent on weather conditions, particularly the amount of rainfall. Revenues are particularly vulnerable to weather conditions in the summer months. Prolonged periods of hot and dry weather generally cause increased water usage for watering lawns, washing cars, and keeping golf courses and sports fields irrigated. Conversely, prolonged periods of dry weather could lead to drought restrictions from governmental authorities. Despite the Company's adequate water supply, customers may be required to cut back water usage under such drought restrictions which would negatively impact our revenues. The Company has addressed some of this vulnerability by instituting minimum customer charges which are intended to cover fixed costs of operations under all likely weather conditions. In 2010, per capita consumption by industrial and commercial customers showed a modest increase over prior year while residential customer use decreased slightly. Total per capita consumption for the year was approximately 0.3% higher compared to 2009.

The Company's business does not require large amounts of working capital and is not dependent on any single customer or a very few customers for a material portion of its business. In 2010, operating revenue was derived from the following sources and in the following percentages: residential, 63%; commercial and industrial, 29%; and other, 8%, which is primarily from the provision for fire service. Increases in revenues are generally dependent on the Company's ability to obtain rate increases from regulatory authorities in a timely manner and in adequate amounts and to increase volumes of water sold through increased consumption and increases in the number of customers served. The Company continuously looks for acquisition and expansion opportunities both within and outside its current service territory. The Company also looks for additional opportunities to enter into bulk water contracts with municipalities and other entities to supply water.

During the five-year period ended December 31, 2010, the Company has maintained growth in the number of customers and distribution facilities as demonstrated by the following chart:

	2010	2009	2008	2007	2006
Average daily consumption (gallons per day)	18,875,000	18,233,000	18,298,000	19,058,000	18,769,000
Miles of mains at year-end	925	922	884	845	817
Additional distribution mains installed/acquired (ft.)	19,886	200,439	206,140	147,803	159,330
Number of customers at year-end	62,505	62,186	61,527	58,890	57,578
Population served at year-end	182,000	180,000	176,000	171,000	166,000

Management's Discussion & Analysis of Financial Condition & Results of Operations

(In thousands of dollars, except per share amounts)

PERFORMANCE MEASURES

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

The Company's 2010 performance was strong under the above measures. Increases in the number of customers and per capita water usage by the customers, increased rates from a rate filing and a higher distribution system improvement charge (DSIC) resulted in higher revenue. The DSIC allows the Company to add a charge to customers' bills for qualified replacement costs of certain infrastructure without submitting a rate filing. In addition, the Company incurred lower operating and maintenance expenses in 2010. The overall effect was an increase in net income in 2010 over 2009 of 18.9% and a return on year end common equity at its highest level in five years.

The efficiency ratio, which is calculated as net income divided by revenues, is used by management to evaluate its ability to keep expenses in line. Over the five previous years, our ratio averaged 20.7%. In 2010, the ratio increased to 22.9% due to the higher net income resulting from higher revenue and reduced expenses. Management is confident that our ratio will again exceed that of our peers. Management continues to look for ways to decrease expenses and increase efficiency as well as to file for rate increases promptly when needed. Effective November 4, 2010, the PPUC authorized an increase in rates which will allow for recovery of some of the expected increases in expense.

RESULTS OF OPERATIONS

2010 COMPARED WITH 2009

Net income for 2010 was \$8,929, an increase of \$1,417, or 18.9%, from net income of \$7,512 for 2009. The primary contributing factors to the increase in net income were higher water revenues and reduced expenses for salary and wages, distribution system maintenance and employee retirement. Higher capitalized overhead and lower interest expense added to the reduction in expenses which were partially offset by higher depreciation expense, a reduced allowance for funds used during construction, higher power costs and increased capital stock tax.

Water operating revenues for the year increased \$1,962, or 5.3%, from \$37,043 for 2009 to \$39,005 for 2010. The primary reasons for the increase in revenues were an increased DSIC, a rate increase effective November 4, 2010 and growth in the customer base. The average number of customers served in 2010 increased as compared to 2009 by 577 customers, from 61,897 to 62,474 customers. The total per capita volume of water sold in 2010 increased compared to 2009 by approximately 0.3%. Per capita consumption by industrial and commercial customers showed a modest increase over prior year and was partially offset by a slight decrease in use by residential customers. The Company expects revenues to continue to increase in 2011 as a result of the full year's impact of the rate increase granted in November 2010. Drought warnings or restrictions as well as regulatory actions and weather patterns could impact results.

Operating expenses for the year decreased \$417, or 2.1%, from \$19,655 for 2009 to \$19,238 for 2010. The decrease was primarily due to lower salary and wage expense of approximately \$177. This was mainly a result of the vacation accrual recorded in 2009 as discussed in Note 1 (Reclassifications) to the Company's financial statements included herein. Lower distribution system maintenance expense of approximately \$158, increased capitalized overhead of approximately \$152, and reduced pension cost and other expenses aggregating approximately \$275 added to the reduction of expenses. Higher depreciation expense due to increased plant investment, increased power costs and higher capital stock tax aggregating

Management's Discussion & Analysis of Financial Condition & Results of Operations

(In thousands of dollars, except per share amounts)

approximately \$345 partially offset the decrease. Depreciation expenses are expected to continue to rise due to investment in utility plant, pension expense is expected to rise due to an expected increase in contributions to be made to the plans and other operating expenses are expected to increase at a moderate rate as costs to serve customers and to extend our distribution system continue to rise.

Interest on debt for 2010 decreased \$84, or 1.7%, from \$4,990 for 2009 to \$4,906 for 2010. The primary reasons for the decrease were lower interest payments of \$131 due to the retirement of the 3.60% Industrial Development Authority Revenue Refunding Bonds, Series 1994, in May of 2009 and the 3.75% Industrial Development Authority Revenue Refunding Bonds, Series 1995, in June of 2010, lower interest of \$81 on the Company's lines of credit due to reduced borrowings and lower interest of \$47 on the \$12,000 variable rate bonds due to reduced interest rates. The decrease in expense was partially offset by higher interest of \$175 primarily for the newly issued 5.00% Senior Notes, Series 2010A, in October of 2010. The average interest rate on the lines of credit was 1.54% for 2010 compared to 1.41% for 2009. The average debt outstanding under the lines of credit was \$7,191 for 2010 and \$16,848 for 2009. Interest expense is expected to increase due to the long-term debt issued in October.

Allowance for funds used during construction decreased \$99, from \$210 for 2009 to \$111 in 2010, due to a lower volume of eligible construction. Eligible 2009 construction expenditures included a main extension to West Manheim Township. Allowance for funds used during construction is expected to remain consistent in 2011 with the 2010 level based on a projected comparable amount of construction expenditures.

Other income (expenses), net for 2010 reflects decreased expenses of \$52 as compared to 2009. The decrease was primarily due to lower employee retirement expense.

Income taxes for 2010 increased by \$999, or 21.8%, compared to 2009, primarily due to an increase in taxable income. The Company's effective tax rate was 38.5% in 2010 and 37.9% in 2009.

2009 COMPARED WITH 2008

Net income for 2009 was \$7,512, an increase of \$1,081, or 16.8%, from net income of \$6,431 for 2008. The primary contributing factors to the increase in net income were higher water revenues which were partially offset by increased depreciation, higher pension cost, reduced interest capitalized, increased interest expense on debt and higher salary and wage expense.

Water operating revenues for the year increased \$4,205, or 12.8%, from \$32,838 for 2008 to \$37,043 for 2009. The primary reasons for the increase in revenues were a rate increase of 17.9% effective October 9, 2008 and growth in the customer base. The average number of customers served in 2009 increased as compared to 2008 by 2,414 customers, from 59,483 to 61,897 customers. Approximately 2,050 of the additional customers were due to the Asbury Pointe and West Manheim acquisitions. Despite this increase in customers, the total per capita volume of water sold in 2009 decreased compared to 2008 by approximately 5.7%. The largest decline occurred in the industrial category followed by the commercial and residential categories.

Operating expenses for the year increased \$1,497, or 8.2%, from \$18,158 for 2008 to \$19,655 for 2009. The increase was primarily due to higher depreciation of \$790 due to increased plant investment, increased pension expense of \$487, higher salary and wage expense of \$229 due mainly to the increased vacation accrual discussed in Note 1 (Reclassifications) to the Company's financial statements included herein and higher distribution system maintenance expense, chemical expense, power costs, rate case expense, provision for doubtful accounts, banking fees, realty taxes and other expenses aggregating approximately \$482. The increase was partially offset by reduced health insurance costs, increased capitalized overhead, lower transportation expenses and reduced software support and legal expenses aggregating approximately \$491.

Management's Discussion & Analysis of Financial Condition & Results of Operations

(In thousands of dollars, except per share amounts)

RESULTS OF OPERATIONS (CONTINUED)

Interest on debt for 2009 increased \$231, or 4.9%, from \$4,759 for 2008 to \$4,990 for 2009. Interest on the Company's long-term debt increased by \$706 due to an increase in the amount of long-term debt outstanding from new debt issued on October 15, 2008 in the aggregate principal amount of \$15,000 at an interest rate of 6%. The increased expenses were partially offset by lower interest on the \$12,000 variable rate bonds of approximately \$69 due to lower variable interest rates. Interest on the Company's lines of credit decreased by \$346 due to lower interest rates. The average interest rate on the lines of credit was 1.41% for 2009 compared to 3.61% for 2008. The average debt outstanding under the lines of credit was \$16,848 for 2009 and \$16,128 for 2008. Other long-term interest decreased \$60.

Allowance for funds used during construction decreased \$437, from \$647 for 2008 to \$210 in 2009, due to a lower volume of eligible construction. Eligible 2008 construction expenditures included an investment in a large water treatment replacement and expansion project and a main extension to West Manheim Township that was placed in service in December, 2008.

Other income (expenses), net for 2009 reflects increased expenses of \$8 as compared to 2008. The increase was primarily due to increased charitable contributions, higher debt cost amortization and other expenses which were partially offset by reduced retirement expenses.

Income taxes for 2009 increased by \$951, or 26.2%, compared to 2008, primarily due to an increase in taxable income. The Company's effective tax rate was 37.9% in 2009 and 36.1% in 2008. The increase in the effective tax rate was due to taxable gains on the surrender of life insurance policies and bonus depreciation initially being taxable for state tax purposes.

RATE DEVELOPMENTS

From time to time, the Company files applications for rate increases with the PPUC and is granted rate relief as a result of such requests. These rate increases are designed to cover operating expenses, taxes, interest on debt used to finance capital investments and a return on equity. The most recent rate request was filed by the Company on May 14, 2010 and sought an increase of \$6,220, which would have represented a 15.9% increase in rates. Effective November 4, 2010, the PPUC authorized an average increase of 8.7% in rates designed to produce approximately \$3,400 in additional annual revenues. The Company does not expect to file a base rate increase request in 2011.

ACQUISITIONS

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

CAPITAL EXPENDITURES

During 2010, the Company invested \$10,541 in construction expenditures including routine items, upgrades to its water treatment facilities, backup generators at various booster stations, reinforcing water mains, and various replacements of aging infrastructure. The Company replaced and relined over 37,000 feet of main in 2010. The Company was able to fund operating activities and construction expenditures using internally-generated funds, borrowings against the Company's lines of credit, proceeds from a long-term debt issue, proceeds from its stock purchase plans (see Note 5 to the Company's financial statements included herein), customer advances and the DSIC allowed by the PPUC.

The Company anticipates construction and acquisition expenditures for 2011 and 2012 of approximately \$12,800 and \$13,415, respectively. In addition to routine transmission and distribution projects, a portion of the anticipated 2011 and 2012 expenditures will be for additional main extensions, further upgrades to water treatment facilities, reinforcement of one of

Management's Discussion & Analysis of Financial Condition & Results of Operations

(In thousands of dollars, except per share amounts)

our dams, and various replacements of aging infrastructure including a standpipe. The Company intends to use internally-generated funds for at least half of our anticipated 2011 and 2012 construction and fund the remainder through line of credit borrowings, proceeds from our stock purchase plans, potential debt and equity offerings, the DSIC and customer advances and contributions (see Note 1 to the Company's financial statements included herein). Customer advances and contributions are expected to account for approximately 8% of funding requirements in 2011 and 15% of funding requirements in 2012. We believe we will have adequate access to the capital markets, if necessary during 2011, to fund anticipated construction and acquisition expenditures.

LIQUIDITY AND CAPITAL RESOURCES**Cash**

Although the Company is able to generate funds internally through customer bill payments, we have not historically maintained cash on the balance sheet. The Company manages its cash through a cash management account that is directly connected to a line of credit. Excess cash generated automatically pays down outstanding borrowings under the line of credit arrangement. If there are no outstanding borrowings, the cash is automatically invested in an interest-bearing account overnight. Likewise, if additional funds are needed, besides what is generated internally, for payroll, to pay suppliers, or to pay debt service, funds are automatically borrowed under the line of credit. The cash management facility has historically provided the necessary liquidity and funding for our operations and we expect that to continue to be the case for the foreseeable future. The cash balance of \$1,327 at December 31, 2010 represents the proceeds of the October long-term debt issue that were not utilized until 2011.

Accounts Receivable

Historically the Company has seen an upward trend in its accounts receivable balance. This trend is generally a result of increased revenues. Increases in accounts receivable have corresponded with increases in revenue. Recently the Company has noticed a decline in the timeliness of payments by its customers resulting in an increase in accounts receivable in excess of the increase in revenues. Despite this trend of slower payments, the Company has not seen a dramatic deterioration of its accounts receivable aging or the amount of uncollectible accounts written off. The Company has increased its allowance for doubtful accounts in consideration of this trend. If this trend continues, the Company may incur additional expenses for uncollectible accounts and see a reduction in its internally-generated funds.

Internally-generated Funds

The amount of internally-generated funds available for operations and construction depends on our ability to obtain timely and adequate rate relief, our customers' water usage, weather conditions, customer growth and controlled expenses. In 2010, we generated \$14,755 internally as compared to \$15,801 in 2009 and \$11,527 in 2008. An increase in net income was offset by higher accounts receivable and an increase in income taxes paid resulting in lower cash flow from operating activities during 2010. In addition to internally-generated funds, we used our bank lines of credit and proceeds from a long-term debt issue to help fund operations and construction.

Credit Lines

Historically, the Company has borrowed \$15,000 to \$20,000 under its lines of credit before refinancing with long-term debt or equity capital. As of December 31, 2010, the Company maintained unsecured lines of credit aggregating \$33,000 with three banks. One line of credit includes a \$4,000 portion which is payable upon demand and carries an interest rate of LIBOR plus 2.00%, and a \$13,000 committed portion with a revolving 2-year maturity (currently May 2012), which carries an interest rate of LIBOR plus 2.00%. The Company had no outstanding borrowings under the committed portion and no on-demand borrowings under this line of credit as of December 31, 2010. The second line of credit, in the amount of \$11,000, is a committed line of credit, which matures in May 2012 and carries an interest rate of LIBOR plus 1.50%. This line of credit has a compensating balance requirement of \$500. The Company had no outstanding borrowings under this line of credit as of December 31, 2010. The third line of credit, in the amount of \$5,000, is a committed line of credit, which matures in June 2011

Management's Discussion & Analysis of Financial Condition & Results of Operations

(In thousands of dollars, except per share amounts)

LIQUIDITY AND CAPITAL RESOURCES (CONTINUED)

and carries an interest rate of LIBOR plus 2.00%. The Company had no outstanding borrowings under this line of credit as of December 31, 2010. The Company plans to renew the line of credit that expires in 2011 under similar terms and conditions.

The credit and liquidity crisis which began in 2008 has caused substantial volatility and uncertainty in the capital markets and in the banking industry resulting in increased borrowing costs and reduced credit availability. While actual interest rates are currently low, one of our banks increased the interest rate on our line of credit from LIBOR plus 70 basis points to LIBOR plus 200 basis points in 2009. The higher interest rate remains in effect. One of the lines of credit also carries a commitment fee. Although we have taken steps to manage the risk of reduced credit availability such as maintaining primarily committed lines of credit that cannot be called on demand and obtaining a 2-year revolving maturity, there is no guarantee that we will be able to obtain sufficient lines of credit with favorable terms in the future. In addition, if the Company is unable to refinance our line of credit borrowings with long-term debt or equity when necessary, we may have to eliminate or postpone capital expenditures. The Company was able to pay off its line of credit borrowings by issuing long-term debt in October 2010. We believe we will have adequate capacity under our current lines of credit to meet our financing needs throughout 2011.

Long-term Debt

The Company's loan agreements contain various covenants and restrictions. We believe we are currently in compliance with all of these restrictions. See Note 4 to the Company's financial statements included herein for additional information regarding these restrictions.

The 3.75% Industrial Development Authority Revenue Refunding Bonds, Series 1995, had a mandatory tender date of June 1, 2010. The Company retired the \$4,300 bonds using funds available under its lines of credit.

On October 8, 2010, the Company issued \$15,000 aggregate principal amount of 5.00% Monthly Senior Notes Series 2010A due October 1, 2040 (the "Senior Notes") pursuant to the terms of an indenture, as supplemented by a first supplemental indenture, each dated as of October 1, 2010, between the Company and Manufacturers and Traders Trust Company, as trustee. The Senior Notes bear interest at a rate of 5.00% payable monthly with a maturity date of October 1, 2040. The Senior Notes are direct, unsecured and unsubordinated obligations of the Company. The Company received net proceeds, after deducting issuance costs, of approximately \$14,300. The net proceeds were used to pay off the Company's line of credit borrowings incurred for capital expenditures and acquisitions, to retire maturing long-term debt issues, and for general corporate purposes. The Senior Notes are subject to redemption at the direction of the Company, in whole or in part, at any time on or after October 1, 2015.

The Company's debt (long-term debt plus current portion of long-term debt) as a percentage of the total capitalization, defined as total common stockholders' equity plus long-term debt (including current portion of long-term debt), was 48.3% as of December 31, 2010, compared with 47.2% as of December 31, 2009. As our debt load trends upward in the future, we will likely match increasing debt with increasing equity so that our debt to total capitalization ratio remains at nearly fifty percent. This capital structure has historically been acceptable to the PPUC in that prudent debt costs and a fair return have been granted by the PPUC in rate filings. See Note 4 to the Company's financial statements included herein for the details of our long-term debt outstanding as of December 31, 2010.

The Company has an effective "shelf" Registration Statement on Form S-3 on file with the Securities and Exchange Commission (SEC), pursuant to which the Company may offer an aggregate remaining amount of up to \$25,000 of its common stock or debt securities subject to market conditions at the time of any such offering.

Management's Discussion & Analysis of Financial Condition & Results of Operations

(In thousands of dollars, except per share amounts)

Deferred Income Taxes

The Company has seen an increase in its deferred income tax liability amounts over the last several years. This is primarily a result of the accelerated and bonus depreciation deduction available for federal tax purposes which creates differences between book and tax depreciation expense. We expect this trend to continue as we make significant investments in capital expenditures and as the tax code continues to extend bonus depreciation. Despite having a significant deferred income tax asset balance, the Company does not believe a valuation allowance is required due to the expected generation of future taxable income during the periods in which those temporary differences become deductible. The Company has determined there are no uncertain tax positions that require recognition as of December 31, 2010.

Common Stock

Common stockholders' equity as a percent of the total capitalization was 51.7% as of December 31, 2010, compared with 52.8% as of December 31, 2009. It is the Company's intent to maintain a ratio near fifty percent. The 2009 common stock offering improved our ratio substantially. Under the Registration Statement previously mentioned, we have the ability to issue additional shares of the Company's common stock, subject to market conditions at the time of any such offering.

Credit Rating

Our ability to maintain our credit rating depends, among other things, on adequate and timely rate relief, which we have been successful in obtaining, and our ability to fund capital expenditures in a balanced manner using both debt and equity. In 2011, our objectives will be to continue to maximize our funds provided by operations and maintain the equity component of total capitalization.

DIVIDENDS

During 2010, the Company's dividend payout ratios relative to net income and cash provided by operating activities were 72.9% and 43.8%, respectively. During 2009, the Company's dividend payout ratios relative to net income and cash provided by operating activities were 80.5% and 37.0%, respectively. During the fourth quarter of 2010, the Board of Directors increased the dividend by 2.3% from \$0.128 per share to \$0.131 per share per quarter. This was the fourteenth consecutive annual dividend increase and the 195th consecutive year of paying dividends.

The Company's Board of Directors declared a dividend in the amount of \$0.131 per share at its January 2011 meeting. The dividend is payable on April 15, 2011 to shareholders of record as of February 28, 2011. While the Company expects to maintain this dividend amount in 2011, future dividends will be dependent upon the Company's earnings, financial condition, capital demands and other factors and will be determined by the Company's Board of Directors. See Note 4 to the Company's financial statements included herein for restrictions on dividend payments.

INFLATION

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

Management's Discussion & Analysis of Financial Condition & Results of Operations

(In thousands of dollars, except per share amounts)

CONTRACTUAL OBLIGATIONS

The following summarizes the Company's contractual obligations by period as of December 31, 2010:

	Payments Due by Period						
	Total	2011	2012	2013	2014	2015	Thereafter
Long-term debt obligations (a)	\$ 85,173	\$ 41	\$ 12,042	\$ 42	\$ 43	\$ 43	\$ 72,962
Interest on long-term debt (b)	84,863	4,871	4,870	4,870	4,869	4,869	60,514
Purchase obligations (c)	1,053	1,053	—	—	—	—	—
Defined benefit obligations (d)	3,186	1,593	1,593	—	—	—	—
Deferred employee benefits (e)	4,629	225	239	230	241	240	3,454
Other deferred credits (f)	1,601	351	307	226	157	103	457
Total	\$ 180,505	\$ 8,134	\$ 19,051	\$ 5,368	\$ 5,310	\$ 5,255	\$ 137,387

- (a) Represents debt maturities including current maturities. Included in the table is a payment of \$12,000 in 2012 on the variable rate bonds which would only be due if the bonds were unable to be remarketed. There is currently no such indication of this happening.
- (b) Excludes interest on the \$12,000 variable rate debt as these payments cannot be reasonably estimated. The interest rate on this issue is reset weekly by the remarketing agent based on then current market conditions. Also excludes interest on the committed line of credit due to the variability of both the outstanding amount and the interest rate.
- (c) Represents an approximation of open purchase orders at year end.
- (d) Represents contributions expected to be made to qualified defined benefit plans. The contribution may increase if the minimum required contribution as calculated under Employee Retirement Income Security Act (ERISA) standards is higher than these amounts but in no case will the amount be less. The amount of required contributions in 2013 and thereafter is not currently determinable.
- (e) Represents the obligations under the Company's Supplemental Retirement and Deferred Compensation Plans for executives.
- (f) Represents the estimated settlement payments to be made under the Company's interest rate swap contract.

In addition to these obligations, the Company makes refunds on Customers' Advances for Construction over a specific period of time based on operating revenues related to developer-installed water mains or as new customers are connected to and take service from such mains. The refund amounts are not included in the above table because the timing cannot be accurately estimated. Portions of these refund amounts are payable annually through 2021 and amounts not paid by the contract expiration dates become non-refundable and are transferred to Contributions in Aid of Construction.

See Note 9 to the Company's financial statements included herein for a discussion of our commitments.

CRITICAL ACCOUNTING ESTIMATES

The methods, estimates and judgments we use in applying our accounting policies have a significant impact on the results we report in our financial statements. Our accounting policies require us to make subjective judgments because of the need to make estimates of matters that are inherently uncertain. Our most critical accounting estimates include: regulatory assets and liabilities, revenue recognition and accounting for our pension plans.

Regulatory Assets and Liabilities

Generally accepted accounting principles define professional standards for companies whose rates are established by or are subject to approval by an independent third-party regulator. In accordance with the professional standards, the Company defers costs and credits on its balance sheet as regulatory assets and liabilities when it is probable that these costs and credits will be recognized in the rate-making process in a period different from when the costs and credits were incurred.

Management's Discussion & Analysis of Financial Condition & Results of Operations

(In thousands of dollars, except per share amounts)

These deferred amounts are then recognized in the statement of income in the period in which they are reflected in customer rates. If the Company later finds that these assets and liabilities cannot be included in rate-making, they are adjusted appropriately. See Note 1 for additional details regarding regulatory assets and liabilities.

Revenue Recognition

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

Pension Accounting

Accounting for defined benefit pension plans requires estimates of future compensation increases, mortality, the discount rate, and expected return on plan assets as well as other variables. These variables are reviewed annually with the Company's pension actuary. The Company selected its December 31, 2010 and 2009 discount rates based on the Citigroup Pension Liability Index. This index uses the Citigroup spot rates for durations out to 30 years and matches them to expected disbursements from the plan over the long term. The Company believes this index most appropriately matches its pension obligations. The present values of the Company's future pension obligations were determined using a discount rate of 5.35% at December 31, 2010 and 6.0% at December 31, 2009.

Choosing a lower discount rate normally increases the amount of pension expense and the corresponding liability. In the case of the Company, a reduction in the discount rate would increase its liability, but would not have an impact on its pension expense. The PPUC, in a previous rate settlement, agreed to grant recovery of the Company's contribution to the pension plans in customer rates. As a result, under the professional standards, expense in excess of the Company's pension plan contribution is deferred as a regulatory asset and will be expensed as contributions are made to the plans and the contributions are recovered in customer rates. Therefore, changes in the discount rate affect regulatory assets rather than pension expense.

The Company's estimate of the expected return on plan assets is primarily based on the historic returns and projected future returns of the asset classes represented in its plans. The target allocation of pension assets is 50% to 70% equity securities, 30% to 50% debt securities, and 0% to 10% reserves. The Company used 7% as its estimate of expected return on assets in both 2010 and 2009. If the Company were to reduce the expected return, its liability would increase, but its expense would again remain unchanged because the expense is equal to the Company's contribution to the plans. The additional expense would instead be recorded as an increase to regulatory assets.

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

OFF-BALANCE SHEET TRANSACTIONS

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

IMPACT OF RECENT ACCOUNTING PRONOUNCEMENTS

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

Management's Report on Internal Control Over Financial Reporting

Management of The York Water Company (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 pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

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

Management evaluated the Company's internal control over financial reporting as of December 31, 2010. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in *Internal Control—Integrated Framework* (COSO). As a result of this assessment and based on the criteria in the COSO framework, management has concluded that, as of December 31, 2010, the Company's internal control over financial reporting was effective.

The Company's independent auditors, ParenteBeard LLC, have audited the Company's internal control over financial reporting. Their opinions on the Company's internal control over financial reporting and on the Company's financial statements appear on the following pages of this annual report.



Jeffrey R. Hines
President, Chief Executive Officer



Kathleen M. Miller
Chief Financial Officer

March 8, 2011

Report of Independent Registered Public Accounting Firm

TO THE BOARD OF DIRECTORS AND STOCKHOLDERS
OF THE YORK WATER COMPANY

We have audited The York Water Company's (the "Company") internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The York Water 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, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit 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. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

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 accounting principles generally accepted in the United States of America. 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 our opinion, The York Water Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the balance sheets and the related statements of income, common stockholders' equity and comprehensive income, and cash flows of The York Water Company, and our report dated March 8, 2011 expressed an unqualified opinion.



ParenteBeard LLC
York, Pennsylvania
March 8, 2011

Report of Independent Registered Public Accounting Firm

TO THE BOARD OF DIRECTORS AND STOCKHOLDERS
OF THE YORK WATER COMPANY

We have audited the accompanying balance sheets of The York Water Company (the "Company") as of December 31, 2010 and 2009, and the related statements of income, common stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2010. 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 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The York Water Company as of December 31, 2010 and 2009, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2010 in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), The York Water Company's internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 8, 2011 expressed an unqualified opinion.



ParenteBeard LLC
York, Pennsylvania
March 8, 2011

Balance Sheets

(In thousands of dollars, except per share amounts)

ASSETS	December 31	
	2010	2009
Utility Plant , at original cost	\$ 272,565	\$ 262,598
Plant acquisition adjustments	(2,709)	(2,759)
Accumulated depreciation	(42,179)	(38,364)
Net utility plant	227,677	221,475
Other Physical Property:		
Net of accumulated depreciation of \$190 in 2010 and \$175 in 2009	712	554
Current Assets:		
Cash and cash equivalents	1,327	—
Restricted cash-compensating balance	—	500
Accounts receivable, net of reserves of \$245 in 2010 and \$225 in 2009	3,769	2,938
Unbilled revenues	2,503	2,451
Recoverable income taxes	21	—
Materials and supplies inventories, at cost	608	716
Prepaid expenses	398	387
Deferred income taxes	167	154
Total current assets	8,793	7,146
Other Long-Term Assets:		
Deferred debt expense	2,501	1,906
Notes receivable	407	476
Deferred regulatory assets	15,821	14,010
Restricted cash-compensating balance	500	—
Other assets	3,520	3,270
Total other long-term assets	22,749	19,662
Total Assets	\$ 259,931	\$ 248,837

STOCKHOLDERS' EQUITY AND LIABILITIES

Common Stockholders' Equity:

Common stock, no par value, authorized 46,500,000 shares, issued and outstanding 12,692,054 shares in 2010 and 12,558,724 shares in 2009	\$ 75,481	\$ 73,569
Retained earnings	15,776	13,353
Total common stockholders' equity	91,257	86,922

Preferred Stock , authorized 500,000 shares, no shares issued	—	—
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Long-term Debt , excluding current portion	85,132	73,227
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Commitments	—	—
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Current Liabilities:

Short-term borrowings	—	5,000
Current portion of long-term debt	41	4,341
Accounts payable	1,245	892
Dividends payable	1,440	1,393
Accrued taxes	19	488
Accrued interest	1,068	1,019
Other accrued expenses	1,518	1,472
Total current liabilities	5,331	14,605

Deferred Credits:

Customers' advances for construction	15,031	16,188
Deferred income taxes	25,437	22,507
Deferred employee benefits	9,814	8,765
Other deferred credits	2,003	1,679
Total deferred credits	52,285	49,139
Contributions in aid of construction	25,926	24,944

Total Stockholders' Equity and Liabilities

\$ 259,931	\$ 248,837
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The accompanying notes are an integral part of these statements.

Statements of Income

(In thousands of dollars, except per share amounts)

	2010	Year Ended December 31 2009	2008
Water Operating Revenues:			
Residential	\$ 24,478	\$ 23,299	\$ 20,572
Commercial and industrial	11,440	10,734	9,671
Other	3,087	3,010	2,595
	<u>39,005</u>	<u>37,043</u>	<u>32,838</u>
Operating Expenses:			
Operation and maintenance	6,760	7,067	6,749
Administrative and general	6,725	7,101	6,685
Depreciation and amortization	4,592	4,412	3,622
Taxes other than income taxes	1,161	1,075	1,102
	<u>19,238</u>	<u>19,655</u>	<u>18,158</u>
Operating income	<u>19,767</u>	<u>17,388</u>	<u>14,680</u>
Other Income (Expenses):			
Interest on debt	(4,906)	(4,990)	(4,759)
Allowance for funds used during construction	111	210	647
Other income (expenses), net	(465)	(517)	(509)
	<u>(5,260)</u>	<u>(5,297)</u>	<u>(4,621)</u>
Income before income taxes	14,507	12,091	10,059
Income taxes	<u>5,578</u>	<u>4,579</u>	<u>3,628</u>
Net Income	<u>\$ 8,929</u>	<u>\$ 7,512</u>	<u>\$ 6,431</u>
Basic Earnings Per Share	<u>\$ 0.71</u>	<u>\$ 0.64</u>	<u>\$ 0.57</u>
Cash Dividends Declared Per Share	<u>\$ 0.515</u>	<u>\$ 0.506</u>	<u>\$ 0.489</u>

The accompanying notes are an integral part of these statements.

Statements of Common Stockholders' Equity and Comprehensive Income

For the Years Ended December 31, 2010, 2009 and 2008
(In thousands of dollars, except per share amounts)

	Common Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance, December 31, 2007	\$ 56,566	\$ 10,986	\$ (280)	\$ 67,272
Net income	—	6,431	—	6,431
Other comprehensive income :				
Reclassification adjustment for unrealized loss on interest rate swap to regulatory asset, net of \$191 income tax	—	—	280	280
Comprehensive income				6,711
Dividends (\$0.489 per share)	—	(5,526)	—	(5,526)
Issuance of common stock under dividend reinvestment, direct stock and employee stock purchase plans	1,309	—	—	1,309
Balance, December 31, 2008	57,875	11,891	—	69,766
Net income	—	7,512	—	7,512
Dividends (\$0.506 per share)	—	(6,050)	—	(6,050)
Issuance of 1,070,000 shares of common stock	14,094	—	—	14,094
Issuance of common stock under dividend reinvestment, direct stock and employee stock purchase plans	1,600	—	—	1,600
Balance, December 31, 2009	73,569	13,353	—	86,922
Net income	—	8,929	—	8,929
Dividends (\$0.515 per share)	—	(6,506)	—	(6,506)
Issuance of common stock under dividend reinvestment, direct stock and employee stock purchase plans	1,912	—	—	1,912
Balance, December 31, 2010	\$ 75,481	\$ 15,776	\$ —	\$ 91,257

The accompanying notes are an integral part of these statements.

Statements of Cash Flows

(In thousands of dollars, except per share amounts)

	2010	Year Ended December 31 2009	2008
Cash Flows from Operating Activities:			
Net income.....	\$ 8,929	\$ 7,512	\$ 6,431
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization.....	4,592	4,412	3,622
Increase in deferred income taxes	2,591	2,515	1,911
Other	99	39	(166)
Changes in assets and liabilities:			
(Increase) decrease in accounts receivable, unbilled revenues and recoverable income taxes	(1,127)	440	(816)
Decrease in materials and supplies and prepaid expenses.....	97	50	105
Increase in accounts payable, accrued expenses, regulatory and other liabilities, and deferred employee benefits and credits	705	666	870
Increase (decrease) in accrued interest and taxes	(420)	352	221
Increase in regulatory and other assets.....	(711)	(185)	(651)
Net cash provided by operating activities.....	14,755	15,801	11,527
Cash Flows from Investing Activities:			
Utility plant additions, including debt portion of allowance for funds used during construction of \$62 in 2010, \$117 in 2009 and \$427 in 2008.....	(10,541)	(12,535)	(24,438)
Acquisitions of water systems	—	(2,236)	(259)
Increase in compensating balance.....	—	(500)	—
Decrease in notes receivable.....	69	60	74
Net cash used in investing activities.....	(10,472)	(15,211)	(24,623)
Cash Flows from Financing Activities:			
Customers' advances for construction and contributions in aid of construction	428	443	804
Repayments of customer advances.....	(544)	(926)	(1,489)
Proceeds of long-term debt issues.....	39,491	23,659	52,308
Debt issuance costs.....	(703)	—	(950)
Repayments of long-term debt.....	(34,886)	(32,444)	(36,460)
Borrowings (repayments) under short-term line of credit agreements....	(2,000)	(1,000)	3,000
Changes in cash overdraft position	(195)	(167)	34
Issuance of common stock.....	1,912	15,694	1,309
Dividends paid.....	(6,459)	(5,849)	(5,460)
Net cash (used in) provided by financing activities	(2,956)	(590)	13,096
Net change in cash and cash equivalents	1,327	—	—
Cash and cash equivalents at beginning of year	—	—	—
Cash and cash equivalents at end of year	\$ 1,327	\$ —	\$ —
Supplemental disclosures of cash flow information:			
Cash paid during the year for:			
Interest, net of amounts capitalized	\$ 4,797	\$ 4,911	\$ 4,200
Income taxes.....	3,513	1,284	1,611
Supplemental schedule of non-cash investing and financing activities:			
Accounts payable includes \$726 in 2010, \$292 in 2009 and \$950 in 2008 for the construction of utility plant.			
Accounts payable and other deferred credits includes \$19 in 2009 and \$93 in 2008 for the acquisition of water systems.			
Contributions in aid of construction includes \$51 of contributed land in 2008.			
Short-term line of credit borrowings amounting to \$3,000 were reclassified as long-term borrowings in 2010.			

The accompanying notes are an integral part of these statements.

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

1. SIGNIFICANT ACCOUNTING POLICIES

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

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

Utility Plant and Depreciation

The cost of additions includes contracted cost, direct labor and fringe benefits, materials, overhead and, for certain utility plant, allowance for funds used during construction. In accordance with regulatory accounting requirements, water 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, 2010 and 2009, utility plant includes a credit acquisition adjustment of \$2,709 and \$2,759, respectively. The net acquisition adjustment is being amortized over the remaining life of the respective assets. Amortization amounted to \$50 in 2010, \$49 in 2009, and \$27 in 2008.

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

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

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

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The following remaining lives are used for financial reporting purposes:

Utility Plant Asset Category	2010	December 31, 2009	Approximate range of remaining lives
Mains and accessories.....	\$ 142,162	\$ 138,738	12-85 yrs
Services, meters and hydrants.....	54,970	53,195	21-53 yrs
Operations structures, reservoirs and water tanks.....	40,387	39,928	8-64 yrs
Pumping and purification equipment	20,563	16,167	6-25 yrs
Office, transportation and operating equipment	9,424	9,212	3-23 yrs
Land and other non-depreciable assets.....	2,973	2,963	—
Utility plant in service.....	270,479	260,203	
Construction work in progress.....	2,086	2,395	—
Total Utility Plant.....	<u>\$ 272,565</u>	<u>\$ 262,598</u>	

The effective rate of depreciation was 2.06% in 2010, 2.10% in 2009, and 1.94% in 2008 on average utility plant, net of customers' advances and contributions. Larger depreciation provisions resulting from allowable accelerated methods are deducted for tax purposes.

Accounts Receivable

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

Revenues

Revenues include amounts billed to customers on a cycle basis and unbilled amounts based on actual and estimated usage from the latest meter reading to the end of the accounting period.

Deferred Debt Expense

Deferred debt expense is amortized on a straight-line basis over the term of the related debt.

Notes Receivable

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

Regulatory Assets and Liabilities

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

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

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

Regulatory assets and liabilities are comprised of the following:

	2010	December 31, 2009	Remaining Recovery Periods
Assets			
Income taxes	\$ 4,008	\$ 3,706	Various
Postretirement benefits	9,454	8,632	10-20 years
Unrealized swap losses	1,310	949	1-19 years
Utility plant retirement costs	843	600	5 years
Rate case filing expenses	206	123	2 years
	<u>\$ 15,821</u>	<u>\$ 14,010</u>	
Liabilities			
Income taxes	<u>\$ 830</u>	<u>\$ 853</u>	1-50 years

Certain items giving rise to deferred state income taxes, as well as a portion of deferred federal income taxes related primarily to differences between book and tax depreciation expense, are recognized for ratemaking purposes on a cash or flow-through basis and will be recovered in rates as they reverse.

Postretirement benefits include (a) deferred pension expense in excess of contributions made to the plans, and (b) the underfunded status of the pension plans. The underfunded status represents the excess of the projected benefit obligation over the fair market value of the assets. Both are expected to be recovered in future years as additional contributions are made. The recovery period is dependent on contributions made to the plans, plan asset performance and the discount rate used to value the obligations. The period is estimated at between 10 and 20 years.

Beginning October 1, 2008, the Company began using regulatory accounting treatment to defer the mark-to-market unrealized gains and losses on its interest rate swap to reflect that the gain or loss is included in the ratemaking formula when the transaction actually settles. The value of the swap as of the balance sheet date is recorded as part of other deferred credits. Realized gains or losses on the swap will be recorded as interest expense in the statement of income over its remaining life of 19 years.

The regulatory asset for utility plant retirement costs, including cost of removal, represents costs already incurred which are expected to be recovered over a five-year period in rates, through depreciation expense. Rate case filing expenses are deferred and amortized over a period of two years.

Regulatory liabilities relate mainly to deferred investment tax credits, and additionally to deferred taxes related to postretirement death benefits and bad debts. These liabilities will be given back to customers in rates as tax deductions occur over the next 1-50 years. Regulatory liabilities are part of other accrued expenses and other deferred credits on the balance sheets.

Materials and Supplies Inventories

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

Other Assets

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

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Customers' Advances for Construction

Customer advances are cash payments from developers, municipalities, customers or builders for construction of utility plant, and are refundable upon completion of construction, as operating revenues are earned. If the Company loaned funds for construction to the customer, the refund amount is credited to the note receivable rather than paid out in cash. After all refunds to which the customer is entitled are made, any remaining balance is transferred to contributions in aid of construction. From 1986 to 1996 when customer advances were taxable income to the Company, additional funds were collected from customers to cover the taxes. Those funds were recorded as a liability within Customer Advances and are being amortized as deferred income over the tax life of the underlying assets.

Contributions in Aid of Construction

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

Comprehensive Income

Accounting principles generally accepted in the United States of America require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on interest rate swaps, are usually reported as a separate component of the equity section of the balance sheet, such items, along with net income, are components of comprehensive income. Since October 1, 2008, the Company has used regulatory accounting for its unrealized gains and losses on its interest rate swap, and will no longer report comprehensive income for this item in the future.

Interest Rate Swap Agreement

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

The professional standards regarding accounting for derivatives and hedging activities requires companies to recognize all derivative instruments as either assets or liabilities at fair value on the balance sheet. In accordance with the standards, the interest rate swap is recorded on the balance sheet in other deferred credits at fair value. Prior to October 1, 2008, the Company used hedge accounting to record its swap transactions. The effective portion of the gain or loss on a derivative designated and qualifying as a cash flow hedging instrument was initially reported as a component of other comprehensive income and subsequently reclassified into earnings as interest expense in the same period or periods during which the hedged transaction affected earnings. The ineffective portion of the gain or loss on the derivative instrument was recognized in earnings.

The Company began using regulatory accounting treatment rather than hedge accounting to defer the unrealized gains and losses on its interest rate swap on October 1, 2008. Instead of the effective portion being recorded as other comprehensive income and the ineffective portion being recognized in earnings, the entire unrealized swap value is now recorded as a regulatory asset. Based on current ratemaking treatment, the Company expects the gains and losses to be recognized in rates and in interest

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

expense as the swap settlements occur. Swap settlements are recorded in the income statement with the hedged item as interest expense. During the year ended December 31, 2010, \$360 was reclassified from regulatory assets to interest expense as a result of swap settlements. The overall swap result was a loss of \$722 for the year ended December 31, 2010. During the twelve months ending December 31, 2011, the Company expects to reclassify \$351 (before tax) from regulatory assets to interest expense.

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

Income Taxes

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

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

Investment tax credits have been deferred and are being amortized to income over the average estimated service lives of the related assets. As of December 31, 2010 and 2009, deferred investment tax credits amounted to \$890 and \$928, respectively.

Allowance for Funds Used During Construction

Allowance for funds used during construction (AFUDC) represents the estimated cost of funds used for construction purposes during the period of construction. These costs are reflected as non-cash income during the construction period and as an addition to the cost of plant constructed. AFUDC includes the net cost of borrowed funds and a rate of return on other funds. The PPUC approved rate of 10.04% was applied for 2010 and 2009. We applied a blended rate in 2008 due to our partial use of tax-exempt financing for 2008 construction projects. The tax-exempt borrowing rate of 6.00% was applied to those expenditures so financed, whereas the approved 10.04% rate was applied to the remainder of 2008 expenditures. AFUDC is recovered through water rates as utility plant is depreciated.

Cash and Cash Equivalents

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

The Company had a book overdraft of \$0 and \$195 at December 31, 2010 and 2009, respectively. The book overdraft represents outstanding checks and other items which had not cleared the bank as of the end of the period. The overdraft is included in accounts payable on the balance sheet and the change in overdraft position is recorded as a financing activity on the statement of cash flows.

Use of Estimates in the Preparation of Financial Statements

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

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Reclassifications

As discussed above, the Company changed the accounting treatment for its interest rate swap. For the nine months ended September 30, 2008, the Company accounted for the interest rate swap as a cash flow hedge. As of October 1, 2008, management assessed the probability of collecting the unrealized gain or loss value of the swap in rates as the Company is currently reflecting the realized gain or loss as a component of interest expense in the statement of income. This change in accounting treatment resulted in the reversal of \$224 of long-term interest expense, \$189 recorded in deferred income taxes and \$277 recorded in accumulated other comprehensive income as of September 30, 2008. Management determined that the amounts previously reported using the cash flow hedge method of accounting for each of the three quarters and periods ended March 31, 2008, June 30, 2008 and September 30, 2008 were not materially misstated.

During the first quarter of 2009, the Company determined that it had understated the amount of accrued vacation recorded in its financial statements. As a result, the Company recorded additional salary and wage expense of \$257 in accordance with the professional standards regarding accounting for compensated absences. The additional accrual, amounting to \$152 after taxes, represents an error correction from prior periods. Management determined that the financial statements as of and for the year ended December 31, 2008 were not materially misstated.

Impact of Recent Accounting Pronouncements

In November 2008, the Securities and Exchange Commission (SEC) released a proposed roadmap regarding the potential use by U.S. issuers of financial statements prepared in accordance with International Financial Reporting Standards (IFRS). IFRS is a comprehensive series of accounting standards published by the International Accounting Standards Board (IASB). In February 2010, the SEC expressed support for a single set of high-quality globally accepted accounting standards and established a work plan that sets forth specific areas and factors before transitioning to IFRS. The SEC will make a determination in 2011 regarding the mandatory adoption of IFRS with the expectation that any decision to adopt IFRS would allow issuers four to five years to prepare for the transition. The Company is currently assessing the impact that this potential change would have on its financial statements, and it will continue to monitor the development of the potential implementation of IFRS.

2. ACQUISITIONS

On November 24, 2008, the Company completed the acquisition of the water facilities of Asbury Pointe Water Company in York County, Pennsylvania. The Company acquired and is using Asbury Pointe's distribution system through an interconnection with its current distribution system. This acquisition resulted in the addition of approximately 250 customers and the purchase price was approximately \$242, which is less than the depreciated original cost of the assets. The Company recorded a negative acquisition adjustment of approximately \$207 as of December 31, 2008. Additional acquisition expenditures during the first quarter of 2009 of approximately \$22 resulted in a reduction of the negative acquisition adjustment to \$185. The Company is amortizing the negative acquisition adjustment over the remaining life of the underlying assets.

On January 9, 2009, the Company completed the acquisition of the water system of West Manheim Township in York County, Pennsylvania. The Company had begun serving the customers of West Manheim Township in December 2008 through an interconnection with its current distribution system. This acquisition resulted in the addition of 1,800 customers at a purchase price of approximately \$2,075, which is less than the depreciated original cost of the assets. The Company recorded a negative acquisition adjustment of approximately \$1,440 and is amortizing it over the remaining life of the underlying assets.

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

On November 12, 2009, the Company completed the acquisition of the water system of Beaver Creek Village in Adams County, Pennsylvania. The Company acquired and is using Beaver Creek Village's distribution facilities through an interconnection with its current distribution system. This acquisition resulted in the addition of 167 customers at a purchase price of approximately \$70, which is less than the depreciated original cost of the assets. The Company recorded a negative acquisition adjustment of approximately \$26 and is amortizing it over the remaining life of the underlying assets.

The Company began to include the operating results of the Asbury Pointe and Beaver Creek Village acquisitions in its operating results on the acquisition dates. The West Manheim acquisition was included in operating results prior to the closing date as indicated above. The results have been immaterial to total company results.

3. INCOME TAXES

The provisions for income taxes consist of:

	2010	2009	2008
Federal current	\$ 1,872	\$ 1,176	\$ 1,157
State current	1,115	888	559
Federal deferred	2,645	2,564	1,954
State deferred	(16)	(10)	(3)
Federal investment tax credit, net of current utilization	(38)	(39)	(39)
Total income taxes	<u>\$ 5,578</u>	<u>\$ 4,579</u>	<u>\$ 3,628</u>

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

	2010	2009	2008
Statutory Federal tax provision	\$ 4,933	\$ 4,111	\$ 3,420
State income taxes, net of Federal benefit	725	579	367
Tax-exempt interest	(37)	(39)	(39)
Amortization of investment tax credit	(38)	(39)	(39)
Cash value of life insurance	70	68	(29)
Domestic production deduction	(127)	(79)	(62)
Other, net	52	(22)	10
Total income taxes	<u>\$ 5,578</u>	<u>\$ 4,579</u>	<u>\$ 3,628</u>

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

3. INCOME TAXES (CONTINUED)

The tax effects of temporary differences between book and tax balances that give rise to significant portions of the deferred tax assets and deferred tax liabilities as of December 31, 2010 and 2009 are summarized in the following table:

	2010	2009
Deferred tax assets:		
Reserve for doubtful accounts	\$ 99	\$ 91
Compensated absences	188	166
Deferred compensation	1,091	995
Customers' advances and contributions	81	111
Deferred taxes associated with the gross-up of revenues necessary to return, in rates, the effect of temporary differences	90	89
Pensions	2,951	2,617
Costs deducted for book, not for tax	33	39
Total deferred tax assets	4,533	4,108
Deferred tax liabilities:		
Accelerated depreciation	23,673	20,801
Investment tax credit	529	551
Deferred taxes associated with the gross-up of revenues necessary to recover, in rates, the effect of temporary differences	1,379	1,247
Tax effect of pension regulatory asset	3,838	3,504
Costs deducted for tax, not for book	384	358
Total deferred tax liabilities	29,803	26,461
Net deferred tax liability	\$ 25,270	\$ 22,353
Reflected on balance sheets as:		
Current deferred tax asset	\$ (167)	\$ (154)
Noncurrent deferred tax liability	25,437	22,507
Net deferred tax liability	\$ 25,270	\$ 22,353

No valuation allowance is required for deferred tax assets as of December 31, 2010 and 2009. In assessing the soundness of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. Based upon the level of historical taxable income and the current regulatory environment, management believes it is more likely than not the Company will realize the benefits of these deductible differences.

The Company determined that there were no uncertain tax positions meeting the recognition and measurement test of the professional standards recorded in the years that remain open for review by taxing authorities. The federal income tax returns and the state income tax returns for the years 2007 through 2009 remain open. The Company has not yet filed tax returns for 2010, but has not taken any new positions in its 2010 income tax provision.

The Company's policy is to recognize interest and penalties related to income tax matters in other expenses. There were no interest or penalties for the years ended December 31, 2010, 2009 and 2008.

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

4. LONG-TERM DEBT AND SHORT-TERM BORROWINGS

Long-term debt as of December 31, 2010 and 2009 is summarized in the following table:

	2010	2009
3.75% Industrial Development Authority Revenue Refunding Bonds, Series 1995, due 2010.....	\$ —	\$ 4,300
4.05% Pennsylvania Economic Development Financing Authority Exempt Facilities Revenue Bonds, Series A, due 2016.....	2,350	2,350
5.00% Pennsylvania Economic Development Financing Authority Exempt Facilities Revenue Bonds, Series A, due 2016.....	4,950	4,950
10.17% Senior Notes, Series A, due 2019.....	6,000	6,000
9.60% Senior Notes, Series B, due 2019.....	5,000	5,000
1.00% Pennvest Loan, due 2019.....	373	414
10.05% Senior Notes, Series C, due 2020.....	6,500	6,500
8.43% Senior Notes, Series D, due 2022.....	7,500	7,500
Variable Rate Pennsylvania Economic Development Financing Authority Exempt Facilities Revenue Bonds, Series 2008A, due 2029.....	12,000	12,000
4.75% Industrial Development Authority Revenue Bonds, Series 2006, due 2036.....	10,500	10,500
6.00% Pennsylvania Economic Development Financing Authority Exempt Facilities Revenue Bonds, Series 2008B, due 2038.....	15,000	15,000
5.00% Monthly Senior Notes, Series 2010A, due 2040.....	15,000	—
Committed Lines of Credit, due 2012.....	—	3,054
Total long-term debt.....	85,173	77,568
Less current maturities.....	(41)	(4,341)
Long-term portion.....	\$ 85,132	\$ 73,227

Payments due by year:

2011	2012	2013	2014	2015
\$41	\$12,042	\$42	\$43	\$43

Payments due in 2012 include payments of \$12,000 on the variable rate bonds (due 2029) which would only be payable if all of the bonds were tendered and could not be remarketed. There is currently no such indication of this happening.

On October 8, 2010, the Company issued \$15,000 aggregate principal amount of 5.00% Monthly Senior Notes Series 2010A due October 1, 2040 (the “Senior Notes”) pursuant to the terms of an indenture, as supplemented by a first supplemental indenture, each dated as of October 1, 2010, between the Company and Manufacturers and Traders Trust Company, as trustee.

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

4. LONG-TERM DEBT AND SHORT-TERM BORROWINGS (CONTINUED)

The Senior Notes bear interest at a rate of 5.00% payable monthly with a maturity date of October 1, 2040. The Senior Notes are direct, unsecured and unsubordinated obligations of the Company. The Company received net proceeds, after deducting issuance costs, of approximately \$14,300. The net proceeds were used to pay off the Company's line of credit borrowings incurred for capital expenditures and acquisitions, to retire maturing long-term debt issues, and for general corporate purposes. The Senior Notes are subject to redemption at the direction of the Company, in whole or in part, at any time on or after October 1, 2015.

The 3.75% Industrial Development Authority Revenue Refunding Bonds, Series 1995, had a mandatory tender date of June 1, 2010. The Company retired the \$4,300 obligation using funds available under its lines of credit.

On May 7, 2008, the PEDFA issued \$12,000 aggregate principal amount of PEDFA Exempt Facilities Revenue Refunding Bonds, Series A of 2008 (York Water Company Project) (the "Series A Bonds") for our benefit pursuant to the terms of a trust indenture, dated as of May 1, 2008, between the PEDFA and Manufacturers and Traders Trust Company, as trustee. The PEDFA then loaned the proceeds of the offering of the Series A Bonds to us pursuant to a loan agreement, dated as of May 1, 2008, between us and the PEDFA. The loan agreement provides for a \$12,000 loan with a maturity date of October 1, 2029. Amounts outstanding under the loan agreement are our direct general obligations. The proceeds of the loan were used to redeem the PEDFA Exempt Facilities Revenue Bonds, Series B of 2004 (the "2004 Series B Bonds"). The 2004 Series B Bonds were redeemed because the bonds were tendered and could not be remarketed due to the downgrade of the bond insurer's credit rating.

Borrowings under the loan agreement bear interest at a variable rate as determined by PNC Capital Markets, as remarketing agent, on a periodic basis elected by us. We have currently elected that the interest rate be determined on a weekly basis. The remarketing agent determines the interest rate based on then current market conditions in order to determine the lowest interest rate which would cause the Series A Bonds to have a market value equal to the principal amount thereof plus accrued interest thereon. The variable interest rate under the loan agreement averaged 0.30% in 2010 and 0.51% in 2009. As of December 31, 2010 and 2009, the interest rate was 0.38% and 0.26%, respectively.

The holders of the \$12,000 variable rate PEDFA Series A Bonds may tender their bonds at any time. When the bonds are tendered, they are subject to an annual remarketing agreement, pursuant to which a remarketing agent attempts to remarket the tendered bonds pursuant to the terms of the indenture. In order to keep variable interest rates down and to enhance the marketability of the Series A Bonds, the Company entered into a Reimbursement, Credit and Security Agreement with PNC Bank, National Association ("the bank") dated as of May 1, 2008. This agreement provides for a three-year direct pay letter of credit issued by the bank to the trustee for the Series A Bonds. The bank is responsible for providing the trustee with funds for the timely payment of the principal and interest on the Series A Bonds and for the purchase price of the Series A Bonds that have been tendered or deemed tendered for purchase and have not been remarketed. The Company's responsibility is to reimburse the bank the same day as regular interest payments are made, and within fourteen months for the purchase price of tendered bonds that have not been remarketed. The reimbursement period for the principal is immediate at maturity, upon default by the Company, or if the Bank does not renew the Letter of Credit. The Letter of Credit is a three-year agreement with a one-year extension evaluated annually. The current expiration date is May 6, 2012.

The Company may elect to have the Series A Bonds redeemed, in whole or in part, on any date that interest is payable for a redemption price equal to 100% of the principal amount thereof plus accrued interest to the date of redemption. The Series A Bonds are also subject to mandatory redemption for the same redemption price in the event that the Internal Revenue Service determines that the interest payable on the Series A Bonds is includable in gross income of the holders of the bonds for federal tax purposes.

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

In connection with the issuance of the PEDFA 2004 Series B Bonds, the Company entered into an interest rate swap agreement with a counterparty, in the notional principal amount of \$12,000. We elected to retain the swap agreement for the PEDFA Series A Bonds of 2008. Interest rate swap agreements derive their value from underlying interest rates. These transactions involve both credit and market risk. The notional amounts are amounts on which calculations, payments, and the value of the derivative are based. Notional amounts do not represent direct credit exposure. Direct credit exposure is limited to the net difference between the calculated amounts to be received and paid, if any. Such difference, which represents the fair value of the swap, is reflected on the Company's balance sheet. See Note 10 for additional information regarding the fair value of the swap.

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

The interest rate swap agreement contains provisions that require the Company to maintain a credit rating of at least BBB- with Standard & Poor's. If the Company's rating were to fall below this rating, it would be in violation of these provisions, and the counterparty to the derivative could request immediate payment if the derivative was in a liability position. The Company's interest rate swap was in a liability position as of December 31, 2010. If a violation were triggered on December 31, 2010, the Company would have been required to pay the counterparty approximately \$1,457.

Our interest rate swap agreement provides that we pay the counterparty a fixed interest rate of 3.16% on the notional amount of \$12,000. In exchange, the counterparty pays us a floating interest rate (based on 59% of the U.S. Dollar one-month LIBOR rate) on the notional amount. The floating interest rate paid to us is intended, over the term of the swap, to approximate the variable interest rate on the loan agreement and the interest rate paid to bondholders, thereby managing our exposure to fluctuations in prevailing interest rates. The Company's net payment rate on the swap averaged 3.00% in 2010 and 2.98% in 2009.

As of December 31, 2010, there was a spread of 23 basis points between the variable rate paid to bondholders and the variable rate received from the swap counterparty, which equated to an overall effective rate of 3.39% (including variable interest and swap payments). As of December 31, 2009, there was a spread of 12 basis points which equated to an overall effective rate of 3.28% (including variable interest and swap payments).

The terms of the debt agreements carry certain covenants and limit in some cases the Company's ability to borrow additional funds, to prepay its borrowings and include certain restrictions with respect to declaration and payment of cash dividends and acquisition of the Company's stock. Under the terms of the most restrictive agreements, the Company cannot borrow in excess of 60% of its utility plant, and cumulative payments for dividends and acquisition of stock since December 31, 1982 may not exceed \$1,500 plus net income since that date. As of December 31, 2010, none of the earnings retained in the business are restricted under these provisions. Our 1.00% Pennvest Loan is secured by \$800 of receivables. Other than this loan, our debt is unsecured.

As of December 31, 2010, the Company maintained unsecured lines of credit aggregating \$33,000 with three banks. One line of credit includes a \$4,000 portion which is payable upon demand and carries an interest rate of LIBOR plus 2.00% and a \$13,000 committed portion with a revolving 2-year maturity (currently May 2012), which carries an interest rate of LIBOR plus 2.00%. The Company had no outstanding borrowings under the committed portion and no on-demand borrowings under this line of

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

4. LONG-TERM DEBT AND SHORT-TERM BORROWINGS (CONTINUED)

credit as of December 31, 2010. The Company had \$3,054 in outstanding borrowings under the committed portion and no on-demand borrowings under this line of credit as of December 31, 2009. The second line of credit, in the amount of \$11,000, is a committed line of credit, which matures in May 2012 and carries an interest rate of LIBOR plus 1.50%. This line of credit has a compensating balance requirement of \$500. In 2010, the outstanding borrowings were reclassified to long-term debt based on a renewal that extended the maturity date more than one year. The corresponding compensating balance was also reclassified from current assets to long-term assets due to the extended maturity date. The Company had no outstanding borrowings under this line as of December 31, 2010 and \$3,000 outstanding under this line as of December 31, 2009. The third line of credit, in the amount of \$5,000, is a committed line of credit, which matures in June 2011 and carries an interest rate of LIBOR plus 2.00%. The Company had no outstanding borrowings under this line as of December 31, 2010 and \$2,000 outstanding under this line as of December 31, 2009. The weighted average interest rate on line of credit borrowings as of December 31, 2009 was 1.56%.

Average borrowings outstanding under our lines of credit were \$7,191 in 2010 and \$16,848 in 2009. The average cost of borrowings under our lines of credit during 2010 and 2009 was 1.54% and 1.41%, respectively.

Our lines of credits require us to maintain a minimum equity to total capitalization ratio (defined as the sum of equity plus funded debt) and a minimum interest coverage ratio (defined as net income plus interest expense plus income tax expense divided by interest expense). The Company is currently in compliance with these covenants.

5. COMMON STOCK AND EARNINGS PER SHARE

Earnings per share are based upon the weighted average number of shares outstanding of 12,626,660 in 2010, 11,695,155 in 2009 and 11,298,215 in 2008. The Company does not have dilutive securities outstanding.

Under the employee stock purchase plan, all full-time employees who have been employed at least six consecutive months may purchase shares of the Company's common stock through payroll deductions limited to 10% of gross compensation. The purchase price is 95% of the fair market value (as defined). Shares issued during 2010, 2009 and 2008 were 6,968, 6,860 and 6,841, respectively. As of December 31, 2010, 37,860 authorized shares remain unissued under the plan.

In June 2008, the Company modified its Dividend Reinvestment Plan to include direct stock purchase and sale options. These options are subject to certain restrictions and are available to both current shareholders and the general public. Purchases are made weekly at 100% of the stock's fair market value, as defined in the Prospectus contained in Amendment No. 1 to Securities and Exchange Commission Form S-3, filed by the Company on June 26, 2008. The Company received \$905 in 2010, \$592 in 2009 and \$295 in 2008 of equity proceeds for shares issued under the plan.

Under the optional dividend reinvestment portion of the plan, holders of the Company's common stock may purchase additional shares instead of receiving cash dividends. The purchase price is 95% of the fair market value (as defined). Shares issued under the Dividend Reinvestment and Direct Stock Purchase and Sale Plan, during 2010, 2009, and 2008 were 126,361, 114,616 and 95,484, respectively. As of December 31, 2010, 629,158 authorized shares remain unissued under the plan.

In September 2009, the Company closed an underwritten public offering of 950,000 shares of its common stock. In October 2009, the underwriters exercised an over-allotment of 120,000 shares. Boenning & Scattergood, Inc. and J.J.B. Hilliard, W.L. Lyons, LLC were the underwriters in the offering. The Company received net proceeds in the offering, after deducting offering expenses and underwriter's discounts and commissions, of approximately \$14.1 million. The net proceeds were used to repay a portion of the Company's borrowings under its line of credit agreements incurred to fund capital expenditures and acquisitions, and for general corporate purposes.

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

6. EMPLOYEE BENEFIT PLANS

Pensions

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

The following table sets forth the plans' funded status as of December 31, 2010 and 2009. The measurement of assets and obligations of the plans is as of December 31, 2010 and 2009.

Obligations and Funded Status at December 31	2010	2009
Change in Benefit Obligation		
Pension benefit obligation beginning of year	\$ 23,235	\$ 21,282
Service cost	777	793
Interest cost	1,335	1,311
Actuarial loss	2,190	833
Benefit payments	(991)	(984)
Pension benefit obligation end of year	<u>26,546</u>	<u>23,235</u>
Change in Plan Assets		
Fair value of plan assets beginning of year	16,787	13,702
Actual return on plan assets	2,200	2,686
Employer contributions	1,280	1,383
Benefits paid	(991)	(984)
Fair value of plan assets end of year	<u>19,276</u>	<u>16,787</u>
Funded Status of Plans at End of Year	\$ <u>(7,270)</u>	\$ <u>(6,448)</u>

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

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

6. EMPLOYEE BENEFIT PLANS (CONTINUED)

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

	2010	2009
Net loss (gain) arising during the period	\$ 1,155	\$ (909)
Recognized net actuarial loss.....	(213)	(404)
Recognized prior service cost	(17)	(18)
Total changes in regulatory asset during the year	<u>\$ 925</u>	<u>\$ (1,331)</u>

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

	2010	2009
Net loss	\$ 6,755	\$ 5,812
Prior service cost.....	102	120
Regulatory asset	<u>\$ 6,857</u>	<u>\$ 5,932</u>

Components of Net Periodic Benefit Cost are as follows:

	2010	2009	2008
Service cost	\$ 777	\$ 793	\$ 617
Interest cost.....	1,335	1,311	1,209
Expected return on plan assets	(1,165)	(944)	(1,192)
Amortization of loss	213	404	12
Amortization of prior service cost.....	17	18	17
Rate-regulated adjustment	103	(199)	233
Net periodic benefit cost	<u>\$ 1,280</u>	<u>\$ 1,383</u>	<u>\$ 896</u>

The rate-regulated adjustment set forth above is required in order to reflect pension expense for the Company in accordance with the method used in establishing water rates. The Company is permitted by rate order of the PPUC to expense pension costs to the extent of contributions and defer the remaining expense to regulatory assets to be collected in rates at a later date as additional contributions are made. During 2010, the deferral declined by \$103.

The estimated costs for the defined benefit pension plans relating to the December 31, 2010 balance sheet that will be amortized from regulatory assets into net periodic benefit cost over the next fiscal year are as follows:

Net loss	\$ 293
Net prior service cost	17
	<u>\$ 310</u>

The Company plans to contribute \$1,593 to the plans in 2011.

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

2011	2012	2013	2014	2015	2016-2020
\$1,097	\$1,106	\$1,158	\$1,250	\$1,484	\$8,658

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

The accumulated benefit obligation for both defined benefit pension plans was \$23,244 and \$19,793 at December 31, 2010 and 2009, respectively. The following table shows the accumulated benefit obligation, the projected benefit obligation and the fair value of plan assets for each plan:

	General and Administrative Plan		Union-Represented Plan	
	2010	2009	2010	2009
Accumulated benefit obligation.....	\$ 14,683	\$ 12,654	\$ 8,561	\$ 7,139
Projected benefit obligation.....	16,936	15,010	9,610	8,225
Fair value of plan assets.....	12,106	10,449	7,170	6,338

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

	2010	2009
Discount rate.....	5.35%	6.00%
Expected long-term return on plan assets.....	7.00%	7.00%
Rate of compensation increase.....	3.50 - 4.00%	4.00 - 5.00%

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

	2010	2009	2008
Discount rate.....	6.00%	6.00%	6.50%
Expected long-term return on plan assets.....	7.00%	7.00%	7.00%
Rate of compensation increase.....	4.00 - 5.00%	4.00 - 5.00%	4.00 - 5.00%

The selected long-term rate of return on plan assets (7.0%) was primarily based on the asset allocation of the plan's assets (approximately 50% to 70% equity securities and 30% to 50% fixed income securities). Analysis of the historic returns of these asset classes and projections of expected future returns were considered in setting the long-term rate of return.

The investment objective of the Company's defined benefit pension plans is that of Growth and Income. Our weighted-average target asset allocations are 50% to 70% equity securities, 30% to 50% fixed income securities and 0% to 10% reserves (cash and cash equivalents). Within the equity category, our target allocation is approximately 45-50% large cap, 15% mid cap, 10% small cap, 15% international, 5% emerging markets and 5-10% inflation hedge. Within the debt category, our target allocation is approximately 30% U.S. Treasury and Agency securities, 40% U.S. corporate bonds, 10% mortgage-backed securities, 10% international, and 10% high yield bonds. Our investment performance objectives over a three to five year period are to exceed the annual rate of inflation as measured by the Consumer Price Index by 3%, and to exceed the annualized total return of specified benchmarks applicable to the funds within the asset categories.

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

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

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

6. EMPLOYEE BENEFIT PLANS (CONTINUED)

The fair values of the Company's pension plan assets at December 31, 2010 and 2009 by asset category and fair value hierarchy level are as follows. The majority of the valuations are based on quoted prices on active markets (Level 1), 86% in 2010 and 82% in 2009, with the remaining 14% and 18%, respectively, based on broker/dealer quotes, active market makers, models, and yield curves (Level 2).

Asset Category	Total Fair Value		Quoted Prices in Active Markets for Identical Assets (Level 1)		Significant Other Observable Inputs (Level 2)	
	2010	2009	2010	2009	2010	2009
Cash and Money Market Funds (a)	\$ 346	\$ 341	\$ 346	\$ 341	\$ —	\$ —
Equity Securities:						
Common Equity Securities (b).....	3,714	5,296	3,714	5,296	—	—
Equity Mutual Funds (c).....	8,967	6,745	8,967	6,745	—	—
Fixed Income Securities:						
U.S. Treasury Obligations	856	850	—	—	856	850
U.S. Government Agencies	935	773	—	—	935	773
Corporate and Foreign Bonds (d)	923	1,391	—	—	923	1,391
Fixed Income Mutual Funds (e).....	3,535	1,391	3,535	1,391	—	—
Total Plan Assets	\$ 19,276	\$ 16,787	\$ 16,562	\$ 13,773	\$ 2,714	\$ 3,014

- (a) The portfolios are designed to keep approximately three months of distributions in immediately available funds.
- (b) This category includes investments in 100% U.S. common stocks widely distributed among consumer discretionary, consumer staples, healthcare, information technology, financial services, telecommunications, industrials, energy and utilities. The individual stocks are primarily large cap stocks which track with the S&P 500 with the exception of \$334 (1.7% of total plan assets) which are invested in York Water Company common stock.
- (c) This category includes investments in approximately 10% U.S. commodity mutual funds used primarily as an inflation hedge, 13% international mutual funds, and the remaining 77% in closed-end mutual funds which give the portfolio exposure to small, mid and large cap index funds as well as international diversified index funds.
- (d) This category currently includes only U.S. corporate bonds and notes equitably distributed to the food and staples, financial and information technology sectors.
- (e) This category includes fixed income investments in mutual funds which include municipal, government, corporate and mortgage securities of both the U.S. and other countries. The mortgage and asset-backed securities and non-U.S. corporate and sovereign investments add further diversity to the fixed income portion of the portfolio.

Defined Contribution Plan

The Company has a savings plan pursuant to the provisions of section 401(k) of the Internal Revenue Code. For employees hired before May 1, 2010, this plan provides for elective employee contributions of up to 15% of compensation and Company matching contributions of 100% of the participant's contribution, up to a maximum annual Company contribution of \$2.8 for each employee. The maximum annual Company contribution was increased by \$0.6 during 2010.

Employees hired after May 1, 2010 are entitled to an enhanced feature of the plan. This feature provides for elective employee contributions of up to 15% of compensation and Company matching contributions of 100% of the participant's contribution, up to a maximum of 4% of the employee's compensation. In addition, the Company will make an annual contribution of \$1.2 to each employee's account whether or not they defer their own compensation. Employees eligible for this enhanced 401k plan feature are not eligible for the defined benefit plans. As of December 31, 2010, no employees were participating in the enhanced feature of the plan. The Company's contributions to the plan amounted to \$187 in 2010, \$146 in 2009, and \$168 in 2008.

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

Deferred Compensation

The Company has non-qualified deferred compensation and supplemental retirement agreements with certain members of management. The future commitments under these arrangements are offset by corporate-owned life insurance policies. At December 31, 2010 and 2009, the present value of the future obligations was approximately \$2,692 and \$2,454, respectively. The insurance policies included in other assets had a total cash value of approximately \$3,430 and \$3,173, respectively, at December 31, 2010 and 2009. The Company's expenses under the plans amounted to \$360 in 2010, \$413 in 2009 and \$490 in 2008.

7. RATE INCREASES

From time to time, the Company files applications for rate increases with the PPUC and is granted rate relief as a result of such requests. The most recent rate request was filed by the Company on May 14, 2010 and sought an increase of \$6,220, which would have represented a 15.9% increase in rates. Effective November 4, 2010, the PPUC authorized an average increase of 8.7% in rates designed to produce approximately \$3,400 in additional annual revenues. The Company does not expect to file a base rate increase request in 2011.

8. NOTES RECEIVABLE AND CUSTOMERS' ADVANCES FOR CONSTRUCTION

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

The Company has recorded interest income of \$110 in 2010, \$116 in 2009 and \$114 in 2008. Interest rates on the notes outstanding at December 31, 2010 vary from 6.75% to 7.5%.

Included in the accompanying balance sheets at December 31, 2010 and 2009 were the following amounts related to these projects.

	2010	2009
Notes receivable, including interest.....	\$ 407	\$ 476
Customers' advances for construction	967	1,013

The Company has other customers' advances for construction totaling \$14,064 and \$15,175 at December 31, 2010 and 2009, respectively.

9. COMMITMENTS

Based on its capital budget, the Company plans to spend approximately \$12,800 in 2011 and \$13,415 in 2012 on construction. The Company plans to finance ongoing capital expenditures with internally-generated funds, borrowings against the Company's lines of credit, proceeds from the issuance of common stock under its dividend reinvestment and direct stock purchase and sale plan and ESPP, potential common stock or debt issues, customer advances and the distribution surcharge allowed by the PPUC. The distribution surcharge allows the Company to add a charge to customers' bills for qualified replacement costs of certain infrastructure without submitting a rate filing.

The Company has committed a total of approximately \$2,905 for upgrades to the water treatment facilities. As of December 31, 2010, \$179 remained to be incurred.

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

9. COMMITMENTS (CONTINUED)

As of December 31, 2010, the Company employed 111 full time people, including 42 under union contract. The current contract was ratified during 2010 and expires on April 30, 2013.

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

10. FAIR VALUE OF FINANCIAL INSTRUMENTS

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

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

Description	December 31, 2010	Fair Value Measurements at Reporting Date Using Significant Other Observable Inputs (Level 2)
Interest Rate Swap	\$1,341	\$1,341

Fair values are measured as the present value of all expected future cash flows based on the LIBOR-based swap yield curve as of the date of the valuation. These inputs to this calculation are deemed to be Level 2 inputs. The balance sheet carrying value reflects the Company's credit quality as of December 31, 2010. The rate used in discounting all prospective cash flows anticipated to be made under this swap reflects a representation of the yield to maturity for 30-year debt on utilities rated A- as of December 31, 2010. The use of the Company's credit quality resulted in a reduction in the swap liability of \$116. The fair value of the swap reflecting the Company's credit quality as of December 31, 2009 is shown in the table below.

Description	December 31, 2009	Fair Value Measurements at Reporting Date Using Significant Other Observable Inputs (Level 2)
Interest Rate Swap	\$979	\$979

The carrying amount of current assets and liabilities that are considered financial instruments approximates fair value as of the dates presented. The Company's long-term debt (including current maturities), with a carrying value of \$85,173 at December 31, 2010, and \$77,568 at December 31, 2009, had an estimated fair value of approximately \$94,000 and \$91,000 at December 31, 2010 and 2009, respectively. The estimated fair value of debt was calculated using a discounted cash flow technique that incorporates a market interest yield curve with adjustments for duration and risk profile. The Company recognized its credit rating in determining the yield curve, and did not factor in third party credit enhancements including bond insurance on the 2004 PEDFA Series A and 2006 Industrial Development Authority issues, and the letter of credit on the 2008 PEDFA Series A issue.

Notes to Financial Statements

(In thousands of dollars, except per share amounts)

Customers' advances for construction and notes receivable have carrying values at December 31, 2010 of \$15,031 and \$407, respectively. At December 31, 2009, customers' advances for construction and notes receivable had carrying values of \$16,188 and \$476, respectively. The relative fair values of these amounts cannot be accurately estimated since the timing of future payment streams is dependent upon several factors, including new customer connections, customer consumption levels and future rate increases.

11. TAXES OTHER THAN INCOME TAXES

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

	2010	2009	2008
Regulatory Assessment.....	\$ 205	\$ 210	\$ 194
Property	321	311	266
Payroll, net of amounts capitalized.....	430	419	421
Capital Stock	203	133	219
Other.....	2	2	2
Total taxes other than income taxes	<u>\$ 1,161</u>	<u>\$ 1,075</u>	<u>\$ 1,102</u>

12. SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

2010	First	Second	Third	Fourth	Year
Water operating revenues.....	\$9,016	\$9,748	\$10,487	\$9,754	\$39,005
Water operating income	4,275	5,045	5,604	4,843	19,767
Net income	1,839	2,344	2,670	2,076	8,929
Basic earnings per share.....	0.15	0.18	0.21	0.17	0.71
Dividends declared per share	0.128	0.128	0.128	0.131	0.515
2009	First	Second	Third	Fourth	Year
Water operating revenues.....	\$8,774	\$9,210	\$9,750	\$9,309	\$37,043
Water operating income	3,971	4,228	4,836	4,353	17,388
Net income	1,497	1,913	2,091	2,011	7,512
Basic earnings per share.....	0.13	0.17	0.18	0.16	0.64
Dividends declared per share	0.126	0.126	0.126	0.128	0.506

Supplemental Information (Unaudited)

(In thousands of dollars, except per share amounts)

Year Ended December 31	2010	2009	2008
Selected Financial Data			
Income			
Operating Revenues.....	\$39,005	\$37,043	\$32,838
Operating Expenses	\$19,238	\$19,655	\$18,158
Operating Income.....	\$19,767	\$17,388	\$14,680
Interest Expense.....	\$4,795	\$4,780	\$4,112
Net Income	\$8,929	\$7,512	\$6,431
Percent Change in Net Income Compared to Prior Year	18.9%	16.8%	0.3%
Common Stock Dividends	\$6,506	\$6,050	\$5,526
Dividend Payout Ratio	73%	81%	86%
Weighted Average Common Shares Outstanding.....	12,626,660	11,695,155	11,298,215
Basic Earnings Per Weighted Average Common Share.....	\$0.71	\$0.64	\$0.57
Number of Common Shares Outstanding	12,692,054	12,558,724	11,367,248
ROE on Year End Common Equity	9.8%	8.6%	9.2%
Common Stock Dividends Per Share	\$0.515	\$0.506	\$0.489
Net Cash Flows From Operating Activities	\$14,755	\$15,801	\$11,527
Balance Sheet			
Common Stockholders' Equity	\$91,257	\$86,922	\$69,766
Long-Term Debt Including Current Maturities.....	\$85,173	\$77,568	\$86,353
Total Capitalization	\$176,430	\$164,490	\$156,119
Percent Common Stockholders' Equity	52%	53%	45%
Percent Long-Term Debt	48%	47%	55%
Net Utility Plant	\$227,677	\$221,475	\$210,820
Operating Data			
Revenue Class			
Residential	\$24,478	\$23,299	\$20,572
Commercial and Industrial.....	\$11,440	\$10,734	\$9,671
Other.....	\$3,087	\$3,010	\$2,595
Total Operating Revenues.....	\$39,005	\$37,043	\$32,838
Construction Expenditures	\$10,541	\$12,535	\$24,438
Other Operating Data			
Number of Customers	62,505	62,186	61,527
Number of Employees.....	111	111	110
Common Shareholders	1,649	1,516	1,485
Book Value Per Common Share	\$7.19	\$6.92	\$6.14
Market Value at Year End	\$17.29	\$14.51	\$12.10
Market Value to Book Value	240%	210%	197%
P/E Ratio	24.4	22.7	21.2

Supplemental Information (Unaudited)

(In thousands of dollars, except per share amounts)

2007	2006	2005	2004	2003	2002	2001	2000
\$31,433	\$28,658	\$26,805	\$22,504	\$20,889	\$19,553	\$19,403	\$18,481
\$17,333	\$15,754	\$14,049	\$12,627	\$11,578	\$11,243	\$10,468	\$10,008
\$14,100	\$12,904	\$12,756	\$9,877	\$9,311	\$8,310	\$8,935	\$8,473
\$3,916	\$3,727	\$3,423	\$2,132	\$2,523	\$2,692	\$2,856	\$2,798
\$6,414	\$6,091	\$5,833	\$5,301	\$4,448	\$3,790	\$4,006	\$3,758
5.3%	4.4%	10.0%	19.2%	17.4%	-5.4%	6.6%	19.2%
\$5,332	\$4,820	\$4,392	\$3,930	\$3,512	\$3,323	\$3,126	\$2,950
83%	79%	75%	74%	79%	88%	78%	78%
11,225,822	10,475,173	10,359,374	9,937,836	9,579,690	9,495,591	9,229,875	9,032,025
\$0.57	\$0.58	\$0.56	\$0.53	\$0.46	\$0.40	\$0.43	\$0.42
11,264,923	11,201,119	10,399,995	10,330,571	9,628,845	9,547,205	9,462,996	9,128,199
9.5%	9.3%	11.6%	11.0%	11.4%	10.2%	11.2%	11.6%
\$0.475	\$0.454	\$0.424	\$0.394	\$0.367	\$0.350	\$0.337	\$0.327
\$10,040	\$7,116	\$8,451	\$7,670	\$6,772	\$6,172	\$6,734	\$6,371
\$67,272	\$65,361	\$50,415	\$48,037	\$39,056	\$37,216	\$35,892	\$32,438
\$70,505	\$62,335	\$51,874	\$51,913	\$32,652	\$32,690	\$32,728	\$32,765
\$137,777	\$127,696	\$102,289	\$99,950	\$71,708	\$69,906	\$68,620	\$65,203
49%	51%	49%	48%	54%	53%	52%	50%
51%	49%	51%	52%	46%	47%	48%	50%
\$191,046	\$173,800	\$154,774	\$139,454	\$115,724	\$106,217	\$101,753	\$96,434
\$19,722	\$17,972	\$16,737	\$13,789	\$12,574	\$11,527	\$11,571	\$10,980
\$9,290	\$8,497	\$8,009	\$6,893	\$6,598	\$6,385	\$6,265	\$6,033
\$2,421	\$2,189	\$2,059	\$1,822	\$1,717	\$1,641	\$1,567	\$1,468
\$31,433	\$28,658	\$26,805	\$22,504	\$20,889	\$19,553	\$19,403	\$18,481
\$18,154	\$20,678	\$15,562	\$25,689	\$10,252	\$6,310	\$7,096	\$6,414
58,890	57,578	55,731	53,134	51,916	51,023	50,079	49,195
109	106	97	95	92	89	90	90
1,443	1,463	1,449	1,459	1,392	1,353	1,327	1,307
\$5.97	\$5.84	\$4.85	\$4.65	\$4.05	\$3.90	\$3.79	\$3.55
\$15.50	\$17.88	\$17.23	\$12.93	\$12.13	\$9.47	\$9.75	\$6.00
260%	306%	356%	278%	299%	243%	257%	169%
27.2	30.8	30.8	24.3	26.0	23.7	22.5	14.3

Directors, Officers, & Key Employees

BOARD OF DIRECTORS



Cynthia A. Dotzel, CPA ⁽²⁾
Age 56
Director Since January 26, 2009



John L. Finlayson ^{(2) (3)}
Age 70
Director Since September 2, 1993



Michael W. Gang, Esq. ^{(1) (3)}
Age 60
Director Since January 22, 1996



George Hay Kain, III ⁽⁴⁾
Age 62
Director Since August 25, 1986



William T. Morris
Age 73
Retired from Board on August 17, 2010



Thomas C. Norris ^{(1) (2) (4)}
Age 72
Director Since June 26, 2000

- (1) Executive Committee
- (2) Audit Committee
- (3) Nomination and Corporate Governance Committee
- (4) Compensation Committee

Directors, Officers, & Key Employees

BOARD OF DIRECTORS



Jeffrey R. Hines, P.E. ⁽¹⁾
Age 49
Director Since January 28, 2008



George W. Hodges ^{(2) (4)}
Age 60
Director Since September 26, 2000



Jeffrey S. Osman ⁽¹⁾
Age 68
Director Since July 21, 2001



Ernest J. Waters ⁽³⁾
Age 61
Director Since September 24, 2007

DIRECTORS EMERITI

Josephine S. Appell
Chloé R. Eichelberger
Horace Keesey, III
William T. Morris
Irvin S. Naylor

OFFICERS & KEY EMPLOYEES

Jeffrey R. Hines, P.E.
Age 49
President and
Chief Executive Officer

Joseph T. Hand
Age 48
Chief Operating Officer

Kathleen M. Miller
Age 48
Chief Financial Officer
and Treasurer

Vernon L. Bracey
Age 49
Vice President-Customer Service

Bruce C. McIntosh
Age 58
Vice President-Human Resources
and Secretary

Mark S. Snyder
Age 40
Vice President-Engineering

John H. Strine
Age 54
Vice President-Operations

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STOCK EXCHANGE LISTING

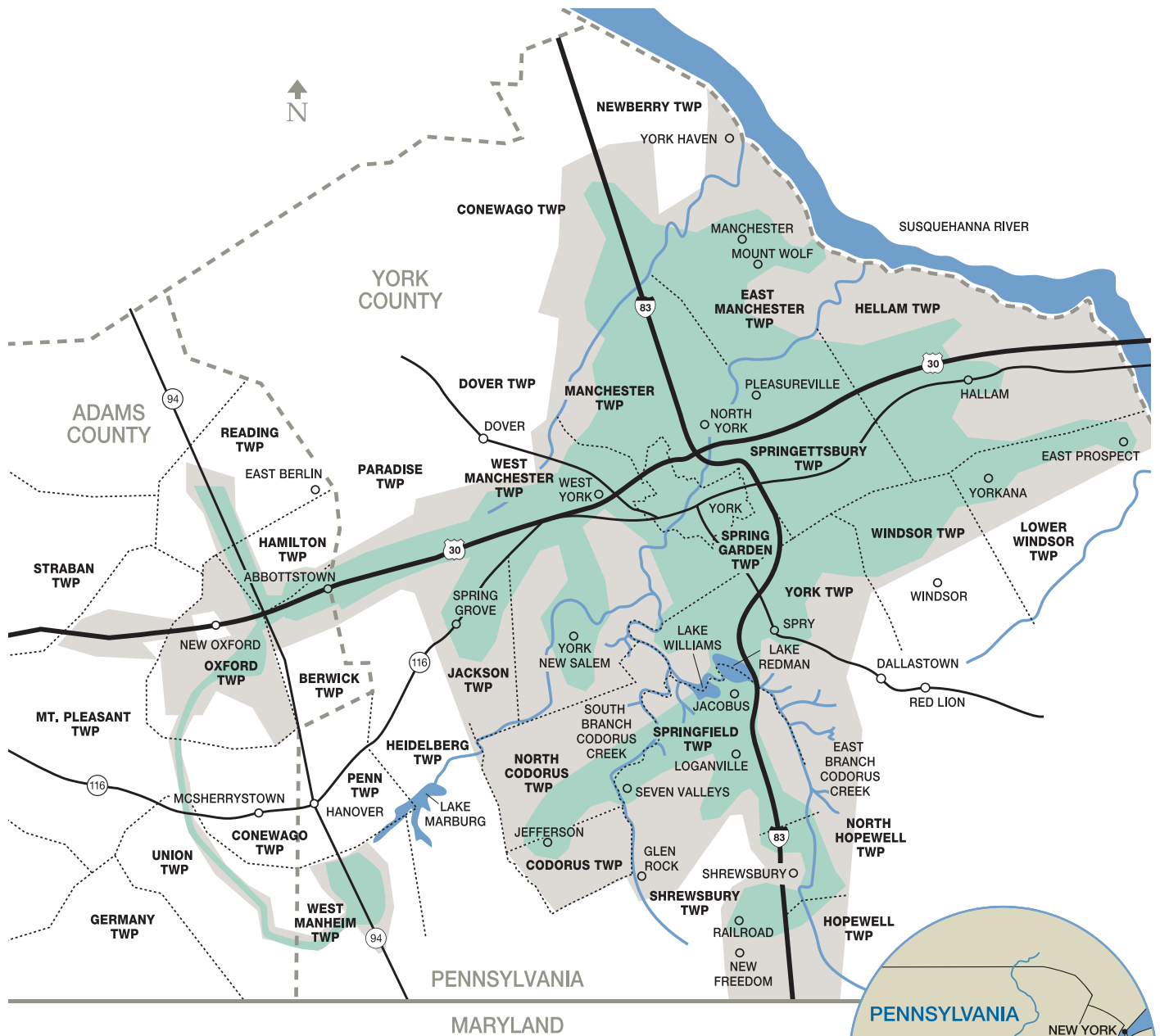
The Company's common shares
trade on the NASDAQ Global
Select Market.

The trading symbol is "YORW".

INDEPENDENT AUDITORS

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York, PA 17401

Chartered Territory Distribution and Supply System



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CHARTERED TERRITORY

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THE YORK WATER COMPANY

