AQUA AMERICA INC
Form 10-Q
May 03, 2019
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2019

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

For the transition period from_______________ to _______________

Commission File Number 1-6659

AQUA AMERICA, INC.

(Exact name of registrant as specified in its charter)

Pennsylvania (State or other jurisdiction of incorporation or organization)	23-1702594 (I.R.S. Employer Identification No.)
762 W. Lancaster Avenue, Bryn Mawr, Pennsylvania (Address of principal executive offices)	19010 -3489 (Zip Code)
(610) 527-8000 (Registrant’s telephone number, including area code)	

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
Emerging growth company	

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

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

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common stock, $.50 par value	WTR	New York Stock Exchange
6.00% Tangible Equity Units	WTRU	New York Stock Exchange

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of April 24, 2019: 215,739,266

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AQUA AMERICA, INC. AND SUBSIDIARIES

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AQUA AMERICA, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands of dollars, except per share amounts)

(UNAUDITED)

Assets	March 31, 2019	December 31, 2018
Property, plant and equipment, at cost	$ 7,747,530	$ 7,648,469
Less: accumulated depreciation	1,727,190	1,718,143
Net property, plant and equipment	6,020,340	5,930,326
Current assets:		
Cash and cash equivalents	4,053	3,627
Accounts receivable and unbilled revenues, net	96,410	101,225
Inventory, materials and supplies	16,209	15,844
Prepayments and other current assets	24,096	23,337
Assets held for sale	3,007	3,139
Total current assets	143,775	147,172
Regulatory assets	803,093	788,076
Deferred charges and other assets, net	40,745	39,237
Investment in joint venture	6,840	6,959
Goodwill	53,069	52,726
Operating lease right-of-use assets	13,088	-
Total assets	$ 7,080,950	$ 6,964,496
Liabilities and Equity		
Stockholders' equity:		
Common stock at $.50 par value, authorized 300,000,000 shares, issued 181,481,408 and 181,151,827 as of March 31, 2019 and December 31, 2018	$ 90,741	$ 90,576
Capital in excess of par value	827,339	820,378
Retained earnings	1,152,197	1,174,245
Treasury stock, at cost, 3,112,330 and 3,060,206 shares as of March 31, 2019 and December 31, 2018	(77,692)	(75,835)
Total stockholders' equity	1,992,585	2,009,364
Long-term debt, excluding current portion	2,483,119	2,419,115
Less: debt issuance costs	20,264	20,651
Long-term debt, excluding current portion, net of debt issuance costs	2,462,855	2,398,464
Commitments and contingencies (See Note 15)		

Current liabilities:		
Current portion of long-term debt	156,455	144,545
Loans payable	32,563	15,449
Accounts payable	55,110	77,331
Book overdraft	5,095	8,950
Accrued interest	27,628	23,300
Accrued taxes	22,563	22,234
Interest rate swap agreements	94,561	59,779
Other accrued liabilities	40,124	47,389
Total current liabilities	434,099	398,977
Deferred credits and other liabilities:		
Deferred income taxes and investment tax credits	855,156	845,403
Customers' advances for construction	99,186	93,343
Regulatory liabilities	528,471	531,027
Operating lease liabilities	11,744	-
Other	96,897	97,182
Total deferred credits and other liabilities	1,591,454	1,566,955
Contributions in aid of construction	599,957	590,736
Total liabilities and equity	$ 7,080,950	$ 6,964,496

See notes to consolidated financial statements beginning on page 7 of this report.

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AQUA AMERICA, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME

(In thousands, except per share amounts)

(UNAUDITED)

	Three Months Ended March 31,	
	2019	2018
Operating revenues	$ 201,132	$ 194,347
Operating expenses:		
Operations and maintenance	79,314	73,946
Depreciation	39,074	35,967
Amortization	336	130
Taxes other than income taxes	14,969	14,967
Total operating expenses	133,693	125,010
Operating income	67,439	69,337
Other expense (income):		
Interest expense, net	27,850	23,471
Allowance for funds used during construction	(4,056)	(2,867)
Change in fair value of interest rate swap agreements	34,782	-
Gain on sale of other assets	(220)	(196)
Equity earnings in joint venture	(543)	(382)
Other	872	603
Income before income taxes	8,754	48,708
Provision for income tax benefit	(8,170)	(2,131)
Net income	$ 16,924	$ 50,839
Comprehensive income	$ 16,924	$ 50,839
Net income per common share:		
Basic	$ 0.09	$ 0.29
Diluted	$ 0.09	$ 0.29
Average common shares outstanding during the period:		
Basic	178,213	177,801
Diluted	178,552	178,238

See notes to consolidated financial statements beginning on page 7 of this report.

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AQUA AMERICA, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CAPITALIZATION

(In thousands of dollars, except per share amounts)

(UNAUDITED)

		March 31, 2019	December 31, 2018
Stockholders' equity:			
Common stock, $.50 par value		$ 90,741	$ 90,576
Capital in excess of par value		827,339	820,378
Retained earnings		1,152,197	1,174,245
Treasury stock, at cost		(77,692)	(75,835)
Total stockholders' equity		1,992,585	2,009,364
Long-term debt of subsidiaries (substantially collateralized by utility plant):			
Interest Rate Range	Maturity Date Range		
0.00% to 0.99%	2023 to 2033	3,687	3,732
1.00% to 1.99%	2019 to 2035	11,301	11,588
2.00% to 2.99%	2019 to 2033	17,039	17,488
3.00% to 3.99%	2019 to 2056	497,026	497,426
4.00% to 4.99%	2020 to 2057	830,650	831,066
5.00% to 5.99%	2019 to 2043	154,633	154,788
6.00% to 6.99%	2026 to 2036	31,000	31,000
7.00% to 7.99%	2022 to 2027	31,365	31,564
8.00% to 8.99%	2021 to 2025	5,446	5,581
9.00% to 9.99%	2020 to 2026	20,000	20,000
		1,602,147	1,604,233
Notes payable to bank under revolving credit agreement, variable rate, due 2023		448,000	370,000
Unsecured notes payable:			
Bank notes at 2.48% and 3.50% due 2019 and 2020		100,000	100,000
Notes ranging from 3.01% and 3.59% due 2027 and 2041		245,000	245,000
		112,000	112,000

Notes ranging from 4.62% to 4.87%, due 2019 through 2024		
Notes ranging from 5.20% to 5.95%, due 2020 through 2037	132,427	132,427
.	2,639,574	2,563,660
Current portion of long-term debt	156,455	144,545
Long-term debt, excluding current portion	2,483,119	2,419,115
Less: debt issuance costs	20,264	20,651
Long-term debt, excluding current portion, net of debt issuance costs	2,462,855	2,398,464
Total capitalization	$ 4,455,440	$ 4,407,828

See notes to consolidated financial statements beginning on page 7 of this report.

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AQUA AMERICA, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EQUITY

(In thousands of dollars)

(UNAUDITED)

	Common Stock	Capital in Excess of Par Value	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income	Total
Balance at December 31, 2018	$ 90,576	$ 820,378	$ 1,174,245	$ (75,835)	$ -	$ 2,009,364
Net income	-	-	16,924	-	-	16,924
Dividends declared ($0.2190 per share)	-	-	(39,014)	-	-	(39,014)
Issuance of common stock under dividend reinvestment plan (117,845 shares)	59	3,976	-	-	-	4,035
Repurchase of stock (52,124 shares)	-	-	-	(1,857)	-	(1,857)
Equity compensation plan (134,257 shares)	67	(67)	-	-	-	-
Exercise of stock options (77,479 shares)	39	1,136	-	-	-	1,175
Stock-based compensation	-	1,929	42	-	-	1,971
Other	-	(13)	-	-	-	(13)
Balance at March 31, 2019	$ 90,741	$ 827,339	$ 1,152,197	$ (77,692)	$ -	$ 1,992,585

	Common Stock	Capital in Excess of Par Value	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income	Total
Balance at December 31, 2017	$ 90,350	$ 807,135	$ 1,132,556	$ (73,280)	$ 860	$ 1,957,621
Net income	-	-	50,839	-	-	50,839
Dividends declared ($0.2047 per share)	-	-	(36,386)	-	-	(36,386)
Issuance of common stock under dividend reinvestment plan (11,252 shares)	6	355	-	-	-	361
Repurchase of stock (71,940 shares)	-	-	-	(2,491)	-	(2,491)
Equity compensation plan (181,670 shares)	91	(91)	-	-	-	-

Exercise of stock options (62,688 shares)	31	979	-	-	-	1,010
Stock-based compensation	-	1,443	(41)	-	-	1,402
Cumulative effect of change in accounting principle - financial instruments	-	-	860	-	(860)	-
Other	-	(197)	-	-	-	(197)
Balance at March 31, 2018	$ 90,478	$ 809,624	$ 1,147,828	$ (75,771)	$ -	$ 1,972,159

See notes to consolidated financial statements beginning on page 7 of this report.

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AQUA AMERICA, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOW

(In thousands of dollars)

(UNAUDITED)

	Three Months Ended March 31, 2019	2018
Cash flows from operating activities:		
Net income	$ 16,924	$ 50,839
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation and amortization	39,410	36,097
Deferred income taxes	(8,852)	(2,849)
Provision for doubtful accounts	803	896
Stock-based compensation	1,930	1,444
Gain on sale of other assets	(220)	(196)
Interest rate swap agreements	34,782	-
Net change in receivables, inventory and prepayments	2,263	5,402
Net change in payables, accrued interest, accrued taxes and other accrued liabilities	(3,402)	(996)
Pension and other postretirement benefits contributions	(3,947)	(5,217)
Other	(404)	2,934
Net cash flows from operating activities	79,287	88,354
Cash flows from investing activities:		
Property, plant and equipment additions, including the debt component of allowance for funds used during construction of $1,030 and $782	(133,792)	(105,136)
Acquisitions of utility systems, net	(469)	(190)
Net proceeds from the sale of other assets	242	174
Other	462	(75)
Net cash flows used in investing activities	(133,557)	(105,227)
Cash flows from financing activities:		
Customers' advances and contributions in aid of construction	1,858	1,742
Repayments of customers' advances	(765)	(1,014)
Net proceeds of short-term debt	17,114	16,692
Proceeds from long-term debt	117,995	66,996
Repayments of long-term debt	(41,976)	(21,898)
Change in cash overdraft position	(3,856)	(8,944)
Proceeds from issuing common stock	4,035	361
Proceeds from exercised stock options	1,175	1,010
Repurchase of common stock	(1,857)	(2,491)

Dividends paid on common stock	(39,014)	(36,386)
Other	(13)	(197)
Net cash flows from financing activities	54,696	15,871
Net change in cash and cash equivalents	426	(1,002)
Cash and cash equivalents at beginning of period	3,627	4,204
Cash and cash equivalents at end of period	$ 4,053	$ 3,202
Non-cash investing activities:		
Property, plant and equipment additions purchased at the period end, but not yet paid for	$ 42,594	$ 23,629
Non-cash customer advances and contributions in aid of construction	17,331	4,979

See notes to consolidated financial statements beginning on page 7 of this report.

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AQUA AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(In thousands of dollars, except per share amounts)

(UNAUDITED)

Note 1 – Basis of Presentation

The accompanying consolidated balance sheets and statements of capitalization of Aqua America, Inc. and subsidiaries (the “Company”, “we”, “us” or “our”) at March 31, 2019, the consolidated statements of operations and comprehensive income for the three months ended March 31, 2019 and 2018 the consolidated statements of cash flow for the three months ended March 31, 2019 and 2018, and the consolidated statements of equity for the three months ended March 31, 2019 and 2018 are unaudited, but reflect all adjustments, consisting of only normal recurring accruals, which are, in the opinion of management, necessary to present a fair statement of its consolidated financial position, consolidated changes in equity, consolidated results of operations, and consolidated cash flow for the periods presented. Because they cover interim periods, the statements and related notes to the financial statements do not include all disclosures and notes normally provided in annual financial statements and, therefore, should be read in conjunction with the Company’s Annual Report on Form 10-K for the year ended December 31, 2018. The results of operations for interim periods may not be indicative of the results that may be expected for the entire year. The December 31, 2018 consolidated balance sheet data presented herein was derived from the Company’s December 31, 2018 audited consolidated financial statements but does not include all disclosures and notes normally provided in annual financial statements.

The preparation of financial statements often requires the selection of specific accounting methods and policies. Further, significant estimates and judgments may be required in selecting and applying those methods and policies in the recognition of the assets and liabilities in its consolidated balance sheets, the revenues and expenses in its consolidated statements of operations, and the information that is contained in its summary of significant accounting policies and notes to consolidated financial statements. Making these estimates and judgments requires the analysis of information concerning events that may not yet be complete and of facts and circumstances that may change over time. Accordingly, actual amounts or future results can differ materially from those estimates that the Company includes currently in its consolidated financial statements, summary of significant accounting policies, and notes.

There have been no changes to the summary of significant accounting policies, other than as described in Note 17 – Leases as a result of the adoption of a new accounting pronouncement adopted on January 1, 2019, previously identified in the Company’s Annual Report on Form 10-K for the year ended December 31, 2018.

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AQUA AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

(UNAUDITED)

Note 2 – Revenue Recognition

The following table presents our revenues disaggregated by major source and customer class:

	Three Months Ended March 31,2019			Three Months Ended March 31,2018		
	Water Revenues	Wastewater Revenues	Other Revenues	Water Revenues	Wastewater Revenues	Other Revenues
Revenues from contracts with customers:						
Residential	$ 114,047	$ 19,947	$ -	$ 113,837	$ 17,532	$ -
Commercial	30,291	3,566	-	30,342	2,888	-
Fire protection	8,078	-	-	7,938	-	-
Industrial	6,865	481	-	6,360	463	-
Other water	12,808	-	-	11,021	-	-
Other wastewater	-	1,396	-	-	791	-
Other utility	-	-	2,890	-	-	2,335
Revenues from contracts with customers	172,089	25,390	2,890	169,498	21,674	2,335
Alternative revenue program	(36)	(113)	-	-	-	-
Other and eliminations	-	-	912	-	-	840
Consolidated	$ 172,053	$ 25,277	$ 3,802	$ 169,498	$ 21,674	$ 3,175

Revenues from Contracts with Customers – These revenues are composed of three main categories: water, wastewater, and other. Water revenues represent revenues earned for supplying customers with water service. Wastewater revenues represent revenues earned for treating wastewater and releasing it into the water supply. Other revenues are associated fees that relate to the regulated business but are not water and wastewater revenues. See description below for a discussion on the performance obligation for each of these revenue streams.

Tariff Revenues – These revenues are categorized by customer class: residential, commercial, fire protection, industrial, and other water and other wastewater. The rates that generate these revenues are approved by the respective state utility commission, and revenues are billed cyclically and accrued for when unbilled. Other water and other wastewater revenues consist primarily of fines, penalties, surcharges, and availability lot fees. Our performance obligation for tariff revenues is to provide potable water or wastewater treatment service to customers. This performance obligation is satisfied over time as the services are rendered. The amounts that the Company has a right to invoice for tariff revenues reflect the right to consideration from the customers in an amount that corresponds directly with the value transferred to the customer for the performance completed to date.

Other Utility Revenues – Other utility revenues represent revenues earned primarily from: antenna revenues, which represent fees received from telecommunication operators that have put cellular antennas on our water towers, operation and maintenance and billing contracts, which represent fees earned from municipalities for our operation of their water or wastewater treatment services or performing billing services, and fees earned from developers for accessing our water mains. The performance obligations vary for these revenues, but all are primarily recognized over time as the service is delivered.

Alternative Revenue Program – These revenues represent the difference between the actual billed utility water and wastewater revenues for Aqua Illinois and the revenues set in the last Aqua Illinois rate case. We recognize revenues based on the target amount established in the last rate case, and then record either a regulatory asset or liability based on the cumulative annual difference between the target and actual, which results in either a refund due to customers or a payment from customers. The cumulative annual difference is either refunded to customers or collected from customers over a nine-month period. This revenue program represents a contract between the utility and its regulators, not customers, and therefore is not within the scope of the Financial Accounting Standards Board's ("FASB") accounting guidance for recognizing revenue from contracts with customers.

Other and Eliminations – Other and eliminations consist of our market-based revenues, which comprises: Aqua Infrastructure and Aqua Resources (described below), and intercompany eliminations for revenue billed between our subsidiaries.

Aqua Infrastructure is the holding company for our 49% investment in a joint venture that operates a private pipeline system to supply raw water to natural gas well drilling operations in the Marcellus Shale of north central Pennsylvania. The joint venture earns revenues through providing non-utility raw water supply services to natural gas drilling companies which enter into water supply contracts. The performance obligation is to deliver non-potable water to the joint venture's customers. Aqua Infrastructure's share of the revenues recognized by the joint venture is reflected, net, in equity earnings in joint venture on our consolidated statements of operations.

Aqua Resources earns revenues by providing non-regulated water and wastewater services through operating and maintenance contracts, and third-party water and sewer service line repair. The performance obligations are performing agreed upon services in the contract, most commonly operation of third-party water or wastewater treatment services, or billing services, or allowing the use of our logo to a third-party water and sewer service line repair. Revenues are primarily recognized over time as service is delivered.

Note 3 – Goodwill

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

	Regulated Segment	Other	Consolidated
Balance at December 31, 2018	$ 47,885	$ 4,841	$ 52,726
Goodwill acquired	343	-	343
Balance at March 31, 2019	$ 48,228	$ 4,841	$ 53,069

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AQUA AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

(UNAUDITED)

Note 4 – Acquisitions

Peoples Gas Acquisition

Pursuant to the Company's growth strategy, on October 22, 2018, the Company entered into a purchase agreement (the "Acquisition Agreement") with LDC Parent LLC ("Seller"), to acquire its interests in LDC Funding LLC ("LDC"). LDC is the parent of LDC Holdings LLC ("LDC Holdings"), and LDC Holdings is the parent of five natural gas public utility companies, which includes Peoples Natural Gas Company, Peoples Gas Company, and Delta Natural Gas Company as well as other operating subsidiaries. This acquisition is referred to as the "Peoples Gas Acquisition," and collectively these businesses are referred to as "Peoples." Peoples is headquartered in Pittsburgh, Pennsylvania, and serves approximately 740,000 gas utility customers in western Pennsylvania, West Virginia, and Kentucky. At the closing of the Peoples Gas Acquisition, the Company will pay $4,275,000, in cash subject to adjustments for working capital, certain capital expenditures, transaction expenses and closing indebtedness as set forth in the Acquisition Agreement. The Company expects to assume approximately $1,370,000 of Peoples' indebtedness upon the closing of the Peoples Gas Acquisition, which would reduce the cash purchase price by approximately $1,370,000.

On October 22, 2018, the Company obtained a commitment (the "Bridge Commitment") from certain banks to provide senior unsecured bridge loans in an aggregate amount of up to $5,100,000 to, among other things, backstop the Peoples Gas Acquisition purchase price and refinancing of certain debt of the Company and Peoples. On March 29, 2019, the Company entered into a Stock Purchase Agreement to issue shares of common stock in a private placement to fund a portion of the Peoples Gas Acquisition. The gross proceeds of the Stock Purchase Agreement are expected to amount to approximately $750,000. As of March 31, 2019, the Company had terminated approximately $1,633,000 of commitments under the Bridge Commitment. Further, on April 18, 2019, the Company issued $1,293,750 of its common stock and $690,000 of its tangible equity units, with a stated amount of $50 per unit, and on April 26, 2019, the Company issued $900,000 of senior notes. Lastly, in April 2019, as a result of the Company's common stock, tangible equity units, and senior notes issuances, we terminated approximately $2,717,000 of commitments under the Bridge Commitment. The remaining balance available under the Bridge Commitment is $750,000. Refer to Note 6 – Capitalization for further information on these financings.

On October 23, 2018, the Company entered into interest rate swap agreements to mitigate interest rate risk associated with an anticipated $850,000 of future debt issuances to fund a portion of the Peoples Gas Acquisition. The interest rate swaps were settled on April 24, 2019 in conjunction with the issuance of long-term debt used to finance a portion of the purchase price of this acquisition, which resulted in a payment by the Company of $83,520. Refer to Note 7 – Interest Rate Swap Agreements for further information. The interest rate swaps did not qualify for hedge accounting and any changes in the fair value of the swaps was included in our earnings.

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AQUA AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

(UNAUDITED)

The Peoples Gas Acquisition is subject to regulatory approval by the Pennsylvania public utility commission, and other customary closing conditions set forth in the Acquisition Agreement. Approval from the United States Federal Trade Commission was obtained in December 2018 and approvals from the public utility commissions of Kentucky and West Virginia were obtained in March 2019 and April 2019, respectively. The Peoples Gas Acquisition is expected to close in mid-2019, once all regulatory approvals are obtained, and closing conditions are met, and it is anticipated that this acquisition will result in the recording of goodwill. In the event that the Acquisition Agreement is terminated due to certain breaches by the Company, a fee of $120,000 would be payable to the Seller as a reverse termination fee.

Water and Wastewater Utility Acquisitions

In July 2018, the Company acquired the wastewater utility systems assets of Limerick Township, Pennsylvania which serves 5,497 customers. The total cash purchase price for the utility system was $74,836. The purchase price allocation for this acquisition consisted primarily of acquired property, plant and equipment of $64,759, and goodwill of $10,790. Additionally, during 2018, the Company completed seven acquisitions of water and wastewater utility systems in three states adding 8,661 customers. The total purchase price of these utility systems consisted of $42,519 in cash. The purchase price allocation for these acquisitions consisted primarily of acquired property, plant and equipment. Further, in December 2018, the Company acquired the Valley Creek Trunk Sewer System, serving area municipalities in Pennsylvania, from the Tredyffrin Township Municipal Authority for $28,300. The system receives untreated wastewater from area municipalities, which is conveyed to the Valley Forge Treatment Plant. The system consists of 49,000 linear feet of gravity sewers, pump stations, and force mains

In November 2018, the Company entered into a purchase agreement to acquire the wastewater utility system assets of East Norriton Township, Pennsylvania, which serves approximately 4,950 customers for $21,000. The purchase price for this pending acquisition is subject to certain adjustments at closing, and is subject to regulatory approval, including the final determination of the fair value of the rate base acquired.

In July 2018, the Company entered into a purchase agreement to acquire the wastewater utility system assets of Cheltenham Township, Pennsylvania, which serves approximately 10,500 customers for $50,250. The purchase price for this pending acquisition is subject to certain adjustments at closing, and is subject to regulatory approval, including the final determination of the fair value of the rate base acquired.

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AQUA AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

(UNAUDITED)

In addition to the Company's pending acquisitions in East Norriton and Cheltenham Townships, as part of the Company's growth-through-acquisition strategy, the Company entered into purchase agreements to acquire the water or wastewater utility system assets of four municipalities for a total combined purchase price in cash of $38,950 which we plan to finance by the issuance of debt. The purchase price for these acquisitions is subject to certain adjustments at closing, and the acquisitions are subject to regulatory approvals, including the final determination of the fair value of the rate base acquired. Closings for our remaining acquisitions (other than the Peoples Gas Acquisition) are expected to occur by the end of 2019, subject to the timing of the regulatory approval process. In total, these acquisitions (other than the Peoples Gas Acquisition) will add approximately 4,000 customers in two of the states in which the Company operates in.

Note 5 – Assets Held for Sale

In the fourth quarter of 2018, the Company decided to market for sale a water system in Virginia that serves approximately 500 customers. This water system is reported as assets held for sale in the Company's consolidated balance sheet, and in April 2019, the Company completed the sale for proceeds of $1,882.

In the first quarter of 2017, the Company decided to market for sale a water system in Texas that serves approximately 265 customers. This water system is reported as assets held for sale in the Company's consolidated balance sheet, and the sale is expected to close in the second quarter of 2019.

Note 6 – Capitalization

Private Placement

On March 29, 2019, the Company entered into a Stock Purchase Agreement (the "Stock Purchase Agreement") with Canada Pension Plan Investment Board (the "Investor"), pursuant to which the Company has agreed to issue and sell to the Investor in a private placement (the "Private Placement") 21,661,095 newly issued shares of common stock, par value $0.50 per share (the "Common Stock"). The gross proceeds of the Private Placement are expected to amount to approximately $750,000, less estimated expenses of $21,560.

The shares issued and sold to the Investor pursuant to the Private Placement were to be priced at the lower of (1) $34.62, which represents a 4.5% discount to the trailing 20 consecutive trading day volume weighted average price of the Common Stock ending on, and including, March 28, 2019, and (2) the volume weighted average price per share in the Company's subsequent public offering of Common Stock to fund a portion of the Peoples Gas Acquisition. Based on the common stock offering noted below, the Private Placement was priced at $34.62 per share.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands of dollars, except per share amounts)

(UNAUDITED)

The closing of the Private Placement is expected to occur concurrently with the closing of the Peoples Gas Acquisition, subject to certain closing conditions, including the closing of the Peoples Gas Acquisition, and the execution and delivery of a shareholder agreement between the Investor and the Company. The Investor has agreed to certain transfer restrictions for a period of 15 months from the closing date of the Peoples Gas Acquisition.

The Stock Purchase Agreement contains customary representations, warranties and covenants of the Company and the Investor, and the parties have agreed to indemnify each other for losses related to breaches of their respective representations and warranties. Upon closing of the Private Placement, the Company has agreed to reimburse the Investor for reasonable out-of-pocket diligence expenses of up to $4,000, subject to certain exceptions.

Common Stock / Equity Unit Issuances

Subsequent to the quarterly period ended March 31, 2019, on April 23, 2019, the Company issued $1,293,750, less estimated expenses of $30,496, of its common stock and $690,000, less estimated expenses of $16,251, of its tangible equity units (the “Units”), with a stated amount of $50 per unit. These issuances are part of securing the permanent financing to close the Peoples Gas Acquisition. The common stock was issued at $34.62 per share and thus the Private Placement noted above was priced at $34.62 per share.

Each Unit consists of a prepaid stock purchase contract and an amortization note due April 30, 2022, each issued by the Company. Unless earlier settled or redeemed, each stock purchase contract will automatically settle on April 30, 2022 (subject to postponement in limited circumstances) for between 1.1790 and 1.4442 shares of the Company’s common stock, subject to adjustment, based upon the applicable market value of the common stock, as described in the final prospectus supplement relating to the Units. The amortizing notes have an initial principal amount of $8.62909, or $119,081 in aggregate, and bear interest at a rate of 3.00% per year, and pay equal quarterly cash installments of $0.75000 per amortizing note (except for the July 30, 2019 installment payment, which will be $0.80833 per amortizing note), that will constitute a payment of interest and a partial repayment of principal, and which cash payment in the aggregate will be equivalent to 6.00% per year with respect to each $50 stated amount of the Units. The amortizing notes represent unsecured senior obligations of the Company.

The issuance of the common stock and the Units (including the component stock purchase contracts and amortizing notes) were separate public issuances made by means of separate prospectus supplements pursuant to the Company's universal "pay as you go" shelf registration statement, filed with the SEC in February 2018, which allows for the potential future offer and sale by us, from time to time, in one or more public offerings, of an indeterminate amount of the Company's common stock, preferred stock, debt securities, and other securities specified therein at indeterminate prices.

The Company expects to record the issuance of the purchase contract portion of the Units as additional paid-in-capital of $570,919, less estimated allocable issuance costs of $13,446, in our financial statements. The Company also expects to record the amortizing notes portion of the Units of $119,081 as long-term debt and to record estimated allocable issuance costs of $2,805 as debt issuance costs.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

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(UNAUDITED)

Long-term Debt

Subsequent to the quarterly period ended March 31, 2019, on April 26, 2019, the Company issued $900,000 of long-term debt (the “Senior Notes”), less estimated expenses of $9,147, of which $400,000 is due in 2029, and $500,000 is due in 2049 with interest rates of 3.566% and 4.276%, respectively.

The issuance of the Senior Notes was not conditioned upon the consummation of the Peoples Gas Acquisition; however, if (1) the Peoples Gas Acquisition has not been consummated on or prior to April 22, 2020, (2) on or prior to the April 22, 2020 and prior to the consummation of the Peoples Gas Acquisition, the Acquisition Agreement is terminated or (3) prior to the consummation of the Peoples Gas Acquisition, the Company otherwise publicly announces that the acquisition will not be consummated, then the Company will be required to redeem all outstanding Senior Notes on a special mandatory redemption date at a special mandatory redemption price equal to 101% of the aggregate principal amount of the notes, plus accrued and unpaid interest thereon, if any, to, but excluding, the special mandatory redemption date.

The Company intends to use the net proceeds from the issuance of Senior Notes, together with the net proceeds from the common stock offering and tangible equity unit offering noted above, as well as the proceeds from the Private Placement of common stock noted above, to (1) fund the Peoples Gas Acquisition, (2) complete the redemption of $313,500 aggregate principal amount of certain of the Company’s outstanding notes noted below, (3) pay related costs and expenses, and (4) for general corporate purposes. Upon consummation of the Private Placement, the permanent financing for the Peoples Gas Acquisition will be complete.

On May 18, 2019, the Company expects to redeem $313,500 of the Company’s outstanding notes (the “Company Debt Refinancing”) that have maturities ranging from 2019-2037 and interest rates ranging from 3.57-5.83%. Additionally, the Company Debt Refinancing is subject to a make whole payment of approximately $25,000.

If for any reason the Peoples Gas Acquisition is not consummated, the Company intends to use the net proceeds from these financings, after the special mandatory redemption noted above, for general corporate purposes, which may include the redemption of certain of the Company's outstanding notes, repurchases of the Company's common stock, debt repayment, capital expenditures, and investments.

Note 7 – Interest Rate Swap Agreements

In October 2018, the Company entered into interest rate swap agreements to mitigate interest rate risk associated with an anticipated $850,000 of future debt issuances to fund a portion of the Peoples Gas Acquisition and refinance a portion of the Company's borrowings. The interest rate swaps do not qualify for hedge accounting and any changes in the fair value of the swaps was included in our earnings. The interest rate swaps were classified as financial derivatives used for non-trading activities. Other than the interest rate swaps, the Company has no other derivative instruments. The Company recorded the fair value of the interest rate swaps by discounting the future net cash flows associated with the debt issuance and recognized either an asset or liability at the balance sheet date.

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The following table provides a summary of the fair value of our interest rate swap agreements:

	Derivative Assets		Derivative Liabilities	
	March 31,		March 31,	
	Balance Sheet Location	2019	Balance Sheet Location	2019
Derivatives not designated as hedging instrument:				
Interest rate swaps	Current assets	$ -	Current liabilities	$ 94,561

The following table provides a summary of the amounts recognized in earnings for our interest rate swap agreements:

		Amount of Gain (Loss) Recognized in Income on Derivatives Three Months Ended March 31,
	Location of Gain (Loss) Recognized	2019
Derivatives not designated as hedging instrument:		
Interest rate swaps	Other (expense) income	$ (34,782)

Subsequent to the quarterly period ended March 31, 2019, on April 24, 2019, the Company settled the interest rate swap agreements upon issuance of $900,000 of long-term debt used to finance a portion of the purchase price of the Peoples Gas Acquisition. The settlement resulted in a payment by the Company of $83,520.

Note 8 – Financial Instruments

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

- Level 1: unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access;
- Level 2: inputs other than Level 1 that are observable, either directly or indirectly, such as quoted market prices in active markets for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in non-active markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; or
- Level 3: inputs that are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used

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need to maximize the use of observable inputs and minimize the use of unobservable inputs. There have been no changes in the valuation techniques used to measure fair value, or asset or liability transfers between the levels of the fair value hierarchy for the quarter ended March 31, 2019.

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

The fair value of loans payable is determined based on its carrying amount and utilizing Level 1 methods and assumptions. As of March 31, 2019, and December 31, 2018, the carrying amount of the Company’s loans payable was $32,563 and $15,449, respectively, which equates to their estimated fair value. The fair value of the interest rate swap agreements was determined by discounting the future net cash flows utilizing level 2 methods and assumptions. As of March 31, 2019 and December 31, 2018, the fair value of the Company’s interest rate swap agreements represented a liability of $94,561 and $59,779, respectively. The fair value of cash and cash equivalents, which is comprised of uninvested cash, is determined based on the net asset value per unit utilizing Level 1 methods and assumptions. As of March 31, 2019, and December 31, 2018, the carrying amounts of the Company's cash and cash equivalents was $4,053 and $3,627, respectively, which equates to their fair value. The Company’s assets underlying the deferred compensation and non-qualified pension plans are determined by the fair value of mutual funds, which are based on quoted market prices from active markets utilizing Level 1 methods and assumptions. As of March 31, 2019, and December 31, 2018, the carrying amount of these securities was $22,068 and $20,388, respectively, which equates to their fair value, and is reported in the consolidated balance sheet in deferred charges and other assets.

Unrealized gain and losses on equity securities held in conjunction with our non-qualified pension plan is as follows:

	Three Months Ended

	March 31,	
	2019	2018
Net gain recognized during the period on equity securities	$ 133	$ 21
Less: net gain / loss recognized during the period on equity securities sold during the period	-	-
Unrealized gain recognized during the reporting period on equity securities still held at the reporting date	$ 133	$ 21

The net gain recognized on equity securities is presented on the consolidated statements of operations on the line item "Other."

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