

making

CONNECTICUT WATER

Water

2016 ANNUAL REPORT

work



Carol P. Wallace
Lead Independent Director



Judy E. Wallingford, recently retired President of Maine Water, at Mirror Lake in Rockport, Maine. Through Judy's stewardship 1,400 acres of watershed land around Mirror Lake are being permanently protected.



Maureen P. Westbrook
Vice President,
Customer and Regulatory Affairs



Jen
Senior Manager of
Program Management



Kay Ann
Customer Account Analyst



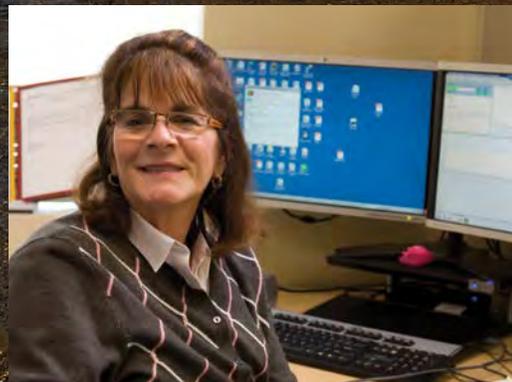
Pam
Customer Service Manager



Marissa
Water Treatment Plant Operator



Joann
Billing Specialist



Kim
Customer Service



Allison
Senior Financial Analyst



Vilmarie
Water Operator



Denise
Capital Planning Manager



Kristen
Senior Water Treatment Plant Operator



Kristen A. Johnson
Vice President, Human Resources
and Corporate Secretary

■ **Connecticut Water**

is committed to fostering socially responsible programs and policies that enhance sustainability efforts. We strive to be good stewards of the environment and to manage our resources in a manner that promotes water and energy conservation, source protection and preservation.

Financial Highlights

Years Ended December 31,	2016	2015	% Change
Financials (in thousands)			
Operating Revenues	\$ 98,667	\$ 96,041	2.7%
Total Revenues	\$105,316	\$103,088	2.2%
Gain (Loss) on Real Estate Transactions, Net of Taxes	\$ (54)	\$ 349	-
Non-Water Sales Earnings, Net of Taxes	\$ 1,219	\$ 1,394	-12.6%
Net Income	\$ 23,387	\$ 22,761	2.8%
Common Stock (per share)			
Basic Earnings per Average Share	\$ 2.12	\$ 2.07	2.4%
Stock Price (end of year)	\$ 55.85	\$ 38.01	46.9%
Dividends Declared	\$ 1.115	\$ 1.050	6.2%
Book Value per Common Share (end of year)	\$ 20.98	\$ 20.01	4.8%
Operations			
Number of Customers (end of year)	124,968	123,633	1.1%
Number of Employees (end of year)	266	266	0.0%

Dear Shareholders,

It was truly a privilege to lead our company in 2016.

Results proved that 2016 was a good year for our shareholders and customers. Our 2016 total return to shareholders was 50.4% on the strength of a 46.9% appreciation in stock price over the year coupled with a 6.2% increase in our quarterly common stock dividend. We have now raised our quarterly dividend for 47 years in a row. We are also pleased that 2016 was our 16th straight year of achieving high levels of customer satisfaction.

2016 Financial Results

In 2016, net income grew to \$23.4 million, and basic earnings per share grew 2.4%, to \$2.12. Total revenues were \$105.3 million, a 2.2% increase from 2015. In every year since 2012, and in nine out of the last 10 years, our closing share price at year-end has been higher than it was at the previous year-end.

We deliver solid results like these because of the growth strategy we follow, which consists of the following elements:

- ongoing investment in infrastructure to enhance service reliability and water quality for our customers;
- prudent acquisitions of other water and wastewater utilities (public and private) to expand our service areas; and
- continued development of strong non-regulated utility businesses.

Infrastructure Investment

During 2016, we invested \$66.4 million to improve our infrastructure. Upgrading our pipelines and plant across Connecticut and Maine, and seeking recovery of those investments through regular rate adjustments, are at the core of our earnings growth strategy.

Both states have programs that allow for timely recovery of eligible infrastructure improvement costs between general rate cases. Connecticut's program is called the Water Infrastructure and Conservation Adjustment (WICA), and Maine's is called the Water Infrastructure Charge (WISC). In almost all cases, our regulators must review and authorize eligible projects before the work can begin. While the two states have different project eligibility criteria, each allows investment costs to be recovered through a surcharge on customer bills that can be adjusted twice a year. Last year, about one-third of our capital spending, or \$21.0 million, was invested in projects eligible under these two programs. We expect to fully recover those investments.

In Connecticut, where WICA has been in place since 2007, we have replaced more than 100 miles of aging pipe, or about 6% of our distribution system piping. The replaced pipe had an average age of 75 years. Maine's WISC program has been in effect since 2014. During that time, we have used the program to replace 12 miles of aging water mains, upgrade two pump stations, construct a three-million-gallon storage tank, replace IT systems and fund treatment improvements.

The upgrades we make improve service reliability and water quality and reduce the amount of water lost to leaks. We estimate that in 2016, we saved more than 205 million gallons of water in Connecticut and Maine through targeted leak detection efforts and infrastructure replacement projects. Reducing water lost to leaks also saves the energy used to pump and treat the lost water and the treatment additives. For 2017, the Board of Directors has approved a \$55.4 million capital spending plan. About 40%, or \$22.2 million, has been allocated to WICA- and WISC-eligible projects.

Of the \$33.2 million allocated to non-WICA and non-WISC projects, \$13.9 million will go toward completion of a major upgrade of the treatment process at our Rockville Water

Treatment Facility (RWTF) in Connecticut and toward preliminary work on the construction of a new Saco River Water Treatment Facility (SRWTF) in Biddeford, Maine. The RWTF upgrade should be completed by June 2017.

Both projects are generational investments that will enhance water quality and service reliability for years to come.

The RWTF is our oldest surface water treatment facility in Connecticut, having gone online in 1970. Preliminary planning and design work is being done for the SRWTF, which will replace the existing Biddeford Water Treatment Facility that went online in 1884. At 133 years of age, the Biddeford plant may be the oldest surface water treatment facility still in operation in the nation. The new facility will be supplied by the Saco River just as the current facility is, but it will be located out of the flood zone. In addition to serving our customers, the SRWTF, which we expect to be online by 2020, will likely benefit many neighboring communities as well.

Acquisitions and Service Area Growth

Since January 2012, Connecticut Water has grown its customer base by 44%, or nearly 40,000 customers, primarily through large acquisitions in both Maine and Connecticut. This includes the recently completed acquisition of the Heritage Village Water Company (HVWC), which added 4,700 water customers in the Connecticut towns of Southbury, Middlebury and Oxford, and 3,000 wastewater customers in Southbury. We expect to gain an additional 4,800 customers by the third quarter of 2017 through the acquisition of the Avon Water Company (AWC).

The acquisition of the Southbury based HVWC with a total enterprise value of \$20.7 million, was completed in February 2017. HVWC's wastewater utility is the only investor-owned wastewater utility regulated by the Connecticut Public Utilities Regulatory Authority (PURA), and it is the first to be owned by Connecticut Water. We are eager to serve these new customers and establish Connecticut Water as a trusted wastewater utility.

The planned acquisition of AWC, with a total enterprise value of approximately \$36.6 million, was announced in October. AWC serves 4,800 customers in the Connecticut towns of Avon, Farmington and Simsbury and will be a great addition to our company. We are currently in the process of securing PURA approval for the acquisition. Our team will focus on operating these latest acquisitions efficiently to create value while providing world-class customer service, a reliable supply of high-quality water, and dependable wastewater service.

Besides seeking acquisitions of larger water systems such as HVWC and AWC, we will continue to pursue smaller "tuck-in" water systems where we can similarly create long-term value by enhancing efficiency.

Our service territory now includes the important growth area around the University of Connecticut (UConn) in Storrs. We completed our five-mile-long pipeline project in 2016, and, as part of our agreement with UConn and the Town of Mansfield, we acquired approximately 300 customers in the Storrs Center area that were formerly customers of UConn. The pipeline will support both UConn's anticipated growth and growth in Mansfield itself.



**Eric W. Thornburg,
Chairman,
President and
Chief Executive Officer**

Non-Regulated Businesses

We achieve earnings not only through our regulated utility operations but also through non-regulated, low-risk ventures that are related to our core business but involve little or no capital investment. These ventures make up our Services and Rentals segment.

In 2016, the segment generated \$5.3 million in revenue and \$1.2 million in net income—or 5.2% and 5.4%, respectively, of our total revenues and earnings (the segment's income contribution is shown in the Consolidated Statements of Income as "Non-Water-Sales Earnings"). The most significant of the businesses are the utility operating services we provide under contract to municipalities and other water systems, and the Linebacker® program that covers the cost of repairing broken or leaking water or wastewater lines and household plumbing.

These businesses are a good strategic fit and help us to build our brand and serve customers and communities.

World-Class Service

Each year, we conduct a survey to measure our customers' perception of the service they have received, and in our 2016 survey, we again achieved world-class customer satisfaction levels. Our year-end Customer Satisfaction Index (CSI) average was an outstanding 92.3%. We have achieved a CSI of 85.0% or better for each of the past 16 years.

Dedication to superior customer service has taken firm root in our culture. Achieving this result in 2016 was especially gratifying since continuing publicity about the tragic lead contamination of drinking water in Flint, Michigan, had the potential to undermine customer confidence in water utilities across the nation. As you may know, the predominant source

of lead in drinking water comes from plumbing and fixtures owned by customers.

The crisis in Flint brought attention to the risks of lead in drinking water, and our team gave personal care to any customer who was concerned about lead. Further, we voluntarily reached out to all of the public schools we serve and offered to test water fountains and faucets in food preparation areas at no cost. Many schools took us up on our offer, giving the administrators in these schools access to real data. Some schools have already used the data to replace problem fixtures in their buildings.

Our culture of service also extends to our communities. Over the past several years, our employees have organized and participated in a wide variety of community events. They have held watershed cleanups, tag sales and coat and food drives to benefit those in our communities who can use a helping hand. In 2016, we launched a day-of-service initiative so that our people could share a few hours of their talents in the community during work time. The project was well received and will be continued in 2017.

Environmental Stewardship

In 2016, we held the Water Drop Challenge in Connecticut. We provided the nearly 5,000 residential customers who enrolled in the challenge with monthly water conservation tips via e-mail to help them lower their water usage. Those who reduced their billed usage by 10% from the 2015 level earned a one-time credit on their water bills. The program was a success, and customers who met the goal saved approximately 30.2 million gallons of water in 2016. We continue to look for additional innovative ways to promote water conservation.

Some Closing Thoughts

In 2016, The Connecticut Water Company celebrated its 60th year. Since its founding, Connecticut Water and its employees have earned a reputation for building reliable, sustainable water systems and for being committed to customer satisfaction. We look forward to building on that legacy.

Our conservative approach to financial management delivers consistent performance, high earnings quality, a robust balance sheet and a strong dividend yield.

According to Standard & Poor's (S&P), our cumulative total return to shareholders (assuming reinvestment of dividends) was 138.5% for the five-year period 2012 to 2016, and 50.4% for 2016. We paid \$1.115 in dividends per common share in 2016, for a dividend yield of 2.0% as of year-end 2016. Since our founding in 1956, we have paid a dividend for 243 consecutive quarters, or 60 years, without interruption or reduction, and we have raised our dividend for 47 consecutive years.

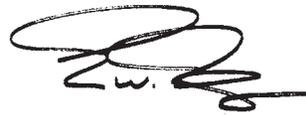
In 2016, Connecticut Water was one of just 14 NASDAQ-listed companies to be recognized by NASDAQ for gender parity on its Board. Five of the eight directors on our Board are women. We are proud of NASDAQ's recognition. Outside the Board, women are playing other vital roles throughout the company—as executives (a subsidiary president and two vice presidents), as field service personnel, as water treatment plant operators, in the accounting and IT departments and in many other areas. Women achieved these positions because they were the best candidates, they embodied our culture, and they did their jobs well. The front and back covers of this report feature the faces of more than 200 men and women who passionately serve customers and each other. Having a workforce that represents the families and communities we serve makes us a better organization.

I would like to recognize Judy Wallingford for her groundbreaking career in the industry. Judy had been President of Maine Water, and its predecessor companies, since 1993 – a time when very few women held such roles in our industry. Judy retired on March 31, 2017, having served with distinction. Recently, the Maine Water Utilities Association bestowed on Judy its Lifetime Achievement Award to recognize her passion and dedication to the drinking water field. We thank her for her leadership and service.

I also want to thank our Board of Directors for their support in 2016. Once again our Lead Director, Carol Wallace, was extremely helpful to me, offering valuable advice and encouragement.

On behalf of the Board and my colleagues at the Connecticut, Maine and Heritage Village water companies, I thank you for your support. We look forward to another successful year.

All the best!



Eric W. Thornburg

Chairman, President and Chief Executive Officer

Directors and Committees

Age as of May 11, 2017, in parentheses, followed by 2016 committee memberships

Richard Forde (63) 2, 3, 4	Retired; former Senior Vice President and Chief Investment Officer of Cigna Corporation; Trustee of Bates College
Mary Ann Hanley (60) 1, 3	An attorney; Assistant to the President of St. Francis Hospital and Medical Center; Director, The Valencia Society (endowment fund)
Heather Hunt (51) 2, 3	An attorney; Executive Director of the New England States' Committee on Electricity
Bradford A. Hunter (61) 3, 4	Retired; former Chief Financial Officer of Dead River Company; Trustee of Bowdoin College
Lisa J. Thibdaue (64) 1, 2	Retired; former Vice President, Rates, Regulatory Affairs and Compliance, Northeast Utilities
Eric W. Thornburg (57)	Chairman of the Board, President and Chief Executive Officer of the Company
Carol P. Wallace (62) 2, 3, 4	Lead Director; President and Chief Executive Officer of Cooper-Atkins Corporation (temperature acquisition instruments manufacturer)
Ellen C. Wolf (63) 2, 4	Retired; former Senior Vice President and Chief Financial Officer of American Water Works Company, Inc.

Officers

Eric W. Thornburg	Chairman of the Board, President and Chief Executive Officer
David C. Benoit	Senior Vice President, Chief Financial Officer and Treasurer
Richard L. Knowlton	Division President, The Maine Water Company
Kristen A. Johnson	Vice President, Human Resources and Corporate Secretary
Craig J. Patla	Vice President, Service Delivery
Maureen P. Westbrook	Vice President, Customer and Regulatory Affairs
Peter J. Bancroft	Assistant Treasurer and Director, Rates and Forecasting
Robert J. Doffek	Controller

- 1 Audit Committee appoints, compensates and oversees the work of the independent auditors of the Company and subsidiaries and monitors the Company's financial reporting process and internal controls system; and oversees the Company's enterprise risk management and cyber security initiatives.
- 2 Compensation Committee determines officer compensation and the promotion and hiring of officers; reviews Company fringe benefit plans other than retirement plans; and administers the performance stock programs.
- 3 Corporate Governance Committee reviews the qualifications and independence standards of director nominees and makes recommendations to the Board; oversees the Company's succession planning process; and reviews the overall effectiveness of the Board.
- 4 Corporate Finance and Investments Committee reviews the Pension Trust Fund of The Connecticut Water Company Employees' Retirement Fund, the Connecticut Water Company Savings Plan (401(k)), the Connecticut Water Company Welfare Benefits Plan for Retirees for retiree medical benefits, and the Supplemental Executive Retirement Program; reviews and determines actuarial policies and investment guidelines; selects the investment managers; makes recommendations to and advises the Board on financial policy and issuance of securities; and assists in the evaluation of proposed merger and acquisition transactions.

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

Form 10-K

- Annual Report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended **December 31, 2016** or
- Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period to _____ from _____

Commission File Number **0-8084**



Connecticut Water Service, Inc.
(Exact name of registrant as specified in its charter)

Connecticut
(State or other jurisdiction of
incorporation or organization)

93 West Main Street, Clinton, CT
(Address of principal executive office)

06-0739839
(I.R.S. Employer Identification No.)

06413
(Zip Code)

Registrant's telephone number, including area code **(860) 669-8636**
Registrant's website: www.ctwater.com

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

Title of each Class
Common Stock, without par value

Name of each exchange on which registered
The Nasdaq Stock Market, LLC

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes No

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 twelve (12) months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (Section 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large Accelerated Filer
Non-Accelerated Filer

Accelerated Filer
Smaller Reporting Company

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

As of June 30, 2016, the aggregate market value of the registrant's voting Common Stock held by non-affiliates of the registrant was \$619,633,255 based on the closing sale price on such date as reported on the NASDAQ.

Number of shares of Common Stock, no par value, outstanding as of February 1, 2017 was 11,258,790, including 227,673 common stock equivalent shares.

DOCUMENTS INCORPORATED BY REFERENCE

Document	Part of Form 10-K Into Which Document is Incorporated
Definitive Proxy Statement, to be filed on or about March 30, 2017, for Annual Meeting of Shareholders to be held on May 11, 2017.	Part III

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

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

- projected capital expenditures and related funding requirements;
- the availability and cost of capital;
- developments, trends and consolidation in the water and wastewater utility industries;
- dividend payment projections;
- our ability to successfully acquire and integrate regulated water and wastewater systems, as well as unregulated businesses, that are complementary to our operations and the growth of our business;
- the capacity of our water supplies, water facilities and wastewater facilities;
- the impact of limited geographic diversity on our exposure to unusual weather;
- the impact of conservation awareness of customers and more efficient plumbing fixtures and appliances on water usage per customer;
- our capability to pursue timely rate increase requests;
- our authority to carry on our business without unduly burdensome restrictions;
- our ability to maintain our operating costs at the lowest possible level, while providing good quality water service;
- our ability to obtain fair market value for condemned assets;
- the impact of fines and penalties;
- changes in laws, governmental regulations and policies, including environmental, health and water quality and public utility regulations and policies;
- the decisions of governmental and regulatory bodies, including decisions to raise or lower rates;
- our ability to successfully extend and expand our service contract work within our Service and Rentals Segment in both Connecticut and Maine;
- the development of new services and technologies by us or our competitors;
- the availability of qualified personnel;
- the condition of our assets;
- the impact of legal proceedings;
- general economic conditions;
- the profitability of our Real Estate Segment, which is subject to the amount of land we have available for sale and/or donation, the demand for any available land, the continuation of the current state tax benefits relating to the donation of land for open space purposes and regulatory approval for land dispositions;
- the amount of repair tax deductions and the Internal Revenue Service’s ultimate acceptance of the deduction methodology;
- delays in completing the merger with The Avon Water Company, or difficulties in achieving anticipated benefits or cost savings from the merger; and
- acquisition-related costs and synergies.

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

- changes in public utility regulations and policies;
- changes in general economic, business, credit and financial market conditions;
- changes in environmental conditions, including those that result in water use restrictions;
- the determination of what qualifies for a repair expense tax deduction;
- abnormal weather conditions;
- increases in energy and fuel costs;
- unfavorable changes to the federal and/or state tax codes;
- significant changes in, or unanticipated, capital requirements;

- significant changes in our credit rating or the market price of our common stock;
- our ability to integrate businesses, technologies or services which we may acquire;
- our ability to manage the expansion of our business;
- the continuous and reliable operation of our information technology systems, including the impact of cyber security attacks or other cyber-related events;
- the extent to which we are able to develop and market new and improved services;
- the continued demand by telecommunication companies for antenna site leases on our property;
- the effect of the loss of major customers;
- our ability to retain the services of key personnel and to hire qualified personnel as we expand;
- labor disputes;
- increasing difficulties in obtaining insurance and increased cost of insurance;
- cost overruns relating to improvements or the expansion of our operations;
- increases in the costs of goods and services;
- civil disturbance or terroristic threats or acts; and
- changes in accounting pronouncements.

Given these uncertainties, you should not place undue reliance on these forward-looking statements. You should read this 10-K and the documents that we incorporate by reference into this 10-K completely and with the understanding that our actual future results, performance and achievements may be materially different from what we expect. These forward-looking statements represent our assumptions, expectations and beliefs only as of the date of this 10-K. Except for our ongoing obligations to disclose certain information under the federal securities laws, we are not obligated, and assume no obligation, to update these forward-looking statements, even though our situation may change in the future. For further information or other factors which could affect our financial results and such forward-looking statements, see Part I, Item 1A “Risk Factors.” We qualify all of our forward-looking statements by these cautionary statements.

PART I

ITEM 1. BUSINESS

The Company

The Registrant, Connecticut Water Service, Inc. (referred to as “the Company”, “we”, “us”, or “our”) was incorporated in 1974, with The Connecticut Water Company (“Connecticut Water”) as its largest subsidiary which was organized in 1956. Connecticut Water Service, Inc. is a non-operating holding company, whose income is derived from the earnings of its five wholly-owned subsidiary companies as of December 31, 2016. In 2016, approximately 95% of the Company’s net income was attributable to water operations carried out within its regulated water companies, Connecticut Water and The Maine Water Company (“Maine Water”), together the “Regulated Companies”. As of December 31, 2016, the Regulated Companies supplied water to 124,968 customers, representing a population of approximately 400,000, in 77 municipalities throughout Connecticut and Maine. The Regulated Companies are subject to state regulation regarding financial issues, rates, and operating issues, and to various other state and federal regulatory agencies concerning water quality and environmental standards.

In addition to its Regulated Companies, the Company owns two active unregulated companies. In 2016, these unregulated companies, together with real estate transactions within Connecticut Water, contributed the remaining 5% of the Company’s net income through real estate transactions as well as services and rentals. The two active unregulated companies are Chester Realty, Inc., a real estate company in Connecticut; and New England Water Utility Services, Inc. (“NEWUS”), which provides contract water and sewer operations and other water related services.

Our mission is to provide high quality water service to families and communities at a fair return to our shareholders while maintaining a work environment that attracts, retains and motivates our employees to achieve a high level of performance.

Our corporate headquarters are located at 93 West Main Street, Clinton, Connecticut 06413. Our telephone number is (860) 669-8636, and our Internet address is www.ctwater.com. The references to our Web site and the Securities and Exchange Commission’s (“SEC”) website are intended to be inactive textual references only, and the contents of those Web sites are not incorporated by reference herein and should not be considered part of this or any other report that we file with or furnish to the SEC.

The Company’s annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements and all amendments to these documents will be made available free of charge through the “INVESTORS” section of the Company’s Internet website (www.ctwater.com) as soon as practicable after such material is electronically filed with, or furnished to, the SEC. The following documents are also available through the “INVESTORS” section of our website, under the “Corporate Governance” tab:

- Board of Directors Code of Conduct
- Compensation Committee Charter
- Corporate Finance and Investments Committee Charter
- Corporate Governance Committee Charter
- Bylaws of Connecticut Water Service, Inc.
- Employee Code of Conduct
- Audit Committee Charter

Additionally, information concerning the Company’s 2017 Annual Meeting Materials (2016 Annual Report and 2017 Proxy Statement) can be found under the “INVESTORS” menu, under the “Investor Resources” tab when the Annual Meeting Materials are filed with the SEC on or about March 30, 2017.

Copies of each of the Company’s SEC filings (without exhibits) and corporate governance documents mentioned above will also be mailed to investors, upon request, by contacting the Company’s Corporate Secretary, Kristen A. Johnson, at Connecticut Water, 93 West Main Street, Clinton, CT 06413.

Our Regulated Companies

Our Regulated Companies are subject to seasonal fluctuations and weather variations. The demand for water is generally greater during the warmer months than the cooler months due to customers' incremental water consumption related to cooling systems and various outdoor uses such as private and public swimming pools and lawn sprinklers. Demand will vary with rainfall and temperature levels from year to year and season to season, particularly during the warmer months. The financial risk associated with changes in demand was mitigated in the State of Connecticut due to the adoption of the Water Revenue Adjustment ("WRA") by Connecticut Water in 2013.

In general, the profitability of the water utility industry is largely dependent on the timeliness and adequacy of rates allowed by utility regulatory commissions. In addition, profitability is affected by numerous factors over which we have little or no control, such as costs to comply with security, environmental, and water quality regulations. Inflation and other factors also impact costs for construction, materials and personnel related expenses.

The Company believes that we are presently in compliance with current environmental and water quality regulations, but the regulations are subject to change at any time. The costs to comply with future changes in state or federal regulations, which could require us to modify existing filtration facilities and/or construct new ones, or to replace any reduction of the safe yield from any of our current sources of supply, could be substantial.

Regulatory Matters

The rates we charge our water customers in Connecticut and Maine are established under the jurisdiction of and are approved by the Connecticut Public Utilities Regulatory Authority ("PURA") and the Maine Public Utilities Commission ("MPUC"), respectively. It is our policy to seek rate relief as necessary to enable us to achieve an adequate rate of return. Connecticut Water's allowed return on equity and return on rate base, effective as of December 31, 2016 were 9.75% and 7.32%, respectively. Maine Water's average allowed return on equity and return on rate base, as of December 31, 2016 were 9.50% and 7.96%, respectively. The PURA establishes rates in Connecticut on a company-wide basis while the MPUC approves Maine Water's rates on a division-by-division basis. Both Connecticut Water and Maine Water are permitted to add surcharges to customers' bills in order to recover certain approved capital projects in between full rate cases, as well as approved surcharges for Water Revenue Adjustments in Connecticut, as discussed in more detail below.

Heritage Village Water Company Acquisition

On May 10, 2016, the Company announced that it had reached an agreement to acquire The Heritage Village Water Company ("HVWC"), pending a vote of HVWC shareholders, approval by PURA and MPUC and the satisfaction of other various closing conditions, pursuant to the terms of that certain Agreement and Plan of Merger dated May 10, 2016 between and among HVWC, the Company, and HAC, Inc., the Company's wholly-owned Maine subsidiary (the "Merger Agreement"). HVWC serves approximately 4,700 water customers in the Towns of Southbury, Middlebury, and Oxford, Connecticut and approximately 3,000 wastewater customers in the Town of Southbury, Connecticut.

Under the Merger Agreement, the acquisition was agreed to be executed through a stock-for-stock merger transaction valued at approximately \$16.1 million. Holders of HVWC common stock will receive shares of the Company's common stock in a tax-free exchange. In addition the transaction reflects a total enterprise value of HVWC of approximately \$20.7 million.

The Company received regulatory approval from MPUC on September 28, 2016 and from PURA on December 5, 2016, to proceed with the transaction. The shareholders of HVWC voted to approve the acquisition at a special meeting of HVWC's shareholders held on February 27, 2017.

On February 27, 2017, the Company completed the acquisition of HVWC by completing the merger of Connecticut Water's wholly-owned subsidiary HAC, Inc. with and into HVWC, with HVWC as the surviving corporation, pursuant to the terms of the Merger Agreement and Connecticut corporate law. Upon the effective time of the Merger, the holders of HVWC's 1,620 issued and outstanding shares of common stock became entitled to receive an aggregate of 300,445 shares of the Company's common stock in a tax-free exchange, which exchange was commenced by the issuance of a letter of transmittal and related materials by Connecticut Water's exchange agent.

Avon Water Company Acquisition

On October 11, 2016, the Company entered into an Agreement and Plan of Merger (the "Avon Agreement") with The Avon Water Company, a specially-chartered Connecticut corporation ("Avon Water"). Founded in 1911, Avon Water serves about 4,800 customers in the Farmington Valley communities of Avon, Farmington, and Simsbury, Connecticut, and is located near Connecticut Water's existing operations in Avon and Farmington.

The Boards of Directors of the Company and Avon Water have each unanimously approved the Avon Agreement and the transactions contemplated thereby. Consummation of the merger is subject to regulatory, Avon Water shareholder and other specified approvals described below and is expected to be consummated by the end of the third quarter of 2017.

Under the terms of the Avon Agreement, each of the 121,989 Avon Water common stock shares outstanding at the time of the closing of the merger will be exchanged and converted into the right to receive the following merger consideration: (i) a cash payment of \$50.37; and (ii) a stock consideration component, consisting of 4.38 shares of Company Common Stock, provided that the Company's Share Price (as defined below) over a specified period prior to the closing date of the merger is equal to or greater than \$45.00 but less than or equal to \$52.00. If the Company's Share Price is less than \$45.00 as of the closing date, each share of Avon Water common stock issued and outstanding at the time of the closing of the merger will be exchanged and converted into the right to receive that number of shares of Company Common Stock equal to 197.10 divided by the Company's Share Price, rounded to the nearest hundredth. If the Company's Share Price is more than \$52.00 as of the closing date, each share of Avon Water common stock issued and outstanding at the time of the closing of the merger will be exchanged and converted into the right to receive that number of shares of Company Common Stock equal to 227.76 divided by the Company's Share Price, rounded to the nearest hundredth. The "Company's Share Price" is determined by calculating an average of the closing prices for shares of the Company's Common Stock on the Nasdaq Stock Market, LLC for the twenty trading days immediately preceding the third business day prior to the closing of the Merger. Holders of Avon Water common stock prior to the Merger will receive cash in lieu of fractional shares of Company Common Stock.

The Avon Agreement contains customary representations and warranties regarding, on the one hand, Avon Water, its business and operations and related matters, and, on the other hand, the Company, made by the parties as of specified dates, and customary affirmative and negative covenants with respect to the conduct of Avon Water's business prior to the closing. In the Avon Agreement, Avon Water has agreed that its Board of Directors will, subject to certain exceptions, recommend adoption of the Avon Agreement by Avon Water shareholders and the transactions contemplated by the Avon Agreement. Avon Water has also agreed: (i) to cause a special meeting of shareholders of Avon Water to be held to consider the approval and adoption of the Agreement and the transactions contemplated thereby; and (ii) not to solicit proposals relating to alternative business combination transactions or, subject to certain exceptions, enter into discussions concerning confidential information in connection with alternative business combination transactions.

The obligation of the parties to complete the merger is subject to the satisfaction or waiver on or prior to the closing date of certain specified conditions, including the following: (i) receipt of final and non-appealable orders from each of PURA and the MPUC approving the merger in form and substance reasonably acceptable to the parties; (ii) approval of the merger by the affirmative vote of the holders of not less than two-thirds (66 2/3rd %) Avon Water's issued and outstanding shares of common stock as required under the Connecticut Business Corporation Act; (iii) the receipt of all other necessary consents or approvals to the merger; (iv) approval for listing of the Company Common Stock to be issued in the merger on the Nasdaq Stock Market, LLC; (v) the absence of laws, orders, judgments and injunctions that restrain, enjoin or otherwise prohibit consummation of the Merger; (vi) effectiveness under the Securities Act of the Company's registration statement on Form S-4 relating to the issuance of the Company Common Stock in the merger and absence of any stop order in respect thereof or proceedings by the SEC for that purpose; (vii) the receipt of a legal opinion from counsel to Avon Water regarding certain corporate law matters; (viii) the receipt of a customary tax opinion from counsel to the Company that will state that the merger will qualify as a tax-free reorganization within the meaning of Section 368(a) of the Internal Revenue Code of 1986; (ix) the accuracy of representations and warranties with respect to the businesses of Avon Water and the Company and compliance by Avon Water and the Company with their respective covenants contained in the Avon Agreement; (xi) no event(s) occurring that could reasonably be expected to result in either a "Company Material Adverse Effect" or a "CWS Material Adverse Effect" (each, as defined in the Avon Agreement) and (xii) holders of no more than 5% of Avon Water's common stock have exercised appraisal rights under Connecticut law.

The Avon Agreement contains certain termination rights for both the Company and Avon Water and further provides that, in connection with the termination of the Avon Agreement under specified circumstances, Avon Water may be required to pay to the Company, or the Company may be required to pay to Avon Water, a termination fee of \$200,000 in cash, as liquidated damages.

During the fourth quarter of 2016, Connecticut Water filed an application with PURA seeking approval of the transaction, which the Company expects to receive in April 2017.

Connecticut Rates

In Connecticut, the Water Infrastructure Conservation Adjustment (“WICA”) was 7.13%, 4.19% and 1.59% above base rates at December 31, 2016, 2015, and 2014, respectively. On January 26, 2017, Connecticut Water filed a WICA application with the PURA requesting a 1.09% surcharge to customers’ bills, representing approximately \$8.5 million in WICA related projects. Additionally, on February 9, 2017, Connecticut Water filed its annual WICA reconciliation which requested a 0.06% surcharge, which would replace the 0.03% reconciliation adjustment filed in January 2016. If approved as filed, Connecticut Water’s cumulative WICA surcharge, effective April 1, 2017, will be 8.25%.

Since 2013, Connecticut law has authorized a Water Revenue Adjustment (“WRA”) to reconcile actual water demands with the demands projected in the last general rate case and allows companies to adjust rates as necessary to recover the revenues approved by PURA in the last general rate case. The WRA removes the financial disincentive for water utilities to develop and implement effective water conservation programs. The WRA allows water companies to defer on the balance sheet, as a regulatory asset or liability, for later collection from or crediting to customers the amount by which actual revenues deviate from the revenues allowed in the most recent general rate proceedings, including WICA proceedings. Additionally, projects eligible for WICA surcharges were expanded to include energy conservation projects, improvements required to comply with streamflow regulations, and improvements to acquired systems.

Connecticut Water’s allowed revenues for the year ended December 31, 2016, as approved by PURA during our 2010 general rate case and including subsequently approved WICA surcharges, were approximately \$76.7 million. Through normal billing for the year ended December 31, 2016 operating revenue for Connecticut Water would have been approximately \$75.6 million had the WRA not been implemented. As a result of the implementation of the WRA, Connecticut Water recorded \$1.1 million in additional revenue for the year ended December 31, 2016. During the years ended December 31, 2015 and 2014, Connecticut Water recorded \$1.6 million and \$3.7 million, respectively, in additional revenue related to the WRA.

Maine Rates

In Maine, the overall, approved cumulative Water Infrastructure Charge (“WISC”) for all divisions was 4.7%, 1.6% and 2.0% above base rates as of December 31, 2016, 2015 and 2014, respectively. Two pending WISC filings as of December 31, 2016 have since been approved in the first quarter of 2017, bringing the total to 6.5%.

In 2014 and 2015, Maine Water petitioned the MPUC for approval of accounting orders that would address (1) the return to its customers a federal income tax refund stemming from the adoption of the Internal Revenue Service (“IRS”) Revenue Procedure 2012-19 (“Repair Regulations”), and (2) the treatment of any benefit resulting from the elimination of deferred tax liabilities previously recorded on these qualifying fixed assets that are now deducted under the Repair Regulations.

On February 26, 2015, the MPUC approved a stipulation between Maine Water and the Office of the Public Advocate that refunds \$2.9 million to the customers of the eight divisions over a two-year period starting no later than July 1, 2015, and allows the flow-through treatment of the repair deduction as of January 1, 2014. In addition, Maine Water agreed not to file a general rate case during the two-year refund period in any of the eight divisions that were allowed the refund.

On June 22, 2015, the MPUC approved a settlement agreement between Maine Water and the Office of the Public Advocate that allowed for the amortization of the deferred tax liabilities over a one to nine year period, depending on the division. Maine Water commenced amortization per the agreed upon schedule.

With the completion of these two dockets, Maine Water recorded in the quarter ended June 30, 2015 the retroactive benefit associated with the flow-through of the Repair Regulations from January 1, 2014. The 2014 benefit, reflected in the second quarter of 2015, was approximately \$931,000, or \$0.09 per basic share outstanding.

A newly passed water revenue adjustment mechanism law in Maine became available to regulated water utilities in Maine on October 15, 2015. Maine Water is currently precluded from seeking new rates in certain divisions due to various agreements with the MPUC, but is evaluating how and when this new mechanism can be implemented.

Our Water Systems

As of December 31, 2016, our water infrastructure consisted of 75 noncontiguous water systems in the States of Connecticut and Maine. Our system, in total, consists of approximately 2,100 miles of water main and reservoir storage capacity of 9.4 billion gallons. The safe, dependable yield from our 236 active wells and 25 surface water supplies is approximately 176 million gallons per day. Water sources vary among the individual systems, but overall approximately 80% of the total dependable yield comes from surface water supplies and 20% from wells.

For the year-ended December 31, 2016, our Regulated Companies' 124,968 customers consumed approximately 9.8 billion gallons of water, generating \$98,667,000 in operating revenues. We supply water, and in most cases, fire protection to all or portions of 77 towns throughout Connecticut and Maine.

The following table breaks down the above total figures by customer class as of December 31, 2016, 2015, and 2014:

	2016	2015	2014
Customers:			
Residential	111,494	110,254	109,662
Commercial	8,626	8,569	8,586
Industrial	479	478	484
Public Authority	948	964	943
Fire Protection	2,876	2,815	2,834
Other (including non-metered accounts)	545	553	562
Total	<u>124,968</u>	<u>123,633</u>	<u>123,071</u>
Water Revenues (in thousands):			
Residential	\$ 59,884	\$ 58,439	\$ 57,095
Commercial	12,250	11,816	11,473
Industrial	3,176	3,229	2,984
Public Authority	3,510	3,193	3,215
Fire Protection	18,486	18,016	17,757
Other (including non-metered accounts)	1,361	1,348	1,496
Total	<u>\$ 98,667</u>	<u>\$ 96,041</u>	<u>\$ 94,020</u>
Customer Water Consumption (millions of gallons):			
Residential	6,583	6,551	6,341
Commercial	1,954	1,941	1,865
Industrial	724	777	739
Public Authority	539	503	483
Total	<u>9,800</u>	<u>9,772</u>	<u>9,428</u>

The Regulated Companies own various small, discrete parcels of land that are no longer required for water supply purposes. At December 31, 2016, this land totaled over 600 acres. Over the past several years, we have been disposing of these land parcels through sales and/or donations, primarily to towns and municipalities. For more information, please refer to *Segments of Our Business* below.

Additional information on land dispositions can be found in Item 7 – “Management’s Discussion and Analysis of Financial Conditions and Results of Operations – Commitments and Contingencies”.

University of Connecticut Agreement

Connecticut Water and the University of Connecticut (“UCONN”) negotiated a definitive agreement for Connecticut Water to provide a long-term supply of potable water for UCONN’s Storrs campus facilities which was approved by the Board of Trustees at their December 11, 2013 meeting and executed on December 18, 2013. The definitive agreement is consistent with the requirements of the project’s Environmental Impact Evaluation (“EIE”) and record of decision, as approved by the Office of Policy and Management, an agency of the State of Connecticut, that identified the Company as the preferred option to supply UCONN and the Town of Mansfield, Connecticut with up to 2.2 million gallons of water per day over the next 47 years. Connecticut Water funded a 5-mile pipeline from Tolland and other necessary infrastructure improvements at no cost to UCONN, the Town or the state’s taxpayers to serve the area. The Company was responsible for obtaining any required regulatory permits, licenses and approvals to implement the water supply solution, including but not limited to those from PURA, the Connecticut Department of Energy and Environmental Protection (“DEEP”) and the Connecticut Department of Public Health (“DPH”). The capital improvements were completed on time and the pipeline was connected to the UCONN campus in December 2016, which was within the agreed upon timeframe.

Town of Mansfield Agreement

Connecticut Water and the Town of Mansfield entered into an agreement for Connecticut Water to serve the Town of Mansfield community. On January 13, 2014, the Mansfield Town Council voted to authorize the Town Manager to execute the agreement with Connecticut Water and it was signed by the parties on January 21, 2014.

The key provisions of the agreement with the Town of Mansfield are as follows:

- Current off-campus customers of UCONN will become customers of Connecticut Water at UCONN's water rates in effect at that time (subject to any state-approved surcharges);
- Future water customers in the Town of Mansfield will be served by Connecticut Water at the rates authorized by the PURA;
- Connecticut Water will assume responsibility for maintaining, repairing and replacing the off-campus water system serving the Town of Mansfield;
- Connecticut Water will make any source or system improvements to meet current and future water supply needs of the area; and
- Pursuant to the Agreement, a Water System Advisory Committee ("WSAC") was created with representatives of the Town of Mansfield, UCONN, regional representatives and other key stakeholders to advise Connecticut Water regarding water service and the system's operations, expansion or integration as well as recommended best management practices, including water conservation programs. The WSAC meets quarterly.

The former off-campus customers of UCONN in the Town of Mansfield became customers of Connecticut Water in December 2016.

Competition

Our Regulated Companies face competition from a few small privately-owned water systems operating within, or adjacent to, our franchise areas and from municipal and public authority systems whose service areas in some cases overlap portions of our franchise areas.

Employees

As of December 31, 2016, we employed a total of 266 people. Our employees are not covered by collective bargaining agreements.

Executive Officers of the Registrant

The following is a list of the executive officers of the Company as of March 13, 2017:

Name	Age in 2017*	Offices	Period Held or Prior Position	Term of Office Expires
E. W. Thornburg	56	Chairman, President, and Chief Executive Officer	Held positions since March 2006	2017 Annual Meeting
D. C. Benoit	60	Senior Vice President – Finance, Chief Financial Officer and Treasurer	Held current position or other executive position with the Company since April 1996	2017 Annual Meeting
C. J. Patla	50	Vice President – Service Delivery	Held current position or other engineering position with the Company since June 1990	2017 Annual Meeting
M. P. Westbrook	58	Vice President – Customer and Regulatory Affairs	Held current position or other management position with the Company since September 1988	2017 Annual Meeting
K. A. Johnson	50	Vice President – Human Resources and Corporate Secretary	Held current position or other human resources position with the Company since May 2007	2017 Annual Meeting
J. E. Wallingford	60	Division President – The Maine Water Company	President of The Maine Water Company (and its predecessor companies) since 1993	Retiring effective March 31, 2017

* - Age shown is as of filing date of March 13, 2017.

For further information regarding the executive officers see the Company's Proxy Statement to be filed on or about March 30, 2017.

Segments of Our Business

For management and financial reporting purposes we divide our business into three segments: Water Operations (our Regulated Companies), Real Estate Transactions (through either our regulated or unregulated companies), and Services and Rentals (our unregulated companies and certain unregulated transactions within Maine Water).

Water Operations – The Water Operations segment is comprised of our core regulated water operations to supply public drinking water to our customers. This segment encompasses all transactions of our Regulated Companies with the exception of certain real estate transactions. More detailed information, including revenues, costs and income taxes associated with the segment can be found in Note 14, "Segment Reporting" in the Company's "Notes to the Consolidated Financial Statements".

Real Estate Transactions – Our Real Estate Transactions segment involves the sale or donation for income tax benefits of our real estate holdings. These transactions can be effected by any of our subsidiary companies. Through land donations and sales in previous years, the Company earned tax credits to use in future years. The Company is limited by time and the amount of taxable income when using these credits. In the year ended December 31, 2014, the Company sold two small parcels of real estate, resulting in net income of \$50,000. During 2015, the Company donated land associated with a previously sold land conservation easement in Connecticut and the sale of three small parcels of land in Maine. These transactions generated \$349,000 in net income in the Real Estate segment. For the year ended December 31, 2016, the Company sold a small parcel of land and adjusted previously adjusted tax reserves related to previously completed land sales/donations resulting in a loss of \$54,000. Net income from the Real Estate Transactions segment is shown net in the "Other Income (Deductions), Net of Taxes" portion of the Company's Consolidated Statements of Income. More detailed information, including revenues, costs and income taxes associated with the segment can be found in Note 14, "Segment Reporting" in the Company's "Notes to the Consolidated Financial Statements".

A breakdown of the net income of this segment between our regulated and unregulated companies for the past three years is as follows:

	(Loss) Income from Real Estate Transactions		
	Regulated	Unregulated	Total
2016	\$ (54,000)	\$ —	\$ (54,000)
2015	\$ 349,000	\$ —	\$ 349,000
2014	\$ 4,000	\$ 46,000	\$ 50,000

Services and Rentals – Our Services and Rentals segment provides contracted services to water and wastewater utilities and other clients and also leases certain of our properties to third parties through our unregulated companies in the State of Connecticut and through Maine Water in the State of Maine. The types of services provided include contract operations of water and wastewater facilities; *Linebacker*[®], our service line protection plan for public drinking water customers; and providing bulk deliveries of emergency drinking water to businesses and residences via tanker truck. Our lease and rental income comes primarily from the renting of residential and commercial property. Net income from the Services and Rentals segment is shown net in the “Other Income (Deductions), Net of Taxes” portion of the Company’s “Consolidated Statements of Income”. More detailed information, including revenues, costs and income taxes associated with the segment can be found in Note 14, “Segment Reporting” in the Company’s “Notes to the Consolidated Financial Statements”.

Linebacker is an optional service line protection program offered by the Company to eligible residential customers through NEWUS in Connecticut and Maine Water in Maine covering the cost of repairs for leaking or broken water service lines which provide drinking water to a customer’s home. For customers who enroll in this program, the Company will repair or replace a leaking or broken water service line, curb box, curb box cover, meter pit, meter pit cover, meter pit valve plus in-home water main shut off valve before the meter. This was the fifth year that NEWUS has successfully offered expanded coverage to Connecticut Water customers for failure of in-home plumbing, sewer and septic drainage lines and implemented modified terms and conditions with limitations on certain coverages. As of December 31, 2016, NEWUS had approximately 20,000 customers enrolled in its *Linebacker* protection program and over 35% were enrolled in one of our expanded coverage plans. Depending on the coverage selected, *Linebacker* prices range between \$85 and \$185 per year for residential customers. Maine Water offers basic service line protection under *Linebacker* to its customers at a rate of \$85. As of December 31, 2016, Maine Water had approximately 2,500 customers enrolled in *Linebacker*. During 2015, NEWUS began expanding its *Linebacker* offering in towns in the State of Connecticut not currently served by Connecticut Water.

Some of the services listed above have limited competition. However, the Company has seen competitors in the service line protection business begin to market to Connecticut Water and Maine Water customers. Additionally, there can be considerable competition for contract operations of large water and wastewater facilities and systems. The Company sought to develop a niche market by attaching our name to service line protection plans and by seeking to serve smaller facilities and systems in our service areas where there is less competition. The Services and Rentals segment has provided between 5-8% of our overall net income in 2016, 2015, and 2014. Net income generated by this segment of our business was \$1,219,000, \$1,394,000 and \$1,471,000 for the years 2016, 2015, and 2014, respectively.

ITEM 1A. RISK FACTORS

Our business, financial condition, operating results and cash flows can be impacted by a number of factors, including, but not limited to, those set forth below, any one of which could cause our actual results to vary materially from recent results or anticipated future results. For a discussion identifying additional risk factors and important factors that could cause actual results to differ materially from those anticipated, see the discussion in “Special Note Regarding Forward-Looking Information”, in Item 7 below – “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Notes to Consolidated Financial Statements.”

Because we incur significant capital expenditures annually, we depend on the rates we charge our customers, which are subject to regulation.

The water utility business is capital intensive. On an annual basis, we spend significant amounts of capital for additions to or replacement of property, plant and equipment. Our ability to maintain and meet our financial objectives is dependent upon the rates we charge our customers. These rates are subject to approval by the PURA in Connecticut and the MPUC in Maine. Our Regulated Companies are entitled to file rate increase requests, from time to time, to recover our investments in utility plant and expenses. Once a rate increase petition is filed with the respective agency, the ensuing administrative and hearing process may be lengthy and costly. We can provide no assurances that any future rate increase requests will be approved by each agency; and, if approved, we cannot guarantee that any such rate increase requests will be granted in a timely or sufficient manner to cover the investments and expenses for which we initially sought the rate increase. Additionally, a regulatory agency may rule that a company must reduce its rates.

Under a 2007 Connecticut law, the PURA authorizes regulated water companies to use a rate adjustment mechanism, known as WICA, for eligible projects completed and in service for the benefit of the customers. During 2013, the Maine Legislature enacted a law that will allow Maine Water for expedited recovery of investments in water systems infrastructure replacement, both treatment and distribution, through WISC, similar to WICA in Connecticut. Maine Water began to use the WISC during 2014.

If we are unable to pay the principal and interest on our indebtedness as it comes due, or we default under certain other provisions of our loan documents, our indebtedness could be accelerated and our results of operations and financial condition could be adversely affected.

As of December 31, 2016, we had approximately \$197.0 million in long-term debt outstanding. Our ability to pay the principal and interest on our indebtedness as it comes due will depend upon our current and future performance. Our performance is affected by many factors, some of which are beyond our control. We believe that our cash generated from operations, and, if necessary, borrowing under our existing and planned credit facilities, will be sufficient to enable us to make our debt payments as they become due. If, however, we do not generate sufficient cash, we may be required to refinance our obligations or sell additional equity, which may be on terms that are not as favorable to the Company as current terms.

No assurance can be given that any debt refinancing or sale of equity will be possible when needed or that we will be able to negotiate acceptable terms. In addition, our failure to comply with certain provisions contained in our trust indentures and loan agreements relating to our outstanding indebtedness could lead to a default on these documents, which could result in an acceleration of our indebtedness.

Credit market volatility may affect our ability to refinance our existing debt, borrow funds under our existing lines of credit or incur additional debt.

During certain periods of the United States credit and liquidity crisis of 2008-2009, the volatility and disruption in the credit and banking markets reached unprecedented levels. In many cases, the markets contained limited credit capacity for certain issuers, and lenders had requested shorter terms. The market for new debt financing was limited and in some cases not available at all. In addition, the markets had increased the uncertainty that lenders will be able to comply with their previous commitments. The Company noted improvements during the second half of 2009 and continuing through 2016. If significant market disruption and volatility return, the Company may not be able to refinance our existing debt when it comes due, draw upon our existing lines of credit or incur additional debt, which may require us to seek other funding sources to meet our liquidity needs or to fund our capital expenditures budget. We cannot assure you that we will be able to obtain debt or other financing on reasonable terms, or at all.

Failure to maintain our existing credit ratings could affect our cost of funds and related margins and liquidity position.

Since 2003, Standard & Poor's Ratings Services ("S&P") has rated our outstanding debt and has given credit ratings to us and our subsidiary The Connecticut Water Company. Their evaluations are based on a number of factors, which include financial strength as well as transparency with rating agencies and timeliness of financial reporting. In March 2017, S&P affirmed its 'A' corporate credit rating on the Company. Additionally, S&P also affirmed the Company's ratings outlook as stable.

We may sustain losses that exceed or are excluded from our insurance coverage or for which we are not insured.

We maintain insurance coverage as part of our overall legal and risk management strategy to minimize our potential liabilities. Our insurance programs have varying coverage limits, exclusions and maximums, and insurance companies may seek to deny claims we might make. Generally, our insurance policies cover property damage, worker's compensation, employer's liability, general liability and automobile liability. Each policy includes deductibles or self-insured retentions and policy limits for covered claims. As a result, we may sustain losses that exceed or that are excluded from our insurance coverage or for which we are not insured.

Although in the past we have been generally able to cover our insurance needs, there can be no assurances that we can secure all necessary or appropriate insurance in the future, or that such insurance can be economically secured. For example, catastrophic events can result in decreased coverage limits, more limited coverage, increased premium costs or deductibles.

We are subject to adverse publicity and reputational risks, which make us vulnerable to negative customer perception and could lead to increased regulatory oversight or other sanctions.

Water utilities, including our Regulated Companies, have a large consumer customer base and as a result are exposed to public criticism regarding, among other things, the reliability of their water services, the quality of water provided, and the timeliness and accuracy of bills that are provided for such services. Adverse publicity and negative consumer sentiment may render legislatures and other governing bodies, the MPUC, PURA and other regulatory authorities, and government officials less likely to view companies such as the Company and its Regulated Companies in a favorable light, and may cause the Company and its Regulated Companies to be susceptible to less favorable legislative and regulatory outcomes, as well as increased regulatory oversight and more stringent regulatory requirements. Unfavorable regulatory outcomes may include the enactment of more stringent laws and regulations governing our operations, as well as fines, penalties or other sanctions or requirements. The imposition of any of the foregoing could have a material negative impact on the Company and each of our regulated companies' business, financial condition, results of operations and cash flows.

Our inability to comply with debt covenants under our credit facilities could result in prepayment obligations.

We are obligated to comply with debt covenants under our loan and debt agreements. Failure to comply with covenants under our credit facilities could result in an event of default, which if not timely cured or waived, could result in us being required to repay or finance these borrowings before their due date, could limit future borrowings, and result in cross default issues and increase our borrowing costs. The covenants are normal and customary in bank and loan agreements. The Company and its subsidiaries were in compliance with all covenants at December 31, 2016.

Market conditions, interest rate changes or changes in demographics may unfavorably impact the value of our benefit plan assets and liabilities which then could require significant additional funding.

The performance of the capital markets affects the values of the assets that are held in trust to satisfy future obligations under the Company's pension and post-retirement benefit plans and could significantly impact our results of operations and financial position. As detailed in the "Notes to Consolidated Financial Statements", the Company has significant obligations in these areas and the Company holds significant assets in these trusts. These assets are subject to market fluctuations, which may affect investment returns, which may fall below the Company's projected return rates. A decline in the market value of the pension and post-retirement benefit plan assets will increase the funding requirements under the Company's pension and post-retirement benefit plans if the actual asset returns do not recover these declines in value. Additionally, the Company's pension and post-retirement benefit plan liabilities are sensitive to changes in interest rates. As interest rates decrease, the liabilities increase, potentially increasing benefit expense and funding requirements. Further, changes in demographics, including increased numbers of retirements or changes in life expectancy assumptions may also increase the funding requirements of the obligations related to the pension and other post-retirement benefit plans. Also, future increases in pension and other post-retirement costs as a result of reduced plan assets may not be fully recoverable from our customers, and the results of operations and financial position of the Company could be negatively affected.

Our operating costs could be significantly increased because of state and federal environmental and health and safety laws and regulations.

Our water operations are governed by extensive federal and state environmental protection and health and safety laws and regulations, including the federal Safe Drinking Water Act, the Clean Water Act and similar state laws, and federal and state regulations issued under these laws by the U.S. Environmental Protection Agency and state environmental regulatory agencies. These laws and regulations establish, among other things, criteria and standards for drinking water and for discharges into the waters of the United States, the State of Connecticut or the State of Maine. Pursuant to these laws, we are required to obtain various environmental permits from environmental regulatory agencies for our operations. We cannot assure that we have been or will be at all times in full compliance with these laws, regulations and permits. If we violate or fail to comply with these laws, regulations or permits, we could be fined or otherwise sanctioned by regulators.

Environmental laws and regulations are complex and change frequently. These laws, and the enforcement thereof, have tended to become more stringent over time. For example, Connecticut is in the process of adopting a revision to its Water Diversion Regulations. The proposed revision would restrict the current exemption from Water Diversion permitting for certain expansions of service beyond Exclusive Service Areas identified as of October 2016. If this regulatory change is approved by the General Assembly's Legislative Regulation Review Committee, Water Diversion permits will be required for more service area expansions. While we have budgeted for future capital and operating expenditures to maintain compliance with these laws and our permits, it is possible that new or stricter standards could be imposed that will raise our operating costs. Although these costs may be recovered in the form of higher rates, there can be no assurance that either the PURA or the MPUC would approve rate increases to enable us to fully recover such costs. In summary, we cannot be assured that our costs of complying with, or discharging liabilities under, current and future environmental and health and safety laws will not adversely affect our business, results of operations or financial condition.

Our business has inherently dangerous workplaces. If we fail to maintain safe work sites, we can be exposed to not only people impacts but also to financial losses such as penalties and other liabilities.

Our safety record is critical to our reputation. We maintain health and safety standards to protect our employees, customers, vendors and the public. Although we intend to adhere to such health and safety standards and aim for zero injuries, it is extremely difficult to avoid accidents at all times.

Our business sites, including construction and maintenance sites, often put our employees and others in close proximity with large pieces of equipment, moving vehicles, pressurized water, underground trenches and vaults, chemicals and other regulated materials. On many sites we are responsible for safety and, accordingly, must implement safety procedures. If we fail to implement such procedures or if the procedures we implement are ineffective or are not followed by our employees or others, our employees and others may be injured or die. Unsafe work sites also have the potential to increase employee turnover and raise our operating costs. Any of the foregoing could result in financial losses, which could have a material adverse impact on our business, financial condition, results of operations and cash flows.

In addition, our operations can involve the handling and storage of hazardous chemicals, which, if improperly handled, stored or disposed of, could subject us to penalties or other liabilities. We are also subject to regulations dealing with occupational health and safety. Although we maintain functional employee groups whose primary purpose is to ensure we implement effective health, safety, and environmental work procedures throughout our organization, including construction sites and maintenance sites, the failure to comply with such regulations or procedures could subject us to liability.

Climate change laws and regulations may be adopted that could require compliance with greenhouse gas emissions standards and other climate change initiatives. Additional capital expenditures could be required and our operating costs could be increased in order to comply with new regulatory standards imposed by federal and state environmental agencies.

Climate change has been receiving ever increasing attention worldwide in the past decade. Many scientists, legislators, and others attribute global warming to increased levels of greenhouse gases, including carbon dioxide, which has led to significant legislative and regulatory efforts to limit greenhouse gas emissions. Possible new climate change laws and regulations, if enacted, may require us to monitor and/or change our utility operations. It is possible that new standards could be imposed that will require additional capital expenditures or raise our operating costs. Because it is uncertain what laws will be enacted, we cannot predict the potential impact of such laws on our future consolidated financial condition, results of operations, or cash flows. Although these expenditures and costs may be recovered in the form of higher rates, there can be no assurance that either the PURA or the MPUC or other regulatory bodies that govern our business would permit us to recover such expenditures and costs. We cannot assure you that our costs of complying with new standards or laws will not adversely affect our business, results of operations or financial condition.

Streamflow Regulations in Connecticut could potentially impact our ability to serve our customers.

In December 2011, regulations concerning the flow of water in Connecticut's rivers and streams were adopted. As promulgated, the regulations require that certain downstream releases be made from seven of Connecticut Waters's eighteen active reservoirs no later than ten years following the adoption of stream classifications by the Department of Energy and Environmental Protection ("DEEP"). Currently, downstream releases are made at two locations. No groundwater supply wells are affected by the regulations.

DEEP has finalized stream classifications in two areas of the state where Connecticut Water maintains and operates sources of supply. Other areas of the state, including areas where Connecticut Water operates, remain to be classified. The Company remains engaged in the process in order to minimize impact to our available water supply. Although significantly and favorably modified from prior versions, the regulations still have the potential to lower our safe yield, raise our capital and operating expenses and adversely affect our revenues and earnings. Because they affect only a subset of the Company's supplies and allow for releases to be scaled back in response to drought events, the overall impact is anticipated to be manageable. Costs associated with the regulations may be recovered in the form of higher rates. Although there can be no assurance the PURA would approve rate increases to enable us to recover all such costs, legislation passed in 2013 allows for a WICA surcharge to recover capital improvement costs necessary to achieve compliance with the regulations.

The State of Maine also has regulations that govern the flow of water in rivers and streams and also govern lake levels on great ponds. Code of Maine Rules Chapter 587 ("Chapter 587") regulates any activity that alters the flow or level of classified state waters after August 2007. Maine Water operates five water systems that use surface waters governed by this chapter. Maine Water has operated in full compliance with the chapter since its effective date and fully expects continued compliance. For public water systems, Chapter 587 allows the Maine Department of Environmental Protection ("MDEP") to impose site specific conditions in locations where Maine's water quality classifications are not being met. Any conditions proposed on a water withdrawal by a public water system must consider the provisions of any legislative charter, the watershed protection benefits provided by the utility and the financial viability of the utility. Further, any conditions imposed must be accommodated by the existing MPUC approved rate schedule for the utility and may not, in and of themselves, cause a utility to request a rate increase from their customers. To date, the MDEP has not imposed any withdrawal conditions on any public water system in Maine.

Maine Water's business is subject to seasonal fluctuations which could adversely affect demand for its water services and its revenues.

Demand for our water during the warmer months is generally greater than during cooler months due primarily to additional requirements for water in connection with irrigation systems, swimming pools, cooling systems and other outside water use. Throughout the year, and particularly during typically warmer months, demand will vary with temperature and rainfall levels. In the event that temperatures during the typically warmer months are cooler than normal, or if there is more rainfall than normal, the demand for our water may decrease and adversely affect our revenues. As Maine Water becomes eligible to use the recently passed water revenue adjustment mechanism upon the expiration of the agreed upon stay out period, this risk will be mitigated.

Declining per customer residential water usage in the State of Maine may reduce our revenues, financial condition and results of operations in future years.

A trend of declining per customer residential water usage has been observed for the last several years, which we attribute to increased water conservation, including the use of more efficient household fixtures and appliances among residential users. Our regulated business in Maine is heavily dependent on revenue generated from rates we charge to our residential customers for the volume of water they use. The rate we charge for our water is regulated by the MPUC in Maine and we may not unilaterally adjust our rates to reflect changes in demand. Declining volume of residential water usage may have a negative impact on our operating revenues in the future if regulators do not reflect any usage declines in the rate setting design process. As Maine Water becomes eligible to use the recently passed water revenue adjustment mechanism upon the expiration of the agreed upon stay out periods, this risk will be mitigated.

Potential regulatory changes or drought conditions may impact our ability to serve our current and future customers' demand for water and our financial results.

We depend on an adequate water supply to meet the present and future demands of our customers. Changes in regulatory requirements could affect our ability to utilize existing supplies and/or secure new sources, as required. Insufficient supplies or an interruption in our water supply could have a material adverse effect on our financial condition and results of operations. Drought conditions could interfere with our sources of water supply and could adversely affect our ability to supply water in sufficient quantities to our existing and future customers. An interruption in our water supply could have a material adverse effect on our financial condition and results of operations. Moreover, governmental restrictions on water usage during drought conditions may result in a decreased demand for our water, even if our water reserves are sufficient to serve our customers during these drought conditions, which may adversely affect our revenues and earnings. Persistent dry weather and continued drought conditions in 2016 in the State of Connecticut prompted Connecticut Water to join other major water utilities in the state and request that all customers voluntarily reduce their water usage by 10% in July in an effort to extend the availability of existing supplies and to support the rivers and streams in the state. While supplies in our reservoirs are lower than normal, Connecticut Water also has groundwater sources in nearly all of its water systems that provide operational flexibility so we are not solely dependent on our reservoirs for water supply. Connecticut Water continues to encourage all customers to reduce their water usage by 10% and, in October, began asking customers in the shoreline communities of Guilford, Madison, Clinton, Westbrook and Old Saybrook to reduce their water usage by 15%. Connecticut Water will continue to monitor precipitation rates, reservoir levels, and water demands and will modify its request for water conservation measures accordingly.

Wastewater operations entail significant risks and may impose significant costs.

Wastewater collection and treatment and septage pumping and sludge hauling involve various unique risks. If collection or treatment systems fail or do not operate properly, or if there is a spill, untreated or partially treated wastewater could discharge onto property or into nearby streams and rivers, causing various damages and injuries, including environmental damage. These risks are most acute during periods of substantial rainfall or flooding, which are the main causes of wastewater overflow and system failure. Liabilities resulting from such damages and injuries could harm our business, financial condition, and results of operations.

We are increasingly dependent on the continuous and reliable operation of our information technology systems, and a disruption of these systems, resulting from cyber security attacks or other events, could adversely affect our business.

We rely on our information technology systems in connection with the operation of our business, especially with respect to customer service and billing, accounting and, in some cases, the monitoring and operation of our treatment, storage and pumping facilities. In addition, we rely on our systems to track our utility assets and to manage maintenance and construction projects, materials and supplies, and our human resource functions. A loss of these systems, or major problems with the operation of these systems, could adversely affect our operations and have a material adverse effect on our business, financial condition, and results of operations. Our information technology systems may be vulnerable to damage or interruption from the following types of cyber security attacks or other events:

- power loss, computer systems failures, and internet, telecommunications or data network failures;
- operator negligence or improper operation by, or supervision of, employees;
- physical and electronic loss of data;
- computer viruses, cyber security attacks, intentional security breaches, hacking, denial of service actions, misappropriation of data and similar events;
- difficulties in the implementation of upgrades or modification to our information technology systems; and
- hurricanes, fires, floods, earthquakes and other natural disasters.

Recognizing the increasing importance of managing and protecting electronic data, the Company, beginning in 2014, partnered with a consulting firm to evaluate the Company's cyber security strengths and vulnerabilities and to help in creating an evaluation of the Company's current information technology ("IT") structure within the organization. In April 2014, a cyber security assessment analysis identified and prioritized steps that the Company should take to enhance its security surrounding cyber security. In September 2014, the consultant delivered a report related to the IT structure which contained recommendations aimed at strengthening the IT organization. The Company has implemented the recommendations contained in the cyber security assessment and will continue to monitor developments across the cyber security environment.

Although we do not believe that our systems are at a materially greater risk of cyber security attacks than other similar organizations, our information technology systems may be vulnerable to damage or interruption from the types of cyber security attacks or other events listed above or other similar actions, and such incidents or other events may go undetected for a

period of time. Such cyber security attacks or other events may result in: the loss or compromise of customer, financial or operational data; disruption of billing, collections or normal field service activities; disruption of electronic monitoring and control of operational systems; and delays in financial reporting and other normal management functions. Possible impacts associated with a cyber security attack or other events may include remediation costs related to lost, stolen, or compromised data, repairs to data processing systems, increased cyber security protection costs, adverse effects on our compliance with regulatory and environmental laws and regulation, including standards for drinking water, litigation and reputational damage.

The failure of, or the requirement to repair, upgrade or dismantle, any of our dams may adversely affect our financial condition and results of operations.

We own and operate numerous dams throughout the States of Connecticut and Maine. While the Company maintains robust dam maintenance and inspection programs, a failure of any of those dams could result in injuries and damage to residential and/or commercial property downstream for which we may be responsible, in whole or in part. The failure of a dam could also adversely affect our ability to supply water in sufficient quantities to our customers and could adversely affect our financial condition and results of operations. Any losses or liabilities incurred due to the failure of one of our dams might not be covered by insurance policies or be recoverable in rates, and such losses may make it difficult for us to secure insurance in the future at acceptable rates.

Any failure of our reservoirs, storage tanks, mains or distribution networks could result in losses and damages that may affect our financial condition and reputation.

Connecticut Water and Maine Water distribute water through an extensive network of mains and stores water in reservoirs and storage tanks located across Connecticut and Maine. A failure of major mains, reservoirs, or tanks could result in injuries and damage to residential and/or commercial property for which we may be responsible, in whole or in part. The failure of major mains, reservoirs or tanks may also result in the need to shut down some facilities or parts of our water distribution network in order to conduct repairs. Such failures and shutdowns may limit our ability to supply water in sufficient quantities to our customers and to meet the water delivery requirements prescribed by governmental regulators, including the PURA and the MPUC, and adversely affect our financial condition, results of operations, cash flow, liquidity and reputation. Any business interruption or other losses might not be covered by insurance policies or be recoverable in rates, and such losses may make it difficult for us to secure insurance in the future at acceptable rates.

Any future acquisitions we may undertake may involve risks and uncertainties.

An important element of our growth strategy is the acquisition and integration of water systems in order to move into new service areas and to broaden our current service areas. As of December 31, 2016, our Regulated Companies serve 124,968 customers, or a population of approximately 400,000 people, in 77 municipalities throughout Connecticut and Maine. We will be unable to acquire other businesses if we cannot identify suitable acquisition opportunities or reach mutually agreeable terms with acquisition candidates. It is our intent, when practical, to integrate any businesses we acquire with our existing operations. The negotiation of potential acquisitions as well as the integration of acquired businesses could require us to incur significant costs and cause diversion of our management's time and resources. Future acquisitions by us could result in:

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

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

The failure to consummate the pending acquisition of The Avon Water Company could adversely affect our business.

We recently entered into an acquisition agreement to acquire Avon Water. The transaction is subject to regulatory and other specified approvals, including a final order of the PURA approving the transaction and the effectiveness under the Securities Act of 1933 (the “Securities Act”) of the Company’s registration statement on Form S-4 which is expected to be filed in the second quarter of 2017.

The completion of this transaction is subject to risks and uncertainties. First, if the required conditions and regulatory approvals are not satisfied or waived, then the acquisition likely would not be completed. Second, if the closing of the acquisition is substantially delayed or the closing does not occur at all, or if the terms of the acquisition are required to be modified substantially due to regulatory concerns, we may not be able to realize the anticipated benefits of the acquisition fully or at all. Third, under certain circumstances specified in the purchase agreement, we may be required to pay a termination fee if the agreement is terminated under specified circumstances. Fourth, the failure to consummate the pending acquisition may result in negative publicity and a negative impression of us in the investment community. There can be no assurance that our business, the price of our common stock or our financial condition will not be adversely affected, as compared to the condition prior to the announcement of the acquisition, if the acquisition is not consummated.

Water supply contamination may adversely affect our business.

Our water supplies are subject to possible contamination, including contamination from the development of naturally-occurring compounds, chemicals in groundwater systems, pollution resulting from man-made sources, and possible terrorist attacks. In the event that our water supply is contaminated, we may have to interrupt the use of that water supply until we are able to substitute the flow of water from an uncontaminated water source or provide additional treatment. We may incur significant costs in order to treat the contaminated source through expansion of our current treatment facilities, or development of new treatment methods. If we are unable to substitute water supply from an uncontaminated water source, or to adequately treat the contaminated water source in a cost-effective manner, there may be an adverse effect on our revenues, operating results and financial condition. The costs we incur to decontaminate a water source or an underground water system could be significant and could adversely affect our business, operating results and financial condition and may not be recoverable in rates. We could also be held liable for consequences arising out of human exposure to hazardous substances in our water supplies or other environmental damage. For example, private plaintiffs have the right to bring personal injury or other toxic tort claims arising from the presence of hazardous substances in our drinking water supplies. Our insurance policies may not be sufficient to cover the costs of these claims.

We operate a number of water and wastewater systems under Operation and Maintenance (“O&M”) contracts and face the risk that the owners of those systems may fail to provide capital to properly maintain those systems, which may negatively affect us as the operators of the systems.

We operate a number of water and wastewater systems under O&M contracts. Pursuant to these contracts, we operate the system according to the standards set forth in the applicable contract, and it is generally the responsibility of the owner of the system to undertake capital improvements. In some cases, we may not be able to convince the owner to make needed improvements in order to maintain compliance with applicable regulations. Although violations and fines incurred by water and wastewater systems may be the responsibility of the owner of the system under these contracts, those non-compliance events may reflect poorly on us as the operator of the system and damage our reputation, and in some cases, may result in liability to the same extent as if we were the owner. Effective February 27, 2017, the only wastewater O&M contract customer served by the Company was acquired as part of the Heritage Village acquisition.

Increased security measures may continue to increase our operating costs.

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

The accuracy of our judgments and estimates about financial and accounting matters will impact our operating results and financial condition.

We make certain estimates and judgments in preparing our financial statements regarding, among others:

- the number of years to depreciate certain assets;
- amounts to set aside for uncollectible accounts receivable and uninsured losses;
- our legal exposure and the appropriate accrual for claims, including medical and workers' compensation claims;
- future costs for pensions and other post-retirement benefit obligations; and
- possible tax allowances.

The quality and accuracy of those estimates and judgments will have an impact on our operating results and financial condition.

In addition, we must estimate unbilled revenues and costs at the end of each accounting period. If our estimates are not accurate, we will be required to make an adjustment in a future period.

The final determination of our income tax liability may be materially different from our income tax provision.

Significant judgment is required in determining our provision for income taxes. Our calculation of the provision for income taxes is subject to our interpretation of applicable business tax laws in the jurisdictions in which we file. In addition, our income tax returns are subject to periodic examination by the Internal Revenue Service and other taxing authorities. During 2013 and 2014, Connecticut Water and Maine Water, respectively, changed their tax method of accounting to permit the expensing of qualifying utility asset costs that were previously being capitalized and depreciated for tax purposes. Our determination of what qualifies as a capital cost versus a repair expense tax deduction is subject to subsequent adjustment and may impact the income tax benefits that have been recognized. Although we believe our income tax estimates, including any tax reserves or valuation allowances we have recorded or may record, are appropriate, there is no assurance that the final determination of our income tax liability will not be materially different; either higher or lower, from what is reflected in our income tax provision. In the event we are assessed additional income taxes, our business, financial condition, and results of operations could be adversely affected.

Key employee turnover may adversely affect our operating results.

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

We must continue to attract and retain qualified technical and managerial personnel in order to succeed.

Our future success will also depend largely upon our ability to attract and retain highly skilled technical, operational and financial managers. There is significant competition for such personnel in our industry. We try to ensure that we offer competitive compensation and benefits as well as opportunities for continued development, and we continually strive to recruit and train qualified personnel and retain key employees. There can be no assurance, however, that we will continue to be successful in attracting and retaining the personnel we require to grow and operate profitably.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None

ITEM 2. PROPERTIES

At December 31, 2016, the properties of our Regulated Companies consisted of land, easements, rights (including water rights), buildings, reservoirs, standpipes, dams, wells, supply lines, treatment plants, pumping plants, transmission and distribution mains and conduits, mains and other facilities and equipment used for the collection, purification, storage and distribution of water. In certain cases, Connecticut Water and Maine Water are or may be a party to limited contractual arrangements for the provision of water supply from neighboring utilities. Water mains are located, for the most part, in public streets and, in a few instances, are located on land that we own in fee simple and/or land utilized pursuant to easement right, most of which are perpetual and adequate for the purpose for which they are held. Substantially all of our treatment, storage, and distribution properties are owned by our subsidiaries, Connecticut Water and Maine Water. A substantial portion of such properties owned by Maine Water are subject to liens of mortgage or indentures that secure bonds, notes and other evidences of long-term indebtedness.

The net utility plant of the Company at December 31, 2016 was solely owned by the Regulated Companies. The “Net Utility Plant” balance as of December 31, 2016 was \$601,396,000, approximately \$55.1 million more than the balance of “Net Utility Plant” as of December 31, 2015, due primarily to normal plant additions and construction spending related to infrastructure improvements.

Sources of water supply owned, maintained, and operated by our Regulated Companies include 25 surface water supplies and 99 well fields, as of December 31, 2016. In addition, Connecticut Water and Maine Water have agreements with various neighboring water utilities to provide water, at negotiated rates, to our water systems. Collectively, these sources have the capacity to deliver approximately 75 million gallons of potable water daily to the 25 major operating systems. The Regulated Companies own, maintain, and operate 50 small, non-interconnected satellite and consecutive water systems that, combined, have the ability to deliver about 3.5 million gallons of additional water per day to their respective systems. For some small consecutive water systems, purchased water may comprise substantially all of the total available supply of the system.

As of December 31, 2016, the Regulated Companies own and operate 30 water filtration facilities, having a combined treatment capacity of approximately 52 million gallons per day.

As of December 31, 2016, the transmission and distribution systems of the Regulated Companies consisted of approximately 2,100 miles of main. On that date, approximately 75% of our mains were 8 inch diameter or larger. Substantially all new main installations are cement-lined ductile iron pipe of 8 inch diameter or larger.

We believe that our properties are maintained in good condition and in accordance with current regulations and standards of good waterworks industry practice.

ITEM 3. LEGAL PROCEEDINGS

We are involved in various legal proceedings from time to time. Although the results of legal proceedings cannot be predicted with certainty, there are no pending legal proceedings to which we, or any of our subsidiaries are a party, or to which any of our properties is subject, that presents a reasonable likelihood of a material adverse impact on the Company’s financial condition, results of operations or cash flows.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable

PART II

ITEM 5. MARKET FOR THE REGISTRANTS'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our Common Stock is traded on the NASDAQ Global Select Market under the symbol "CTWS". Our quarterly high and low stock prices as reported by NASDAQ and the cash dividends we paid during 2016 and 2015 for our Common Stock are listed as follows:

Period	Price		Dividends Paid
	High	Low	
2016			
First Quarter	\$ 45.66	\$ 37.48	\$ 0.2675
Second Quarter	56.27	43.16	0.2825
Third Quarter	56.62	45.13	0.2825
Fourth Quarter	58.32	48.00	0.2825
2015			
First Quarter	\$ 38.55	\$ 35.07	\$ 0.2575
Second Quarter	37.99	33.20	0.2575
Third Quarter	36.58	33.15	0.2675
Fourth Quarter	39.93	34.15	0.2675

As of February 1, 2017, there were approximately 3,000 holders of record of our common stock.

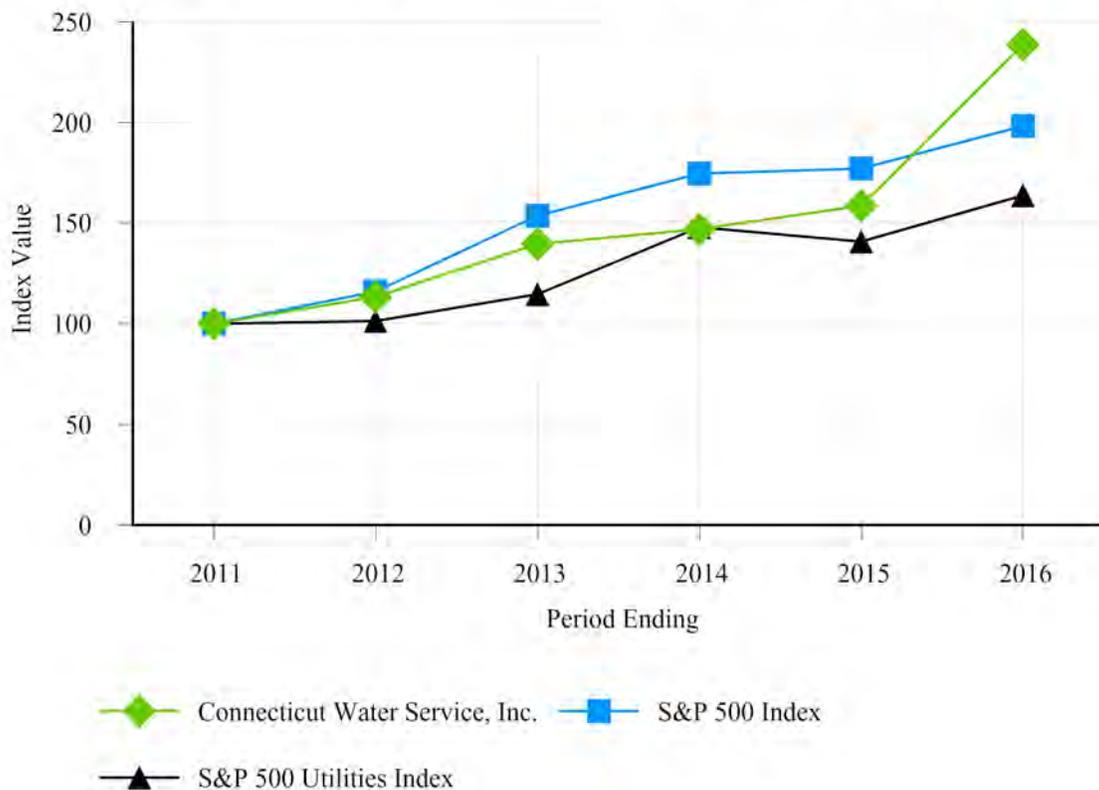
We presently intend to pay quarterly cash dividends in 2017 on March 15, June 15, September 15 and December 15, subject to our earnings and financial condition, regulatory requirements and other factors our Board of Directors may deem relevant.

The Company's Annual Meeting of Shareholders is scheduled for May 11, 2017 in Madison, Connecticut.

Purchases of Equity Securities by the Company – In May 2005, the Company adopted a common stock repurchase program ("Share Repurchase Program"). The Share Repurchase Program allows the Company to repurchase up to 10% of its outstanding common stock, at a price or prices that are deemed appropriate. As of December 31, 2016, no shares have been repurchased. Currently, the Company has no plans to repurchase shares under the Share Repurchase Program.

Performance Graph – Set forth below is a line graph comparing the cumulative total shareholder return for each of the years 2012 – 2016 on the Company’s Common Stock, based on the market price of the Common Stock and assuming reinvestment of dividends, with the cumulative total shareholder return of companies in the S&P’s 500 Index and the S&P’s 500 Utility Index.

Comparison of Cumulative Five Year Total Return



ITEM 6. SELECTED FINANCIAL INFORMATION

SUPPLEMENTAL INFORMATION (Unaudited)

SELECTED FINANCIAL DATA

Years Ended December 31, (thousands of dollars except per share amounts and where otherwise indicated)

	2016	2015	2014	2013	2012
CONSOLIDATED STATEMENTS OF INCOME					
Operating Revenues	\$ 98,667	\$ 96,041	\$ 94,020	\$ 91,481	\$ 83,838
Operating Expenses	\$ 70,462	\$ 69,399	\$ 68,856	\$ 69,488	\$ 64,229
Other Utility Income, Net of Taxes	\$ 744	\$ 797	\$ 833	\$ 856	\$ 812
Total Utility Operating Income	\$ 28,949	\$ 27,439	\$ 25,997	\$ 22,849	\$ 20,421
Interest and Debt Expense	\$ 6,916	\$ 6,737	\$ 6,515	\$ 6,130	\$ 8,581
Net Income	\$ 23,387	\$ 22,761	\$ 21,319	\$ 18,269	\$ 13,640
Cash Common Stock Dividends Paid	\$ 12,514	\$ 11,715	\$ 11,188	\$ 10,758	\$ 8,467
Dividend Payout Ratio	54%	51%	52%	59%	62%
Weighted Average Common Shares Outstanding	11,008,565	10,958,499	10,892,986	10,827,220	8,763,418
Basic Earnings Per Common Share from Continuing Operations	\$ 2.12	\$ 2.07	\$ 1.95	\$ 1.68	\$ 1.55
Number of Shares Outstanding at Year End	11,248,458	11,192,882	11,124,630	11,038,232	10,939,486
ROE on Year End Common Equity	9.9%	10.2%	10.2%	9.2%	7.4%
Declared Common Dividends Per Share	\$ 1.115	\$ 1.05	\$ 1.01	\$ 0.98	\$ 0.96
CONSOLIDATED BALANCE SHEET					
Common Stockholders' Equity	\$ 236,028	\$ 223,977	\$ 209,451	\$ 197,753	\$ 185,349
Long-Term Debt (Consolidated, Excluding Current Maturities)	197,047	171,868	170,309	168,201	171,064
Preferred Stock	772	772	772	772	772
Total Capitalization	\$ 433,847	\$ 396,617	\$ 380,532	\$ 366,726	\$ 357,185
Stockholders' Equity (Includes Preferred Stock)	55%	57%	55%	54%	52%
Long-Term Debt	45%	43%	45%	46%	48%
Net Utility Plant	\$ 601,396	\$ 546,284	\$ 506,939	\$ 471,876	\$ 447,911
Total Assets	\$ 784,502	\$ 710,715	\$ 664,897	\$ 623,970	\$ 571,564
Book Value - Per Common Share	\$ 20.98	\$ 20.01	\$ 18.83	\$ 17.91	\$ 16.94
OPERATING REVENUES BY REVENUE CLASS					
Residential	\$ 59,884	\$ 58,439	\$ 57,095	\$ 55,403	\$ 50,783
Commercial	12,250	11,816	11,473	11,238	10,138
Industrial	3,176	3,229	2,984	3,120	3,080
Public Authority	3,510	3,193	3,215	2,967	2,675
Fire Protection	18,486	18,016	17,757	17,337	15,592
Other (Including Non-Metered Accounts)	1,361	1,348	1,496	1,416	1,570
Total Operating Revenues	\$ 98,667	\$ 96,041	\$ 94,020	\$ 91,481	\$ 83,838
Number of Customers (End of Year)	124,968	123,633	123,071	121,768	121,791
Billed Consumption (Millions of Gallons)	9,800	9,772	9,428	9,277	8,332
Number of Employees	266	266	265	259	259

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FINANCIAL CONDITION

Executive Overview

Connecticut Water Service, Inc. (the "Company") is a non-operating holding company, whose income is derived from the earnings of its four active wholly-owned subsidiary companies, as of December 31, 2016: The Connecticut Water Company ("Connecticut Water"), The Maine Water Company ("Maine Water"), New England Water Utility Services, Inc. ("NEWUS"), and Chester Realty Company ("Chester Realty"). Connecticut Water and Maine Water are our regulated water companies (together, the "Regulated Companies").

In 2016, approximately 95% of the Company's net income was attributable to the water operations of the Regulated Companies, which combined had 124,968 customers throughout 77 municipalities in Connecticut and Maine, as of December 31, 2016. The rates charged for service by Connecticut Water are subject to review and approval by the Connecticut Public Utilities Regulatory Authority ("PURA"). The rates charged for service by Maine Water are subject to review and approval by the Maine Public Utilities Commission ("MPUC").

In 2007, the Connecticut General Assembly passed the Water Infrastructure and Conservation Adjustment ("WICA") Act. WICA allows Connecticut Water to add a surcharge to customers' bills, subject to an expedited review and approval by the PURA and no more than twice a year, to reflect the replacement of certain types of aging utility plant; principally water mains, meters, service lines and water conservation related investments. Connecticut Water has been using the WICA surcharge since 2009. Similarly, beginning in June 2013, a Water Infrastructure Charge ("WISC") became available in Maine that allows for expedited recovery of investment in water system infrastructure replacement, both treatment and distribution. Maine Water implemented the WISC mechanism in all of their systems in 2014.

Since 2013, Connecticut law has authorized a Water Revenue Adjustment ("WRA") to reconcile actual water demands with the demands projected in the last general rate case and allows companies to adjust rates as necessary to recover the revenues approved by PURA in the last general rate case. The WRA removes the financial disincentive for water utilities to develop and implement effective water conservation programs. The WRA allows water companies to defer on the balance sheet, as a regulatory asset or liability, for later collection from or crediting to customers the amount by which actual revenues deviate from the revenues allowed in the most recent general rate proceedings, including WICA proceedings. Additionally, the cap for WICA charges has been raised to 10%, from 7.5%, between general rate cases and expands the eligible projects to include energy conservation projects, improvements required to comply with streamflow regulations, and improvements to acquired systems.

On June 28, 2013, Connecticut Water entered into a settlement agreement with the Office of Consumer Council ("OCC") and the Office of the Attorney General for the State of Connecticut (the "Settlement Agreement"), whereby Connecticut Water adjusted the water rates charged to its customers effective April 1, 2014 in accordance with the elements of the Settlement Agreement (the "Connecticut Water Rate Reduction Plan"). On July 1, 2013, Connecticut Water submitted an application to the PURA seeking formal approval of the Settlement Agreement.

The Settlement Agreement contemplated that Connecticut Water would adopt regulations issued by the Internal Revenue Service ("IRS") that allowed the Company to adopt an alternative method for determining how expenditures related to tangible property can be treated for federal tax purposes for tax years beginning on or after January 1, 2012. This tax accounting method change treated certain expenditures that the Company historically capitalized for tax purposes, as a deductible repair expense on its tax return. The adoption of the tax accounting method change allowed Connecticut Water to record a favorable "catch up adjustment" on the Company's consolidated 2012 federal tax return which was filed in September 2013. The Company filed with the IRS a tax refund of approximately \$13.6 million by carrying back the net operating loss generated from this adjustment.

The Settlement Agreement includes, as a result of negotiated compromise of the parties' respective positions, the following key elements related to the Connecticut Water Rate Reduction Plan:

- 1) Connecticut Water crediting its water customers with the amount of the catch up adjustment plus the amount by which 2012 federal income taxes are reduced by the repair deduction (the deduction amount filed on the Company's 2012 federal tax return was approximately \$45 million) that would be offset in whole or in part by an anticipated rate increase arising from the WRA authorized by the State of Connecticut in Public Act No. 13-78 with any associated net change in rates reflected on Connecticut Water customers' bills as of April 1, 2014;

- 2) Resetting Connecticut Water's adjustment under Connecticut's WICA mechanism to zero by integrating the present WICA surcharge of 7.89% into Connecticut Water's base rates; and
- 3) Connecticut Water agreeing not to file for a general rate increase (except under extraordinary circumstances outside Connecticut Water's control) for new rates to be effective any sooner than October 1, 2015.

In the Settlement Agreement, the parties also requested that PURA approve an accounting treatment for Connecticut Water to: 1) allow for the deferral of the tax refund described above and a credit of the tax benefit to customers over a proposed two-year period through a credit on water bills issued which started on April 1, 2014 and 2) as discussed above, use the WRA to defer on the balance sheet as a regulatory asset or liability, for later collection from or crediting to customers of the amount by which actual revenues deviate from the revenues allowed in Connecticut Water's most recent general rate proceedings, including WICA proceedings.

On August 30, 2013, the PURA issued a final decision approving the Settlement Agreement. Connecticut Water began to issue a credit on customers' bills of approximately 8.5% on April 1, 2014, related to the repair deduction. Additionally, Connecticut Water began adding an approximate 4.5% surcharge to customer bills related to the WRA for a net surcredit of approximately 4.0%. Effective April 1, 2015, the 4.5% surcharge to customers was replaced by a 5.07% surcharge based on the WRA revenues recorded during 2014, leaving an approximate 3.4% net surcredit on customer bills.

Connecticut Water's allowed revenues for the year ended December 31, 2016, as approved by PURA during our 2010 general rate case and including subsequently approved WICA surcharges, were approximately \$76.7 million. Through normal billing for the year ended December 31, 2016 operating revenue for Connecticut Water would have been approximately \$75.6 million had the WRA not been implemented. As a result of the implementation of the WRA, Connecticut Water recorded \$1.1 million in additional revenue for the year ended December 31, 2016. During the year ended December 31, 2015 and 2014, Connecticut Water recorded \$1.6 million and \$3.7 million, respectively, in additional revenue related to the WRA.

The Company has and will continue to focus on minimizing operating costs that are passed along to its customers without sacrificing the quality service it values and the customers demand. At the same time, the Company will continue to employ its current strategy of timely collection of appropriate costs and a fair rate of return for its shareholders through appropriate rates for its regulated water service while looking to expand through targeted acquisitions.

University of Connecticut Agreement

Connecticut Water and the University of Connecticut ("UCONN") negotiated a definitive agreement for Connecticut Water to provide a long-term supply of potable water for UCONN's Storrs campus facilities which was approved by the Board of Trustees at their December 11, 2013 meeting and executed on December 18, 2013. The definitive agreement is consistent with the requirements of the project's Environmental Impact Evaluation ("EIE") and record of decision, as approved by the Office of Policy and Management, an agency of the State of Connecticut, that identified the Company as the preferred option to supply UCONN and the Town of Mansfield, Connecticut with up to 2.2 million gallons of water per day over the next 47 years. Connecticut Water funded a 5-mile pipeline from Tolland and other necessary infrastructure improvements at no cost to UCONN, the Town or the state's taxpayers to serve the area. The Company was responsible for obtaining any required regulatory permits, licenses and approvals to implement the water supply solution, including but not limited to those from PURA, the Connecticut Department of Energy and Environmental Protection ("DEEP") and the Connecticut Department of Public Health ("DPH"). The capital improvements were completed on time and the pipeline was connected to the UCONN campus in December 2016, which was within the agreed upon timeframe.

Town of Mansfield Agreement

Connecticut Water and the Town of Mansfield entered into an agreement for Connecticut Water to serve the Town of Mansfield community. On January 13, 2014, the Mansfield Town Council voted to authorize the Town Manager to execute the agreement with Connecticut Water and it was signed by the parties on January 21, 2014.

The key provisions of the agreement with the Town of Mansfield are as follows:

- Current off-campus customers of UCONN will become customers of Connecticut Water at UCONN's water rates in effect at that time (subject to any state-approved surcharges);
- Future water customers in the Town of Mansfield will be served by Connecticut Water at the rates authorized by the PURA;
- Connecticut Water will assume responsibility for maintaining, repairing and replacing the off-campus water system serving the Town of Mansfield;

- Connecticut Water will make any source or system improvements to meet current and future water supply needs of the area; and
- Pursuant to the Agreement, a Water System Advisory Committee (“WSAC”) was created with representatives of the Town of Mansfield, UCONN, regional representatives and other key stakeholders to advise Connecticut Water regarding water service and the system’s operations, expansion or integration as well as recommended best management practices, including water conservation programs. The WSAC meets quarterly.

The former off-campus customers of UCONN in the Town of Mansfield became customers of Connecticut Water in October 2016.

While the Company plans to file timely rate cases, continue to make acquisitions, similar to the recently completed HVWC acquisition and the announced Avon Water acquisition, and, in the future, utilize the WICA and WISC adjustments to allow for more timely recovery of investment in utility plant, it will also look to NEWUS and Maine Water to increase its earnings in unregulated businesses. The Company will continue to seek out maintenance and service contracts with new customers and renew existing contracts that have proven to be beneficial to the Company, as well as to continue the expansion of the *Linebacker*® program. As part of the Maine Water Stipulation Agreement, Maine Water is precluded from filing for a general rate increase that would be effective prior to July 1, 2017 in most of its divisions.

Regulatory Matters and Inflation

The Company, like all other businesses, is affected by inflation, most notably by the continually increasing costs required to maintain, improve, and expand its service capabilities. The cumulative effect of inflation over time results in significantly higher operating costs and facility replacement costs, which must be recovered from future cash flows.

Our regulated water companies’ ability to recover its increased expenses and/or investment in utility plant is dependent on the rates we charge our customers. Changes to these rates must be approved by the PURA and MPUC through formal rate proceedings. Due to the subjectivity of certain items involved in the process of establishing rates such as customer usage, future customer growth, inflation, and allowed return on investment, we have no assurance that we will be able to raise our rates to a level we consider appropriate, or to raise rates at all, through any future rate proceeding.

Our regulated water utilities are also subject to environmental and water quality regulations, which are continually modified and refined to ensure the safety of the Company’s water sources and, ultimately, the public’s health. Costs to comply with environmental and water quality regulations are substantial. The costs to comply with future changes in state or federal regulations, which could require us to modify current filtration facilities and/or construct new ones, or to replace any reduction of the safe yield from any of our current sources of supply, could be substantial. While there can be no guarantee that all expenditures related to increased regulation will be recoverable in rate proceedings, the Company believes that the regulatory environment in Connecticut and Maine would allow prudent expenditures to be recovered in rates. To date, the Company has never had any costs associated with water quality and environmental spending refused in a general rate proceeding. The Company believes that it is in compliance with current regulations, but the regulations are subject to change at any time.

Recognizing the increasing importance of managing and protecting electronic data, the Company, beginning in 2014, partnered with a consulting firm to evaluate the Company’s cyber security strengths and vulnerabilities and to help in creating an evaluation of the Company’s current information technology (“IT”) structure within the organization. In April 2014, a cyber security assessment analysis identified and prioritized steps that the Company should take to enhance its security surrounding cyber security. In September 2014, the consultant delivered a report related to the IT structure which contained recommendations aimed at strengthening the IT organization. The Company has implemented the recommendations contained in the cyber security assessment and will continue to monitor developments across the cyber security environment.

Critical Accounting Policies and Estimates

The Company’s Consolidated Financial Statements are prepared in conformity with accounting principles generally accepted in the United States of America (“GAAP”) and as directed by the regulatory commissions to which the Company’s Regulated Companies are subject. (See Note 1 to the Consolidated Financial Statements for a discussion of our significant accounting policies). The Company believes the following policies and estimates are critical to the presentation of its Consolidated Financial Statements.

Public Utility Regulation – Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 980 “Regulated Operations” (“FASB ASC 980”), requires cost-based, rate-regulated enterprises such as Connecticut Water and Maine Water to reflect the impact of regulatory decisions in their financial statements. The state regulators, through the rate

regulation process, can create regulatory assets that result when costs are allowed for ratemaking purposes in a period after the period in which costs would be charged to expense by an unregulated enterprise. The balance sheet includes regulatory assets and liabilities as appropriate, primarily related to income taxes, post-retirement benefit costs and deferred revenues associated with the WRA. The Company believes, based on current regulatory circumstances, that the regulatory assets recorded are probable to be recovered and that its use of regulatory accounting is appropriate and in accordance with the provisions of FASB ASC 980.

Revenue Recognition – The Company’s accounting policies regarding revenue recognition by segment are as follows:

Water Operations – Most of our water customers are billed quarterly, with the exception of larger commercial and industrial customers, as well as certain public and private fire protection customers who are billed monthly. Most customers, except fire protection customers, are metered. Revenues from metered customers are based on their water usage multiplied by approved, regulated rates and are earned when water is delivered. Public fire protection revenues are based on the length of the water main, and number of hydrants in service and are earned on a monthly basis. Private fire protection charges are based on the diameter of the connection to the water main. Our Regulated Companies accrue an estimate for metered customers for the amount of revenues earned relating to water delivered but unbilled at the end of each quarter, which is reflected as “Accrued Unbilled Revenues” in the accompanying balance sheets. Beginning in 2013, Connecticut Water began to record deferred revenue to represent under collection from customers based upon allowed revenues as approved by PURA. More detailed information, including revenues, costs and income taxes associated with the segment can be found in Note 14, “Segment Reporting” in the Company’s “Notes to the Consolidated Financial Statements”.

Real Estate Transactions – Revenues are recorded when a sale or other transaction has been completed and title to the real estate has been transferred. Net income from the Real Estate Transactions segment is shown net in the “Other Income (Deductions), Net of Taxes” portion of the Company’s Consolidated Statements of Net Income. More detailed information, including revenues, costs and income taxes associated with the segment can be found in Note 14, “Segment Reporting” in the Company’s “Notes to the Consolidated Financial Statements”.

Services and Rentals – Revenues are recorded when the Company has delivered the services called for by contractual obligation. Net income from the Services and Rentals segment is shown net in the “Other Income (Deductions), Net of Taxes” portion of the Company’s Consolidated Statements of Income. More detailed information, including revenues, costs and income taxes associated with the segment can be found in Note 14, “Segment Reporting” in the Company’s “Notes to the Consolidated Financial Statements”.

Income Taxes – The Company provides income tax expense for its utility operations in accordance with the regulatory accounting policies of the applicable jurisdictions. The Company’s income tax provision is calculated on a separate return basis. The Connecticut PURA requires the flow-through method of accounting for most state tax temporary differences as well as for certain federal temporary differences. The MPUC requires the flow-through method of accounting for most state temporary differences and normalized accounting for most federal temporary differences. However, in its approvals of the stipulation agreements between Maine Water and the Office of the Public Advocate, issued in 2015, the MPUC has allowed the flow-through method of accounting stemming from Maine Water’s adoption of the IRS’ Repair Regulations in all of its divisions.

The Company computes deferred tax liabilities for all temporary book-tax differences using the liability method prescribed in FASB ASC 740 “Income Taxes” (“FASB ASC 740”). Under the liability method, deferred income taxes are recognized at currently enacted income tax rates to reflect the tax effect of temporary differences between the financial reporting and tax bases of assets and liabilities. Such temporary differences are the result of provisions in the income tax law that either require or permit certain items to be reported on the income tax return in a different period than they are reported in the financial statements. Deferred tax liabilities that have not been reflected in tax expense due to regulatory treatment are reflected as “Unfunded Future Income Taxes”, and are expected to be included in future years’ rates.

The Company believes that deferred income tax assets, net of provisions, will be realized in the future. The majority of Unfunded Future Income Taxes, prior to 2013, relate to deferred state income taxes regarding book to tax depreciation differences. Beginning in 2013, basis differences resulting from the repair tax deduction contributed to the change in unfunded income taxes.

Deferred Federal and State Income Taxes include amounts that have been provided for accelerated depreciation subsequent to 1981, as required by federal income tax regulations, as well as the basis differences associated with expenditures qualifying for repair tax deduction as clarified by the IRS in regulations issued in 2013. Deferred taxes have also been provided for

temporary differences in the recognition of certain expenses for tax and financial statement purposes as allowed by regulatory ratemaking policies.

Employee Benefit Plan Accounting – Management evaluates the appropriateness of the discount rate through the modeling of a bond portfolio which approximates the pension and post-retirement plan liabilities. Management further considers rates of high quality corporate bonds of approximate maturities as published by nationally recognized rating agencies consistent with the duration of the Company’s pension and post-retirement plans.

The discount rate assumption we use to value our pension and post-retirement benefit obligations has a material impact on the amount of expense we record in a given period. Our 2016 and 2015 pension expense was calculated using assumed discount rates of 4.30% and 3.95%, respectively. Our 2016 and 2015 post-retirement welfare expense was calculated using assumed discount rates of 4.15% and 3.80%, respectively. In 2017, our pension and post-retirement welfare expense will be calculated using assumed discount rates of 4.10% and 3.95%, respectively. The following table shows how much a one percent change in our assumed discount rate would have changed our reported 2016 pension and post-retirement expense:

	Increase (Decrease) in Pension Expense	Increase (Decrease) in Post-retirement Expense
1% Increase in the discount rate	\$ (1,421,000)	\$ (73,000)
1% Decrease in the discount rate	\$ 1,720,000	\$ 92,000

Other assumptions that affect the costs associated with our benefit plans include the assumed rate of return on plan assets and the expected rate of compensation increase. The Company has assumed an 7.25% return on plan investments for 2016 and 2015, and a 4.00% rate of compensation increase for our pension and post-retirement welfare plans, in 2016 and 2015. The assumed health care trend rate was 8.25% and 8.5% at December 31, 2016 and 2015, respectively. RP 2016, issued by the Society of Actuaries in 2016, was used in determination of our pension and post-retirement benefit obligations as of December 31, 2016 and projected costs for 2017.

Goodwill – As part of the purchase of certain regulated water companies, the Company has recorded goodwill of \$30.4 million as of December 31, 2016 representing the amount of the purchase price over net book value of the assets acquired. The Company accounts for goodwill in accordance with Accounting Standards Codification 350 “Intangibles – Goodwill and Other” (“FASB ASC 350”). As a result of a rate order issued by the MPUC, the Company reduced its goodwill balance by \$1.3 million in the year ended December 31, 2015.

As part of FASB ASC 350, the Company is required to perform an annual review of goodwill for any potential impairment, which we perform as of December 31 each year. We update the assessment between the annual testing if events or circumstances occur that would more likely than not reduce the fair value of a reporting unit below its carrying value. As allowed under FASB ASC 350, the Company performed a qualitative analysis of its goodwill for the year ended December 31, 2016. A qualitative analysis includes a review of internal and external factors that could have an impact on a reporting unit’s fair value when compared to its carrying amount. These factors included a review of macroeconomic conditions, industry and market considerations, cost factors, overall financial performance, company specific events, changes in reporting units and a review of the Company’s stock price.

The last quantitative analysis of impairment was performed as of December 31, 2015, which concluded that the estimated fair value of the Water Operations reporting unit, which has goodwill recorded, exceeded the reporting unit’s carrying amount by at least 71% as of December 31, 2015. Additionally, the Company believes that no event has occurred which would trigger impairment since the last quantitative test performed. Based on these factors and other factors considered in its qualitative analysis, the Company believes that it is more likely than not that the fair market value is more than the carrying value of the Water Operation Segment and therefore, no goodwill impairment was recognized in 2016 and 2015.

We may be required to recognize an impairment of goodwill in the future due to market conditions or other factors that are beyond our control and unrelated to our performance. Those market events could include a decline in the forecasted results in our business plan, significant adverse rate case results, changes in capital investment budgets or changes in interest rates that could permanently impair the fair value of a reporting unit. Recognition of impairments of a significant portion of goodwill would negatively impact our reported results of operation and total capitalization, the effects of which could be material and could make it more difficult to maintain our credit ratings, secure financing on favorable terms, maintain compliance with debt covenants and meet expectations of our regulators.

Outlook

The Company's earnings and profitability are primarily dependent upon the sale and distribution of water. In the State of Maine, the amount of water sold and distributed is dependent on seasonal weather fluctuations, particularly during the summer months when water demand will vary with rainfall and temperature levels. The Company's earnings and profitability in future years will also depend upon a number of other factors, such as the ability to maintain our operating costs at current or lower levels, customer growth in the Company's core regulated water utility businesses, growth in revenues attributable to non-water sales operations, availability and desirability of land no longer needed for water delivery for land sales, and the timing and adequacy of rate relief when requested, from time to time, by our Regulated Companies.

The Company believes that the factors described above and those described in detail below under the heading "Commitments and Contingencies" may have significant impact, either alone or in the aggregate, on the Company's earnings and profitability in fiscal years 2017 and beyond. Please also review carefully the risks and uncertainties described in Item 1A – Risk Factors and those described above under the heading "Special Note Regarding Forward Looking Statements".

The Company expects Net Income from its Water Operations segment to increase in 2017 over 2016 levels, primarily due to revenue increases due to the utilization of WISC in Maine and WICA in Connecticut, continued cost containment efforts, modest growth in its Services and Rentals segment and the revenue growth resulting from the acquisitions of The Heritage Water Company and The Avon Water Company. During 2017 and subsequent years, the ability of the Company to maintain and increase its Net Income will principally depend upon the effect on the Company of the factors described above in this "Outlook" section, those factors described in the section entitled "Commitments and Contingencies" and the risks and uncertainties described in the "Special Note Regarding Forward-Looking Statements" and Item 1A "Risk Factors".

FINANCIAL CONDITION

Liquidity and Capital Resources

The Company is not aware of any demands, events, or uncertainties that will result in a decrease of liquidity or a material change in the mix or relative cost of its capital resources, other than those outlined below.

Borrowing Facilities

The Company maintains a \$15 million line of credit agreement with CoBank, ACB, that is currently scheduled to expire on July 1, 2020. The Company maintains an additional line of credit of \$45 million with RBS Citizens, N.A., with an expiration date of April 25, 2021. As of December 31, 2016 the total lines of credit available to the Company were \$60 million. As of December 31, 2016 and 2015, the Company had \$33.0 million and \$16.1 million of "Interim Bank Loans Payable", respectively. As of December 31, 2016, the Company had \$27.0 million in unused lines of credit. Interest expense charged on interim bank loans will fluctuate based on market interest rates.

At December 31, 2016 and 2015, the weighted average interest rates on these short-term borrowings outstanding was 2.7% and 2.4%, respectively.

On March 17, 2015, Maine Water completed the issuance of \$1,864,050 aggregate principal amount of its First Mortgage Bonds, Series Q, 0.01% due March 17, 2035 (the "Series Q Bonds"). The Series Q Bonds were issued by Maine Water to the Bank and the proceeds of the issuance were loaned (the "Series Q Loan") by the Maine Municipal Bond Bank (the "Bank") to Maine Water pursuant to a Loan Agreement by and between Maine Water and the Bank dated as of March 17, 2015. The proceeds of the Series Q Loan were used by Maine Water to fund various water facilities projects, including the replacement of a booster station and modifications to a treatment plant, each located in the City of Biddeford, Maine.

On November 25, 2015, Maine Water completed the issuance of \$2,487,630 aggregate principal amount of its First Mortgage Bonds, Series R, 1.0% due November 25, 2025 (the "Series R Bonds"). The Series R Bonds were issued by Maine Water to the Bank and the proceeds of the issuance were loaned (the "Series R Loan") by the Bank to Maine Water pursuant to a Loan Agreement by and between Maine Water and the Bank dated as of November 25, 2015. The proceeds of the Series R Loan were used by Maine Water to fund the construction of a 3 million gallon water storage tank, located in the City of Biddeford, Maine, which replaced an existing in-ground 7.5 million gallon reservoir.

In April 2016, Connecticut Water filed an application with PURA to issue promissory notes in the aggregate principal amount of up to \$49,930,000 with CoBank, ACB ("CoBank") under its existing Master Loan Agreement by and between Connecticut Water and CoBank dated October 29, 2012, in order for Connecticut Water to redeem its \$19,930,000 2009A Series of

outstanding Water Facility Revenue Bonds previously issued by the Connecticut Development Authority (the “2009A Bonds”) and to provide \$30,000,000 to partially fund its ongoing construction program. On June 1, 2016, Connecticut Water issued \$30,000,000, at 4.36%, in debt under its existing Master Loan Agreement with CoBank, with a maturity date of May 20, 2036. On July 7, 2016, Connecticut Water issued \$19,930,000, at 4.04%, in debt under its existing Master Loan Agreement with CoBank, with a maturity date of July 7, 2036. Connecticut Water used the proceeds to immediately pay off the \$19,930,000 2009A Series of outstanding Water Facility Revenue Bonds.

On January 10, 2017, Maine Water executed and delivered to CoBank a new Promissory Note and Single Advance Term Loan Supplement, dated January 10, 2017 (the “Third Promissory Note”). On the terms and subject to the conditions set forth in the Third Promissory Note issued pursuant to the Agreement, CoBank agreed to make an unsecured loan (the “Loan”) to Maine Water in the principal amount of \$5,000,000 at 4.18%, due December 30, 2026. The proceeds of the Loan will be used to finance new capital expenditures and refinance existing debt owed to the Company, incurred in connection with general water system improvements.

In addition to paying off the 2009 A Series, Due 2039 using the proceeds of the July CoBank issuance discussed above, during the year ending December 31, 2016, the Company paid approximately \$1,035,000 related to Connecticut Water Service’s Term Note Payable issued as part of the 2012 acquisition of Maine Water and approximately \$1,808,000 in sinking funds related to Maine Water’s outstanding bonds.

Capital Budget

In 2016, the Company spent \$66.3 million on capital projects. The Company used a combination of its internally generated funds, borrowings under its lines of credit, the June 2016 long term debt issuance by Connecticut Water, and the March and November 2015 long term debt issuances by Maine Water to fund this construction budget.

The following table shows the total construction expenditures excluding non-cash contributed utility plant for each of the last three years and what we expect to invest on construction projects in 2017.

	Gross Construction Expenditures	Construction Funded by Developers & Others	Construction Funded by Company
2016	\$ 67,887,000	\$ 1,548,000	\$ 66,339,000
2015	\$ 48,555,000	\$ 781,000	\$ 47,774,000
2014	\$ 46,186,000	\$ 1,217,000	\$ 44,969,000
2017 (Projected)	\$ 55,400,000	**	\$ 55,400,000

** – The Company cannot predict the amount of construction funded by others.

Credit Rating

In March 2017, Standard & Poor’s Ratings Services (“S&P”) affirmed its ‘A’ corporate credit rating on the Company. Additionally, S&P also affirmed the Company’s ratings outlook as stable.

Stock Plans

The Company offers a dividend reinvestment and stock purchase plan (“DRIP”) to all registered shareholders, and to the customers and employees of our regulated water companies, whereby participants can opt to have cash dividends directly reinvested into additional shares of the Company. In August 2011, the Board of Directors approved amendments to the DRIP (effective as of January 1, 2012) that permit the Company to add, at the Company’s discretion, an “up to 5.00% purchase price discount” feature to the DRIP which is intended to encourage greater shareholder, customer and employee participation in the DRIP. In August 2014, the Board of Directors approved further amendments to the DRIP to reflect the Company’s appointment of a new common stock transfer agent. During the years ended December 31, 2016 and 2015, participants reinvested \$1,610,000 and \$1,536,000, respectively, as part of the DRIP.

Construction Expenditures

During 2016, the Company incurred approximately \$67.9 million of construction expenditures, including approximately \$1,548,000 funded by developers and others. The Company financed the expenditures through internally generated funds, long-term debt issuances, proceeds from its dividend reinvestment plan, customers' advances, contributions in aid of construction and short-term borrowings.

Our Board of Directors has approved a \$55.4 million construction budget for 2017, net of amounts to be financed by customer advances and contributions in aid of construction. The Company will fund the capital budget through a combination of its internally generated funds, borrowing under its available lines of credit and a potential new debt issuance in 2017.

As the Company looks forward to 2017 and 2018, it anticipates continued reinvestment to replace aging infrastructure and to seek recovery of these costs through periodic WICA and WISC applications. The total cost of that investment may exceed the amount of internally generated funds. The Company expects to rely upon its internally generated funds and short-term borrowing facilities and new debt issuances over the next 12-24 months.

Off-Balance Sheet Arrangements and Contractual Obligations

We do not use off-balance sheet arrangements such as securitization of receivables with any unconsolidated entities or other parties. The Company does not engage in trading or risk management activities and does not have material transactions involving related persons.

The following table summarizes the Company's future contractual cash obligations as of December 31, 2016:

Contractual Obligations	Payments due by Periods				
	<i>(in thousands)</i>				
	Total	Less than 1 year	Years 2 and 3	Years 4 and 5	More than 5 years
Long-Term Debt (LTD)	\$ 205,838	\$ 4,859	\$ 8,536	\$ 6,425	\$ 186,018
Interest on LTD	98,819	8,145	15,504	14,860	60,310
Operating Lease Obligations	209	91	117	1	—
Purchase Obligations (1) (2) (3) (4) (5)	81,437	1,562	3,244	3,147	73,484
Long-Term Compensation Agreements (6)	57,481	5,552	11,406	11,301	29,222
Total (7) (8)	<u>\$ 443,784</u>	<u>\$ 20,209</u>	<u>\$ 38,807</u>	<u>\$ 35,734</u>	<u>\$ 349,034</u>

1. Connecticut Water has an agreement with the South Central Connecticut Regional Water Authority ("RWA") to purchase water from RWA. The agreement was signed in April 2006 and became effective upon the receipt of all regulatory approvals in 2008 and will remain in effect for a minimum of fifty years upon becoming effective. Connecticut Water will pay RWA \$75,000 per year as part of a capacity agreement, for a total of 14 years, starting on the effective date of the agreement. In addition, Connecticut Water is able, but under no obligation, to purchase up to one million gallons of water per day at the then current wholesale rates per the agreement.
2. Connecticut Water has an agreement with The Metropolitan District ("MDC") to purchase water from MDC to serve the Unionville system. The agreement became effective on October 6, 2000 and has a term of fifty years beginning May 19, 2003, the date the water supply facilities related to the agreement were placed in service. Connecticut Water agrees to purchase 283 million gallons of water annually from MDC.
3. Connecticut Water has an agreement with Avon Water ("Avon") to purchase water from Avon. The agreement became effective on October 3, 2008 and has a term of 10 years.
4. Connecticut Water has a 99 year lease with 19 Perry Street to obtain well water for its public water supply system. The agreement became effective in 1975 and is based on current water rates in effect each year. There is no limitation on the amount of water that can be withdrawn from the leased property.
5. Maine Water has an agreement with the Kenebec Water District for potable water service. The agreement was extended and became effective on November 7, 2015 for a new term of 5 years. Maine Water guarantees a minimum consumption of 63.5 million gallons of water annually. Water sales to Maine Water are billed at a flat rate per gallon plus the monthly minimum tariff rate for a 4-inch metered service.
6. Pension and post retirement contributions cannot be reasonably estimated beyond 2017 and may be impacted by such factors as return on pension assets, changes in the number of plan participants and future salary increases.
7. We pay refunds on Advances for Construction over a specific period of time based on operating revenues related to developer-installed water mains or as new customers are connected to and take service from such mains. After all refunds are paid, any remaining balance is transferred to Contributions in Aid of Construction. The refund amounts are not included in the above table because the refund amounts and timing are dependent upon several variables, including new customer connections, customer consumption levels and future rate increases, which cannot be accurately estimated. Portions of these refund amounts are payable annually through 2020 and amounts not paid by the contract expiration dates become non-refundable.
8. We intend to fund these contractual obligations with cash flows from operations and liquidity sources held by or available to us.

In addition to the obligations disclosed in the contractual obligations table above, we have uncertain tax positions of \$9.4 million. Although we believe our tax positions comply with applicable law, we have made judgments as to the sustainability of each uncertain tax position based on its technical merits. Due to the uncertainty of future cash outflows, if any, associated with our uncertain tax positions, we are unable to make a reasonable estimate of the timing or amounts that may be paid.

RESULTS OF OPERATIONS

Overview of 2016 Results from Operations

Net Income for 2016 was \$23,387,000, or \$2.12 basic earnings per share, an increase of \$626,000, or \$0.05 basic earnings per share, compared to 2015. The increase in earnings was principally due to higher net income in our Water Operations segment due to ongoing investment in water infrastructure and the recovery of that investment through WICA and WISC. These investments drove both a revenue increase and lower current income tax expense as a result of the continued application of the Repair Regulations. Changes in net income for our segments were as follows (in thousands):

Business Segment	2016 Net Income	2015 Net Income	Increase (Decrease)
Water Operations	\$ 22,222	\$ 21,018	\$ 1,204
Real Estate	(54)	349	(403)
Services and Rentals	1,219	1,394	(175)
Total	<u>\$ 23,387</u>	<u>\$ 22,761</u>	<u>\$ 626</u>

Water Operations

The increase in net income from Water Operations for 2016 compared to 2015 was \$1,204,000, or 5.7%. The Net Income from Water Operations for the years ended December 31, 2016 and 2015 were each impacted positively by non-recurring items. During the year ended December 31, 2016, the Company reversed incorrectly recorded mark-to-market expense as an out-of-period adjustment resulting in a one-time benefit (reduction) of approximately \$1.6 million in Operation and Maintenance expense. During the twelve months ended December 31, 2015, the Company recorded an approximate \$2.1 million reduction to Income Tax expense related to a June 2015 MPUC approval of a settlement agreement between Maine Water and the State of Maine's Office of Public Advocate that in part allowed for the flow through benefit of Maine Water's adoption of the IRS's Repair Regulations and the reversal of previously established reserves after the completion of an IRS audit of the Company's 2012 federal tax return. The items discussed in detail below reflect the approximate \$1.1 million increase in Net Income related to Water Operations for the year ended December 31, 2016 after the impact of the above non-recurring items. A breakdown of the components of this increase was as follows (in thousands):

	2016	2015	Increase (Decrease)
Operating Revenues	\$ 98,667	\$ 96,041	\$ 2,626
Operation and Maintenance	44,191	48,052	(3,861)
Depreciation	13,905	12,871	1,034
Income Taxes	2,570	(818)	3,388
Taxes Other than Income Taxes	9,796	9,294	502
Other Utility Income	744	797	(53)
Other (Deductions) Income	(1,009)	(214)	(795)
Interest and Debt Expense (net of AFUDC)	5,718	6,207	(489)
Total Net Income from Water Operations	<u>\$ 22,222</u>	<u>\$ 21,018</u>	<u>\$ 1,204</u>

Revenue from our water customers increased by \$2,626,000, or 2.7%, to \$98,667,000 for the year ended December 31, 2016 when compared to the same period in 2015. The primary drivers of higher revenues were the increased rates in 2016 associated with recurring WICA charges in Connecticut and WISC charges in Maine. In 2016, WRA revenues were \$1,132,000 compared to \$1,583,000 in 2015. The reduction in WRA revenues was due primarily to an increase in billed revenues in 2016 compared to 2015.

Operation and Maintenance (“O&M”) expense decreased by \$3,861,000, or 8.0%, during the year ended December 31, 2016 when compared to the 2015 period, primarily due a decrease in expenses related to pension and post-retirement medical costs due to higher discount rates used to determine yearly expense and to the out-of-period adjustment related to stock-based compensation made during 2016. The following table presents the major components of O&M expense (in thousands):

Expense Components	2016	2015	Increase (Decrease)
Mark-to-market	\$ (1,401)	\$ 265	\$ (1,666)
Pension	3,096	4,392	(1,296)
Outside services	3,284	4,224	(940)
Payroll	15,812	16,110	(298)
Post-retirement medical	440	729	(289)
Maintenance	3,312	3,567	(255)
Utility costs	3,899	4,126	(227)
Water treatment (including chemicals)	2,702	2,740	(38)
Property and liability insurance	1,542	1,530	12
Vehicles	1,793	1,666	127
Purchased water	1,675	1,423	252
Customer	1,829	1,494	335
Medical	2,597	2,126	471
Other benefits	1,945	1,211	734
Other	1,666	2,449	(783)
Total	<u>\$ 44,191</u>	<u>\$ 48,052</u>	<u>\$ (3,861)</u>

The changes in individual items are described below:

- The decrease in mark-to-market expense was related to an out-of-period adjustment made during the second quarter of 2016 related to stock-based performance awards previously granted to officers of the Company. The Company had mistakenly marked certain stock-based performance awards classified as equity awards to the market price of the Company’s common stock price at the end of each reporting period. During the second quarter of 2016, the Company reversed all of the incorrectly recorded mark-to-market expense resulting in a one-time benefit of \$2.6 million, including a reversal of approximately \$1.0 million in expense related to the first quarter of 2016 for a net out-of-period adjustment of \$1.6 million;
- Pension and post-retirement medical costs decreased primarily due to an increase in the discount rate used in determining 2016 expense compared to the discount rate used to determine the 2015 expense;
- Outside services expenses decreased in 2016 primarily due to a reduction in costs associated with contractors and consultants. During 2015, the Company was involved in initiatives surrounding succession planning and risk management that were heavily reliant on consultants to assist with assessments prior to the Company implementing the assessments with internal labor;
- Payroll costs decreased in 2016 when compared to 2015 primarily due to the amount of employee time charged to capital projects increasing in 2016 when compared to 2015; and
- Utility costs decreased primarily due to decreased primarily due to a reduction in telephone related expenses, as well as a decrease in heating and electric costs.

The decreases detailed above were offset by the following increases to O&M expense:

- Other benefits increased in 2016 when compared to 2015 primarily due to increased costs associated with a non-officer incentive plan and the Company’s performance stock plan offered to officers;
- Medical costs in 2016 were higher than 2015 primarily due to an increase in medical claims made by employees and their families;
- Customer related expenses increased from 2015 levels due to an increase in uncollectible accounts during 2016 and costs associated with a Company sponsored conservation drive that rewarded customers that were able to reduce their annual consumption by 10%; and
- Purchased water costs increased primarily due to an increase in the amount of water purchased from neighboring utilities, particularly in the Company’s Shoreline Region in Connecticut which has experienced continuing drought conditions throughout 2016.

The Company's Depreciation expense increased \$1,034,000, or 8.0%, when comparing 2016 to 2015. The primary driver of the increase in Depreciation expense was a higher Utility Plant balance in 2016 due to normal plant additions.

Income Tax expense associated with Water Operations increased by \$3,388,000 in the year ended December 31, 2016 when compared to the same period in 2015 due to a higher effective tax rate. The Company had a negative effective tax rate in 2015 primarily due to reversal of previously established provisions, the impact of returning of the repair tax benefit to customers in both Connecticut and Maine and the implementation of the MPUC order allowing flow through treatment of the repair deduction which was recorded in 2015.

Total Interest and Debt Expense, net of Allowance for Funds Used During Construction ("AFUDC") decreased by \$489,000 in the year ended December 31, 2016 when compared to the same period in 2015 due, primarily, to higher AFUDC earnings related to increased construction during 2016 when compared to 2015, partially offset by higher interest costs related to new debt issued by Connecticut Water in 2016 and full year's worth of interest on Maine Water's 2015 issuances.

Real Estate

Income from the Real Estate segment is largely dependent on the tax deductions received on donations and, or, sales of available land. This typically occurs when utility-owned land is deemed to be unnecessary to protect water sources. During 2016, the Company recorded a valuation allowance on a previously completed land donation and the sale of a small parcel of land in Connecticut. These transactions generated \$54,000 in net loss in the Real Estate segment.

During 2015, the Company donated land associated with a previously sold land conservation easement in Connecticut and the sale of three small parcels of land in Maine. These transactions generated \$349,000 in net income in the Real Estate segment.

Other

The increase in net loss seen in the year ended December 31, 2016 in "Other" under "Other Income (Deductions), Net of Taxes" was primarily due to costs due to the acquisitions of Heritage Village and Avon Water.

Overview of 2015 Results from Operations

Net Income for 2015 was \$22,761,000, or \$2.07 basic earnings per share, an increase of \$1,442,000, or \$0.12 basic earnings per share, compared to 2014. The increase in earnings was principally due to higher net income in our Water Operations segment due to ongoing investment in water infrastructure and the recovery of that investment through WICA and WISC. These investments drove both a revenue increase and lower current income tax expense as a result of the continued application of the Repair Regulations. Changes in net income for our segments were as follows (in thousands):

Business Segment	2015 Net Income	2014 Net Income	Increase (Decrease)
Water Operations	\$ 21,018	\$ 19,798	\$ 1,220
Real Estate	349	50	299
Services and Rentals	1,394	1,471	(77)
Total	\$ 22,761	\$ 21,319	\$ 1,442

Water Operations

The increase in net income from Water Operations for 2015 compared to 2014 was \$1,220,000, or 6.2%. A breakdown of the components of this increase was as follows (in thousands):

	2015	2014	Increase (Decrease)
Operating Revenues	\$ 96,041	\$ 94,020	\$ 2,021
Operation and Maintenance	48,052	44,445	3,607
Depreciation	12,871	11,784	1,087
Income Taxes	(818)	3,596	(4,414)
Taxes Other than Income Taxes	9,294	9,031	263
Other Utility Income	797	833	(36)
Other (Deductions) Income	(214)	(202)	(12)
Interest and Debt Expense (net of AFUDC)	6,207	5,997	210
Total Net Income from Water Operations	\$ 21,018	\$ 19,798	\$ 1,220

Revenue from our water customers increased by \$2,021,000, or 2.1%, to \$96,041,000 for the year ended December 31, 2015 when compared to the same period in 2014. The primary drivers of higher revenues were the increased rates in 2015 associated with recurring WICA charges and increased rates in almost all of Maine Water's service areas due to both WISC filings and regular rate cases. In 2015, WRA revenues were \$1,583,000 compared to \$3,700,000 in 2014. The reduction in WRA revenues was due primarily to an increase in billed revenues in 2015 compared to 2014.

Operation and Maintenance ("O&M") expense increased in 2015 by \$3,607,000, or 8.1%, during the year ended December 31, 2015 when compared to the 2014 period primarily due to a increase in employee benefit costs and the use of outside services. The following table presents the major components of O&M expense (in thousands):

Expense Components	2015	2014	Increase (Decrease)
Pension	\$ 4,382	\$ 2,738	\$ 1,644
Outside services	4,224	2,594	1,630
Payroll	16,110	15,280	830
Utility costs	4,126	3,757	369
Maintenance	3,567	3,205	362
Post-retirement medical	729	575	154
Investor relations	770	631	139
Property and liability insurance	1,530	1,424	106
Vehicles	1,666	1,767	(101)
Water treatment (including chemicals)	2,740	2,936	(196)
Customer	1,494	1,719	(225)
Medical	2,126	2,557	(431)
Other benefits	1,211	1,809	(598)
Other	3,377	3,453	(76)
Total	\$ 48,052	\$ 44,445	\$ 3,607

The changes in individual items are described below:

- Pension and post-retirement medical costs increased over the prior year primarily due to a decrease to the discount rate used in determining the 2015 expense. The discount rate selected to calculate the pension and post-retirement medical expenses for 2016 is higher than the rate used for 2015 which will likely cause 2016 pension and post-retirement medical expenses to be lower than 2015 expense;
- Outside services expenses increased in 2015 primarily due to costs associated with Company initiatives surrounding succession planning and risk management and the use of consultants to assist for tax related matters and water quality compliance. Additionally, the Company saw continued costs associated with its ongoing cyber security improvements discussed above. These increases were partially offset by a reduction in legal costs throughout 2015;
- Payroll costs increased in 2015 when compared to 2014 primarily due to regular wage increases;
- Utility costs increased primarily due to increased electrical fees charged by our electric suppliers and higher phone costs in 2015. These increases were partially offset by lower costs associated with fuel oil;
- Investor relation fees increased primarily as the result of increased efforts by senior leadership related to investor outreach throughout 2015 and higher expenses related to the Board of Directors; and
- Property and liability insurance costs increased in 2015 due to higher premiums stemming from growth in insurable assets.

The increases detailed above were offset by the following decreases to O&M expense:

- Other benefits decreased in 2015 when compared to 2014 primarily due to reduced costs associated with a non-officer incentive plan and the Company's performance stock plan offered to officers;
- Medical costs in 2015 were lower than 2014 primarily due to a reduction in medical claims made by employees and their families, partially offset by an increase in the administration of the Company's medical plan;
- Customer related expenses decreased from 2014 levels due to a reduction in uncollectible accounts during 2015, partially offset by higher customer communication costs; and
- Water treatment costs decreased primarily due to a reduction in laboratory testing costs as a result of Connecticut Water now performing most test internally rather than through an outside vendor and lower costs associated with the disposal of certain treatment by-products. Maine Water has historically handled most of their testing in house.

The Company's Depreciation expense increased \$1,087,000, or 9.2%, when comparing 2015 to 2014. The primary driver of the increase in Depreciation expense was a higher Utility Plant balance in 2015 due to normal plant additions.

Income Tax expense associated with Water Operations decreased by \$4,414,000 in the year ended December 31, 2015 when compared to the same period in 2014 due to a lower effective tax rate. The Company's effective tax rate decreased in 2015 primarily due to reversal of previously established provisions, the impact of returning of the repair tax benefit to customers in both Connecticut and Maine and the implementation of the MPUC order allowing flow through treatment of the repair deduction which was recorded in 2015.

Total Interest and Debt Expense, net of Allowance for Funds Used During Construction ("AFUDC") increased by \$210,000 in the year ended December 31, 2015 when compared to the same period in 2014 due, primarily, to higher interest costs related to new debt issuances by Maine Water.

Real Estate

Income from the Real Estate segment is largely dependent on the tax deductions received on donations and, or, sales of available land. This typically occurs when utility-owned land is deemed to be unnecessary to protect water sources. During 2015, the Company donated land associated with a previously sold land conservation easement in Connecticut and the sale of three small parcels of land in Maine. These transactions generated \$349,000 in net income in the Real Estate segment.

During 2014, the Company completed the sale of two small properties which generated \$50,000 of net income in the Real Estate segment.

COMMITMENTS AND CONTINGENCIES

Water Supply – Connecticut Water has an agreement with the RWA to purchase water from RWA. The agreement was signed April 2006 and became effective upon the receipt of all regulatory approvals in 2008 and remains in effect for a minimum of fifty years upon the effective date. Connecticut Water will pay RWA \$75,000 per year, for a total of 14 years, starting on the effective date of the agreement. In addition, Connecticut Water is able, but under no obligation, to purchase up to one million gallons of water per day at the then current wholesale rates per the agreement. Connecticut Water has an agreement with the MDC to purchase water from MDC to serve the Unionville system. The agreement became effective on October 6, 2000 and has a term of fifty years beginning May 19, 2003, the date the water supply facilities related to the agreement were placed in service. Connecticut Water agrees to purchase 283 million gallons of water annually from MDC. Connecticut Water has an agreement with Avon to purchase twelve million gallons per year from Avon. The agreement became effective on October 3, 2008 and has a term of 10 years. Connecticut Water has a 99 year lease with 19 Perry Street to obtain well water for its public water supply system. The agreement became effective in 1975 and is based on current water rates in effect each year. There is no limitation on the amount of water that can be withdrawn from the leased property. Maine Water has an agreement with the Kennebec Water District for potable water service. The agreement was extended and became effective on November 7, 2015 for a new term of 5 years. Water sales to Maine Water are billed at a flat rate per gallon plus the monthly minimum tariff rate for a 4-inch metered service. During 2016, 2015, and 2014, the Company spent \$1,556,000, \$1,112,000 and \$3,700,000, respectively, on these agreements. The Company's expected payments related to these agreements for the years 2017 through 2021 will be as follows:

(in thousands)

2017	\$	1,562
2018	\$	1,601
2019	\$	1,643
2020	\$	1,601
2021	\$	1,546

Reviews by Taxing Authorities – On June 11, 2013, the Company was notified by the Connecticut Department of Revenue Services that its state tax filings for the years 2009 through 2011 would be reviewed beginning in the fourth quarter of 2013. On March 24, 2015, the Company was notified by the Connecticut Department of Revenue Services that the audit was expanded to include the 2012 and 2013 tax years. The State focused its review on tax credits associated with fixed capital investment. The Company and the State came to an agreement (“Closing Agreement”) regarding investments eligible for the credit. The Closing Agreement was executed on May 4, 2015. The Company had previously recorded a provision for the possible disallowance of these credits and, therefore, there was minimal impact in 2015.

On the 2012 tax return, filed in September 2013, Connecticut Water filed a change in accounting method to adopt the IRS's temporary tangible property regulations. On the 2013 Federal tax return, filed in September 2014, Maine Water filed the same change in accounting method. This method change allowed the Company to take a current year deduction for expenses that were previously capitalized for tax purposes. Since the filing of the 2012 tax return, the IRS has issued final regulations. On February 11, 2014, the Company was notified by the IRS that its Federal tax filing for 2012 would be reviewed. This review, which began in the first quarter of 2014 and was completed in the first quarter of 2015, resulted in no change to the tax liability. Since the Company had previously recorded a provision for the possible disallowance of the repair deduction in prior periods, the completion of the audit resulted in the reversal of the reserves in the amount of \$1,185,000. While the Company maintains the belief that the deduction taken on its tax return is appropriate, the methodology for determining the deduction has not been agreed to by the taxing authorities. Therefore, as required by FASB ASC 740, during the year ended December 31, 2016, the Company recorded a provision of \$3.1 million for a portion of the benefit that is not being returned to customers resulting from any possible tax authority challenge. The Company had previously recorded a provision of \$6.3 million in the prior year for a cumulative total of \$9.4 million.

The Company remains subject to examination by federal tax authorities for the 2013 through 2015 tax years; the State of Maine's tax authorities for the 2013 through 2015 tax years; and the State of Connecticut's tax authorities for the 2014 and 2015 tax years.

Environmental and Water Quality Regulation – The Company is subject to environmental and water quality regulations. Costs to comply with environmental and water quality regulations are substantial. We are presently in compliance

with current regulations, but the regulations are subject to change at any time. The costs to comply with future changes in state or federal regulations, which could require us to modify current filtration facilities and/or construct new ones, or to replace any reduction of the safe yield from any of our current sources of supply, could be substantial.

Legal Proceedings – We are involved in various legal proceedings from time to time. Although the results of legal proceedings cannot be predicted with certainty, there are no pending legal proceedings to which we, or any of our subsidiaries are a party, or to which any of our properties is subject, that presents a reasonable likelihood of a material adverse impact on the Company’s financial condition, results of operations or cash flows.

Rate Relief – Connecticut Water and Maine Water are regulated public utilities, which provide water services to their customers. The rates that Regulated Companies charge their water customers are subject to the jurisdiction of the regulatory authority of the PURA in Connecticut and the MPUC in Maine. Connecticut Water’s allowed rate of return on equity and return on rate base are currently 9.75% and 7.32%, respectively. Maine Water’s average allowed return on equity and return on rate base, as of December 31, 2016 were 9.50% and 7.96%, respectively.

Land Dispositions – The Company and its subsidiaries own additional parcels of land in Connecticut and Maine, which may be suitable in the future for disposition or for further protection through conservation easements, through sale or by donation to municipalities, other local governments or private charitable entities such as local land trusts. In Connecticut, these additional parcels would include certain Class I and II parcels previously identified for long term conservation by the Connecticut DEEP, which have restrictions on development and resale based on provisions of the Connecticut General Statutes. In Maine, these parcels include primarily company-owned land used for water supply protection, and a permanent conservation easement may be appropriate for some parcels to ensure the permanent protection of the watersheds, while balancing the appropriate community and recreational use of the land.

Capital Expenditures – The Company has received approval from its Board of Directors to spend \$55.4 million on capital expenditures in 2017, in part to fund improvements to water treatment plants and increased spending related to infrastructure improvements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

The primary market risk faced by the Company is interest rate risk. As of December 31, 2016, the Company had no exposure to derivative financial instruments or financial instruments with significant credit risk or off-balance-sheet risks. In addition, the Company is not subject in any material respect to any currency or other commodity risk.

The Company is subject to the risk of fluctuating interest rates in the normal course of business. The Company’s exposure to interest fluctuations is managed at the Company and subsidiary operations levels through the use of a combination of fixed rate long-term debt (and variable rate borrowings) under financing arrangements entered into by the Company and its subsidiaries. The Company has entered into a \$15 million line of credit agreement with CoBank, ACB, that is currently scheduled to expire on July 1, 2020. The Company maintains an additional line of credit of \$45 million with RBS Citizens, N.A., with an expiration date of April 25, 2021. As of December 31, 2016 the total lines of credit available to the Company were \$60 million. As of December 31, 2016 and 2015, the Company had \$33.0 million and \$16.1 million of “Interim Bank Loans Payable”, respectively. As of December 31, 2016, the Company had \$27.0 million in unused lines of credit. Interest expense charged on interim bank loans will fluctuate based on market interest rates.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The “Consolidated Financial Statements” of Connecticut Water Service, Inc., and the “Notes to Consolidated Financial Statements”, together with the reports of Baker Tilly Virchow Krause, LLP independent registered public accounting firm, are included herein on pages 46 through 82.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

ITEM 9A. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures – As of December 31, 2016, management, including the Company’s Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of the Company’s disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)). Based upon, and as of the date of that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company’s disclosure controls and procedures were effective.

Management’s Report on Internal Control Over Financial Reporting – Internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) 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.

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. We have used the criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) in conducting our evaluation of the effectiveness of the internal control over financial reporting. Based on our evaluation, we concluded that the Company’s internal control over financial reporting was effective as of December 31, 2016. The effectiveness of the Company’s internal control over financial reporting as of December 31, 2016 has been audited by Baker Tilly Virchow Krause, LLP, an independent registered public accounting firm, as stated in their report which appears herein.

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.

Changes in Internal Control Over Financial Reporting – There were no significant changes in the Company’s internal control over financial reporting that occurred during the Company’s most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders
Connecticut Water Service, Inc.

We have audited Connecticut Water Service, Inc.'s (the "Company") internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework). Connecticut Water Service, Inc.'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.

An entity'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. An entity'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 entity; (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 entity are being made only in accordance with authorizations of management and directors of the entity; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the entity'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, Connecticut Water Service, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets and related consolidated statements of income, comprehensive income and cash flows of Connecticut Water Service, Inc., as well as the financial statement schedule listed in the accompanying index, and our report dated March 13, 2017 expressed an unqualified opinion.

/s/ Baker Tilly Virchow Krause, LLP

Philadelphia, Pennsylvania
March 13, 2017

ITEM 9B. OTHER INFORMATION

None

PART III

Pursuant to General Instruction G(3), the information called for by Items 10, 11, 12, 13 and 14 is hereby incorporated by reference to the Company's definitive proxy statement to be filed in EDGAR on or about March 30, 2017 in connection with the annual meeting to be held on May 11, 2017. Certain information concerning the executive officers of the Company is included in Item 1 of this report.

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

ITEM 11. EXECUTIVE COMPENSATION

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a)	1	Financial Statements:	<u>Page</u>
		Index to Consolidated Financial Statements and Schedule	46
		Report of Independent Registered Public Accounting Firm	47
		Consolidated Statements of Income for the years ended December 31, 2016, 2015 and 2014	48
		Consolidated Statements of Comprehensive Income for the years ended December 31, 2016, 2015 and 2014	48
		Consolidated Balance Sheets at December 31, 2016 and 2015	49
		Consolidated Statements of Cash Flows for the years ended December 31, 2016, 2015 and 2014	50
		Notes to Consolidated Financial Statements	51
	2	Financial Statement Schedule:	
		The following schedule of the Company is included on the attached page as indicated	
		Schedule II Valuation and Qualifying Accounts and Reserves for the years ended December 31, 2016, 2015 and 2014	89
		All other schedules provided for in the applicable regulations of the Securities and Exchange Commission have been omitted because of the absence of conditions under which they are required or because the required information is set forth in the financial statements or notes thereto.	
(b)		Exhibits	
		Exhibits for Connecticut Water Service Inc., are in the Index to Exhibits	83
		Exhibits heretofore filed with the Securities and Exchange Commission as indicated below are incorporated herein by reference and made a part hereof as if filed herewith. Exhibits marked by asterisk (* or **) are being filed or furnished herewith.	

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND SCHEDULE

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Report of Independent Registered Public Accounting Firm	47
Consolidated Statements of Income for the years ended December 31, 2016, 2015 and 2014	48
Consolidated Statements of Comprehensive Income for the years ended December 31, 2016, 2015 and 2014	48
Consolidated Balance Sheets at December 31, 2016 and 2015	49
Consolidated Statements of Cash Flows for the years ended December 31, 2016, 2015 and 2014	50
Notes to Consolidated Financial Statements	51
Schedule II Valuation and Qualifying Accounts and Reserves for the years ended December 31, 2016, 2015 and 2014	89

Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders
Connecticut Water Service, Inc.

We have audited the accompanying consolidated balance sheets of Connecticut Water Service, Inc. (the “Company”) as of December 31, 2016 and 2015, and the related consolidated statements of income, comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2016. In connection with our audits of the consolidated financial statements, we have also audited the financial statement schedule listed in the accompanying index. These consolidated financial statements and financial statement schedule are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Connecticut Water Service, Inc. as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2016, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly, in all material respect, the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Connecticut Water Service, Inc.’s internal control over financial reporting as of December 31, 2016, based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated March 13, 2017 expressed an unqualified opinion.

/s/ Baker Tilly Virchow Krause, LLP

Philadelphia, Pennsylvania
March 13, 2017

CONNECTICUT WATER SERVICE, INC.

CONSOLIDATED STATEMENTS OF INCOME

For the Years Ended December 31, (in thousands, except per share data)

	2016	2015	2014
Operating Revenues	\$ 98,667	\$ 96,041	\$ 94,020
Operating Expenses			
Operation and Maintenance	44,191	48,052	44,445
Depreciation	13,905	12,871	11,784
Income Taxes	2,570	(818)	3,596
Taxes Other Than Income Taxes	9,796	9,294	9,031
Total Operating Expenses	70,462	69,399	68,856
Net Operating Revenues	28,205	26,642	25,164
Other Utility Income, Net of Taxes	744	797	833
Total Utility Operating Income	28,949	27,439	25,997
Other Income (Deductions), Net of Taxes			
(Loss) Gain on Real Estate Transactions	(54)	349	50
Non-Water Sales Earnings	1,219	1,394	1,471
Allowance for Funds Used During Construction	1,198	530	518
Other	(1,009)	(214)	(202)
Total Other Income, Net of Taxes	1,354	2,059	1,837
Interest and Debt Expenses			
Interest on Long-Term Debt	7,714	7,087	7,023
Other Interest Income, Net	(922)	(458)	(573)
Amortization of Debt Expense and Premium, Net	124	108	65
Total Interest and Debt Expenses	6,916	6,737	6,515
Net Income	23,387	22,761	21,319
Preferred Stock Dividend Requirement	38	38	38
Total Net Income Applicable to Common Stock	\$ 23,349	\$ 22,723	\$ 21,281
Weighted Average Common Shares Outstanding:			
Basic	11,009	10,958	10,893
Diluted	11,228	11,164	11,091
Earnings Per Common Share:			
Basic	\$ 2.12	\$ 2.07	\$ 1.95
Diluted	\$ 2.08	\$ 2.04	\$ 1.92

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

For the Years Ended December 31, (in thousands)

	2016	2015	2014
Net Income	\$ 23,387	\$ 22,761	\$ 21,319
Other Comprehensive Income (Loss), net of tax			
Adjustment to post-retirement benefit plans, net of tax benefit (expense) of \$15, \$(505), and \$735 in 2016, 2015, and 2014, respectively	(24)	765	(1,527)
Unrealized Investment gain (loss), net of tax (expense) benefit of \$(22), \$62 and \$(25), in 2016, 2015, and 2014, respectively	35	(97)	39
Other Comprehensive Income (Loss), net of tax	\$ 11	\$ 668	\$ (1,488)
Comprehensive Income	\$ 23,398	\$ 23,429	\$ 19,831

The accompanying notes are an integral part of these Consolidated Financial Statements.

CONNECTICUT WATER SERVICE, INC.

CONSOLIDATED BALANCE SHEETS

December 31, (in thousands, except share amounts)

	2016	2015
ASSETS		
Utility Plant	\$ 777,860	\$ 722,447
Construction Work in Progress	33,748	23,298
	<u>811,608</u>	<u>745,745</u>
Accumulated Provision for Depreciation	(210,212)	(199,461)
Net Utility Plant	<u>601,396</u>	<u>546,284</u>
Other Property and Investments	9,071	8,126
Cash and Cash Equivalents	1,564	731
Accounts Receivable (Less Allowance, 2016 - \$1,100; 2015 - \$947)	13,024	11,012
Accrued Unbilled Revenues	8,171	8,259
Materials and Supplies, at Average Cost	1,536	1,617
Prepayments and Other Current Assets	5,069	5,393
Total Current Assets	<u>29,364</u>	<u>27,012</u>
Restricted Cash	—	846
Unrecovered Income Taxes - Regulatory Asset	93,264	77,510
Pension Benefits - Regulatory Asset	12,266	12,414
Post-Retirement Benefits Other Than Pension - Regulatory Asset	265	468
Goodwill	30,427	30,427
Deferred Charges and Other Costs	8,449	7,628
Total Regulatory and Other Long-Term Assets	<u>144,671</u>	<u>129,293</u>
Total Assets	<u>\$ 784,502</u>	<u>\$ 710,715</u>
CAPITALIZATION AND LIABILITIES		
Common Stockholders' Equity:		
Common Stock Without Par Value: Authorized - 25,000,000 Shares		
Issued and Outstanding: 2016 - 11,248,458; 2015 - 11,192,882	\$ 145,739	\$ 144,534
Retained Earnings	91,213	80,378
Accumulated Other Comprehensive Loss	(924)	(935)
Common Stockholders' Equity	<u>236,028</u>	<u>223,977</u>
Preferred Stock	772	772
Long-Term Debt	197,047	171,868
Total Capitalization	<u>433,847</u>	<u>396,617</u>
Current Portion of Long-Term Debt	4,859	2,842
Interim Bank Loans Payable	32,953	16,085
Accounts Payable and Accrued Expenses	13,116	11,882
Accrued Interest	1,012	727
Current Portion of Refund to Customers - Regulatory Liability	855	2,994
Other Current Liabilities	2,330	2,409
Total Current Liabilities	<u>55,125</u>	<u>36,939</u>
Advances for Construction	19,127	21,444
Deferred Federal and State Income Taxes	50,558	48,036
Unfunded Future Income Taxes	90,977	74,712
Long-Term Compensation Arrangements	33,540	34,389
Unamortized Investment Tax Credits - Regulatory Liability	1,189	1,264
Refund to Customers - Regulatory Liability	108	993
Other Long-Term Liabilities	5,074	5,273
Total Long-Term Liabilities	<u>200,573</u>	<u>186,111</u>
Contributions in Aid of Construction	94,957	91,048
Commitments and Contingencies	—	—
Total Capitalization and Liabilities	<u>\$ 784,502</u>	<u>\$ 710,715</u>

The accompanying notes are an integral part of these Consolidated Financial Statements.

CONNECTICUT WATER SERVICE, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Years Ended December 31, (in thousands)

	2016	2015	2014
Operating Activities:			
Net Income	\$ 23,387	\$ 22,761	\$ 21,319
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:			
Deferred Revenues	(893)	(1,344)	(3,461)
Provision for Deferred Income Taxes and Investment Tax Credits, Net	2,950	(7,502)	5,878
Allowance for Funds Used During Construction	(1,198)	(530)	(518)
Depreciation and Amortization (including \$732 in 2016, \$27 in 2015, and \$673 in 2014 charged to other accounts)	13,173	12,898	12,457
Loss (Gain) on Real Estate Transactions	54	(349)	(50)
Change in Assets and Liabilities:			
(Increase) Decrease in Accounts Receivable and Accrued Unbilled Revenues	(1,925)	984	(291)
Decrease (Increase) in Other Current Assets	338	6,540	(5,012)
(Increase) Decrease in Other Non-Current Items, Net	(2,741)	11,383	(1,286)
Increase (Decrease) in Accounts Payable, Accrued Expenses and Other Current Liabilities	176	(3,695)	1,169
Total Adjustments	9,934	18,385	8,886
Net Cash and Cash Equivalents Provided by Operating Activities	33,321	41,146	30,205
Investing Activities:			
Additions to Utility Plant	(66,689)	(48,025)	(45,668)
Proceeds on Real Estate Transactions	9	14	243
Release (Receipt) of Restricted Cash	846	(846)	5,779
Net Cash and Cash Equivalents Used in Investing Activities	(65,834)	(48,857)	(39,646)
Financing Activities:			
Net Proceeds from Interim Bank Loans	32,953	16,085	1,991
Net Repayment of Interim Bank Loans	(16,085)	(1,991)	—
Repayment of Long-Term Debt	(22,772)	(2,476)	(4,114)
Proceeds from Issuance of Long-Term Debt	49,930	4,352	4,500
Proceeds from Issuance of Common Stock	1,610	1,536	1,697
Costs Incurred to Issue Long-Term Debt and Common Stock	(88)	(37)	(2)
Advances from Others for Construction	350	251	699
Cash Dividends Paid	(12,552)	(11,753)	(11,226)
Net Cash and Cash Equivalents Provided by (Used in) Financing Activities	33,346	5,967	(6,455)
Net (Decrease) Increase in Cash and Cash Equivalents	833	(1,744)	(15,896)
Cash and Cash Equivalents at Beginning of Year	731	2,475	18,371
Cash and Cash Equivalents at End of Year	\$ 1,564	\$ 731	\$ 2,475
Non-Cash Investing and Financing Activities:			
Non-Cash Contributed Utility Plant (see Note 1 for details)	\$ 1,394	\$ 1,282	\$ 1,130
Supplemental Disclosures of Cash Flow Information:			
Cash Paid During the Year for:			
Interest	\$ 6,678	\$ 6,761	\$ 6,665
State and Federal Income Taxes	\$ 445	\$ 537	\$ 1,135

The accompanying notes are an integral part of these Consolidated Financial Statements.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION – The Consolidated Financial Statements include the operations of Connecticut Water Service, Inc. (the “Company”), an investor-owned holding company and its wholly-owned subsidiaries, including:

The Connecticut Water Company (“Connecticut Water”)
The Maine Water Company (“Maine Water”)
Chester Realty, Inc. (“Chester Realty”)
New England Water Utility Services, Inc. (“NEWUS”)
The Barnstable Holding Company (“Barnstable Holding”) - Inactive

As of December 31, 2016, Connecticut Water and Maine Water were our regulated public water utility companies (collectively the “Regulated Companies”), which together served 124,968 customers in 77 towns throughout Connecticut and Maine.

Chester Realty is a real estate company whose net profits from rental of property are included in the “Other Income (Deductions), Net of Taxes” section of the Consolidated Statements of Income in the “Non-Water Sales Earnings” category.

NEWUS is engaged in water-related services, including the *Linebacker*[®] program, emergency drinking water, pool water and contract operations. Its earnings are included in the “Non-Water Sales Earnings” category of the Consolidated Statements of Income.

Intercompany accounts and transactions have been eliminated.

During the preparation of the Condensed Consolidated Financial Statements for the quarter ended June 30, 2016, the Company identified two errors related to the accounting treatment of stock-based performance awards granted to officers of the Company. First, the Company had mistakenly classified a portion of its stock-based performance awards as equity awards and, secondly, incorrectly marked those awards to the market price of the Company’s common stock price at the end of each reporting period. A portion of these awards should have been classified as liability awards and only those awards should have been marked-to-market based on the Company’s common stock price. During the second quarter of 2016, the Company reversed all of the incorrectly recorded mark-to-market expense as a cumulative out-of-period adjustment resulting in a one-time benefit of approximately \$2.6 million on the Operation and Maintenance line item on its Condensed Consolidated Statements of Income for the three months ended June 30, 2016 and \$1.6 million for the six months ended June 30, 2016. Approximately \$1.6 million of the out of period adjustment pertained to years prior to 2016, with the remaining \$1.0 million related to the first quarter of 2016. Additionally, the Company decreased its Common Stock Without Par Value and increased its Long-Term Compensation Arrangement line items on the Condensed Consolidated Balance Sheet as of June 30, 2016 by approximately \$0.6 million to reflect both the awards that should have been classified as liability awards and their corresponding mark-to-market adjustments.

The Company performed various quantitative and qualitative analyses and determined that these errors were not material to the previously reported quarterly and annual results. The Company also determined that recording these entries as an out-of-period adjustment during the second quarter of 2016 was not material to the full year ended December 31, 2016 results of operations.

PUBLIC UTILITY REGULATION – Connecticut Water is subject to regulation for rates and other matters by the Connecticut Public Utility Regulatory Authority (“PURA”) and follows accounting policies prescribed by the PURA. Maine Water is subject to regulation for rates and other matters by the Maine Public Utilities Commission (“MPUC”). The Company prepares its financial statements in accordance with accounting principles generally accepted in the United States of America (“GAAP”), which includes the provisions of Financial Accounting Standards Board’s (“FASB”) Accounting Standards Codification (“ASC”) 980 “Regulated Operations” (“FASB ASC 980”). FASB ASC 980 requires cost-based, rate-regulated enterprises, such as Connecticut Water and Maine Water, to reflect the impact of regulatory decisions in their financial statements. The state regulators, through the rate regulation process, can create regulatory assets and liabilities that result when costs and benefits are allowed for ratemaking purposes in a period after the period in which the costs or benefits would be charged to expense by an unregulated enterprise. The Consolidated Balance Sheets include regulatory assets and liabilities as appropriate, primarily related to income taxes, post-retirement benefit costs and deferred revenues associated with the Water Revenue Adjustment (“WRA”) used by Connecticut Water. In accordance with FASB ASC 980, costs which benefit future periods are amortized over the periods they benefit. The Company believes, based on current regulatory circumstances, that the regulatory assets recorded are probable to be recovered and that its use of regulatory accounting is appropriate and in accordance with the provisions of FASB ASC 980.

CONNECTICUT WATER SERVICE, INC.

Regulatory assets and liabilities are comprised of the following:

<i>(in thousands)</i>	December 31,	
	2016	2015
Assets:		
Pension Benefits and Post-Retirement Benefits Other Than Pension	\$ 12,531	\$ 12,882
Unrecovered Income Taxes	93,264	77,510
Deferred revenue (included in Prepayments and Other Current Assets and Deferred Charges and Other Costs)	3,910	5,033
Other (included in Prepayments and Other Current Assets and Deferred Charges and Other Costs)	4,276	3,561
Total regulatory assets	\$ 113,981	\$ 98,986
Liabilities:		
Other (included in Other Current Liabilities)	\$ 1,710	\$ 1,567
Unamortized Investment Tax Credits	1,189	1,264
Refunds to Customers (including Current Portion of Refund to Customers)	963	3,987
Unfunded Future Income Taxes (including Other Long-Term Liabilities)	90,977	74,712
Total regulatory liabilities	\$ 94,839	\$ 81,530

Pension and post-retirement benefits include costs in excess of amounts funded. The Company believes these costs will be recoverable in future years, through rates, as funding is required and has recorded regulatory assets for those costs. The recovery period is dependent on contributions made to the plans and remaining life expectancy.

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 are recognized as unrecovered future income taxes that will be recovered in rates in future years as they reverse. In addition, basis differences resulting from the repair tax deduction adopted in 2013 contribute to the change in unfunded future income taxes.

Deferred revenue represents a portion of the rate increase granted in Connecticut Water's 2007 rate decision. The PURA decision required the Company to defer for future collection, beginning in 2008, a portion of the increase. Additionally, revenue recorded under the WRA, discussed below, is included in deferred revenue.

Regulatory liabilities include deferred investment tax credits and amounts to be refunded to customers as a result of the adoption of the tangible property regulations in Connecticut and Maine. These liabilities will be given back to customers in rates as tax deductions occur in the future.

Regulatory Matters

The rates we charge our customers in Connecticut and Maine are established under the jurisdiction of and are approved by the PURA and MPUC, respectively. It is our policy to seek rate relief as necessary to enable us to achieve an adequate rate of return. Connecticut Water's allowed return on equity and return on rate base, effective as of December 31, 2016 were 9.75% and 7.32%, respectively. Maine Water's average allowed return on equity and return on rate base, as of December 31, 2016 were 9.50% and 7.96%, respectively. The PURA establishes rates in Connecticut on a company-wide basis while the MPUC approves Maine Water's rates on a division-by-division basis. Both Connecticut Water and Maine Water are permitted to add surcharges to customers' bills in order to recover certain approved capital projects in between full rate cases, as well as approved surcharges for Water Revenue Adjustments in Connecticut, as discussed in more detail below.

University of Connecticut Agreement

Connecticut Water and the University of Connecticut ("UCONN") negotiated a definitive agreement for Connecticut Water to provide a long-term supply of potable water for UCONN's Storrs campus facilities which was approved by the Board of Trustees at their December 11, 2013 meeting and executed on December 18, 2013. The definitive agreement is consistent with the requirements of the project's Environmental Impact Evaluation ("EIE") and record of decision, as approved by the Office of Policy and Management, an agency of the State of Connecticut, that identified the Company as the preferred option to supply UCONN and the Town of Mansfield, Connecticut with up to 2.2 million gallons of water per day over the next 47 years. Connecticut Water will fund a 5-mile pipeline from Tolland and other necessary infrastructure improvements at no cost to

UCONN, the Town or the state's taxpayers to serve the area. The Company was responsible for obtaining any required regulatory permits, licenses and approvals to implement the water supply solution, including but not limited to those from PURA, the Connecticut Department of Energy and Environmental Protection ("DEEP") and the Connecticut Department of Public Health ("DPH"). The capital improvements were completed on time and the pipeline was connected to the UCONN campus in December 2016, which was within the agreed upon timeframe.

Town of Mansfield Agreement

Connecticut Water and the Town of Mansfield entered into an agreement for Connecticut Water to serve the Town of Mansfield community. On January 13, 2014, the Mansfield Town Council voted to authorize the Town Manager to execute the agreement with Connecticut Water and it was signed by the parties on January 21, 2014.

The key provisions of the agreement with the Town of Mansfield are as follows:

- Current off-campus customers of UCONN will become customers of Connecticut Water at UCONN's water rates in effect at that time (subject to any state-approved surcharges);
- Future water customers in the Town of Mansfield will be served by Connecticut Water at the rates authorized by the PURA;
- Connecticut Water will assume responsibility for maintaining, repairing and replacing the off-campus water system serving the Town of Mansfield;
- Connecticut Water will make any source or system improvements to meet current and future water supply needs of the area; and
- Pursuant to the Agreement, a Water System Advisory Committee ("WSAC") was created with representatives of the Town of Mansfield, UCONN, regional representatives and other key stakeholders to advise Connecticut Water regarding water service and the system's operations, expansion or integration as well as recommended best management practices, including water conservation programs. The WSAC meets quarterly.

The former off-campus customers of UCONN in the Town of Mansfield became customers of Connecticut Water in December 2016.

Avon Water Company Acquisition

On October 11, 2016, the Company entered into an Agreement and Plan of Merger (the "Avon Agreement") with The Avon Water Company, a specially-chartered Connecticut corporation ("Avon Water"). Founded in 1911, Avon Water serves about 4,800 customers in the Farmington Valley communities of Avon, Farmington, and Simsbury, Connecticut, and is located near Connecticut Water's existing operations in Avon and Farmington.

The Boards of Directors of the Company and Avon Water have each unanimously approved the Avon Agreement and the transactions contemplated thereby. Consummation of the merger is subject to regulatory, Avon Water shareholder and other specified approvals described below and is expected to be consummated by the end of the third quarter of 2017.

Under the terms of the Avon Agreement, each of the 121,989 Avon Water common stock shares outstanding at the time of the closing of the merger will be exchanged and converted into the right to receive the following merger consideration: (i) a cash payment of \$50.37; and (ii) a stock consideration component, consisting of 4.38 shares of Company Common Stock, provided that the Company's Share Price (as defined below) over a specified period prior to the closing date of the merger is equal to or greater than \$45.00 but less than or equal to \$52.00. If the Company's Share Price is less than \$45.00 as of the closing date, each share of Avon Water common stock issued and outstanding at the time of the closing of the merger will be exchanged and converted into the right to receive that number of shares of Company Common Stock equal to 197.10 divided by the Company's Share Price, rounded to the nearest hundredth. If the Company's Share Price is more than \$52.00 as of the closing date, each share of Avon Water common stock issued and outstanding at the time of the closing of the merger will be exchanged and converted into the right to receive that number of shares of Company Common Stock equal to 227.76 divided by the Company's Share Price, rounded to the nearest hundredth. The "Company's Share Price" is determined by calculating an average of the closing prices for shares of the Company's Common Stock on the Nasdaq Stock Market, LLC for the twenty trading days immediately preceding the third business day prior to the closing of the Merger. Holders of Avon Water common stock prior to the Merger will receive cash in lieu of fractional shares of Company Common Stock.

The Avon Agreement contains customary representations and warranties regarding, on the one hand, Avon Water, its business and operations and related matters, and, on the other hand, the Company, made by the parties as of specified dates, and customary affirmative and negative covenants with respect to the conduct of Avon Water's business prior to the closing. In the Avon Agreement, Avon Water has agreed that its Board of Directors will, subject to certain exceptions, recommend adoption of the Avon Agreement by Avon Water shareholders and the transactions contemplated by the Avon Agreement. Avon Water has also agreed: (i) to cause a special meeting of shareholders of Avon Water to be held to consider the approval and adoption of the

CONNECTICUT WATER SERVICE, INC.

Agreement and the transactions contemplated thereby; and (ii) not to solicit proposals relating to alternative business combination transactions or, subject to certain exceptions, enter into discussions concerning confidential information in connection with alternative business combination transactions.

The obligation of the parties to complete the merger is subject to the satisfaction or waiver on or prior to the closing date of certain specified conditions, including the following: (i) receipt of final and non-appealable orders from each of PURA and the MPUC approving the merger in form and substance reasonably acceptable to the parties; (ii) approval of the merger by the affirmative vote of the holders of not less than two-thirds (66 2/3rd %) Avon Water's issued and outstanding shares of common stock as required under the Connecticut Business Corporation Act; (iii) the receipt of all other necessary consents or approvals to the merger; (iv) approval for listing of the Company Common Stock to be issued in the merger on the Nasdaq Stock Market, LLC; (v) the absence of laws, orders, judgments and injunctions that restrain, enjoin or otherwise prohibit consummation of the Merger; (vi) effectiveness under the Securities Act of the Company's registration statement on Form S-4 relating to the issuance of the Company Common Stock in the merger and absence of any stop order in respect thereof or proceedings by the SEC for that purpose; (vii) the receipt of a legal opinion from counsel to Avon Water regarding certain corporate law matters; (viii) the receipt of a customary tax opinion from counsel to the Company that will state that the merger will qualify as a tax-free reorganization within the meaning of Section 368(a) of the Internal Revenue Code of 1986; (ix) the accuracy of representations and warranties with respect to the businesses of Avon Water and the Company and compliance by Avon Water and the Company with their respective covenants contained in the Avon Agreement; (xi) no event(s) occurring that could reasonably be expected to result in either a "Company Material Adverse Effect" or a "CWS Material Adverse Effect" (each, as defined in the Avon Agreement) and (xii) holders of no more than 5% of Avon Water's common stock have exercised appraisal rights under Connecticut law.

The Avon Agreement contains certain termination rights for both the Company and Avon Water and further provides that, in connection with the termination of the Avon Agreement under specified circumstances, Avon Water may be required to pay to the Company, or the Company may be required to pay to Avon Water, a termination fee of \$200,000 in cash, as liquidated damages.

During the fourth quarter of 2016, Connecticut Water filed an application with PURA seeking approval of the transaction, which the Company expects to receive in April 2017.

Maine Water Land Sale

On March 11, 2016, Maine Water entered into a purchase and sale agreement with the Coastal Mountains Land Trust, a Maine nonprofit corporation (the "Land Trust") pursuant to which Maine Water agreed to sell two conservation easements to the Land Trust on approximately 1,300 acres of land located in the towns of Rockport, Camden and Hope, in Knox County, Maine valued in the aggregate at \$3.1 million. The land had a book value of approximately \$600,000 at December 31, 2015 and is included in "Utility Plant" on the Company's Consolidated Balance Sheets. The easements and purchase prices are as follows:

1. Ragged Mountain Mirror Lake Conservation Easement: \$1,875,000; and
2. Grassy Pond conservation Easement: \$600,000.

The two easement sale and donation transactions are expected to close no later than December 31, 2017 and December 31, 2019, respectively. Maine Water will make a \$200,000 contribution to the Land Trust upon completion of the closing of the first easement sale. Maine Water also expects to claim a charitable deduction for the \$600,000 in excess of the fair market value of the second easement over the \$600,000 sale price.

Connecticut Rates

In Connecticut, the Water Infrastructure Conservation Adjustment ("WICA") was 7.13%, 4.19% and 1.59% above base rates at December 31, 2016, 2015, and 2014, respectively. On January 26, 2017, Connecticut Water filed a WICA application with the PURA requesting a 1.09% surcharge to customers' bills, representing approximately \$8.5 million in WICA related projects. Additionally, on February 9, 2017, Connecticut Water filed its annual WICA reconciliation which requested a 0.06% surcharge, which would replace the 0.03% reconciliation adjustment filed in January 2016. If approved as filed, Connecticut Water's cumulative WICA surcharge, effective April 1, 2017, will be 8.25%.

Since 2013, Connecticut law has authorized a WRA to reconcile actual water demands with the demands projected in the last general rate case and allows companies to adjust rates as necessary to recover the revenues approved by PURA in the last general rate case. The WRA removes the financial disincentive for water utilities to develop and implement effective water conservation programs. The WRA allows water companies to defer on the balance sheet, as a regulatory asset or liability, for later collection from or crediting to customers the amount by which actual revenues deviate from the revenues allowed in the most recent general rate proceedings, including WICA proceedings. Additionally, projects eligible for WICA surcharges were

expanded to include energy conservation projects, improvements required to comply with streamflow regulations, and improvements to acquired systems.

Connecticut Water's allowed revenues for the year ended December 31, 2016, as approved by PURA during our 2010 general rate case and including subsequently approved WICA surcharges, were approximately \$76.7 million. Through normal billing for the year ended December 31, 2016 operating revenue for Connecticut Water would have been approximately \$75.6 million had the WRA not been implemented. As a result of the implementation of the WRA, Connecticut Water recorded \$1.1 million in additional revenue for the year ended December 31, 2016. During the year ended December 31, 2015 and 2014, Connecticut Water recorded \$1.6 million and \$3.7 million, respectively, in additional revenue related to the WRA.

Maine Rates

In Maine, the overall, approved cumulative Water Infrastructure Charge ("WISC") for all divisions was 4.7%, 1.6% and 2.0% above base rates as of December 31, 2016, 2015 and 2014, respectively. Two pending WISC filings as of December 31, 2016 have since been approved in the first quarter of 2017, bringing the total to 6.5%.

In 2014 and 2015, Maine Water petitioned the MPUC for approval of accounting orders that would address (1) the return to its customers a federal income tax refund stemming from the adoption of the Internal Revenue Service ("IRS") Revenue Procedure 2012-19 ("Repair Regulations"), and (2) the treatment of any benefit resulting from the elimination of deferred tax liabilities previously recorded on these qualifying fixed assets that are now deducted under the Repair Regulations.

On February 26, 2015, the MPUC approved a stipulation between Maine Water and the Office of the Public Advocate that refunds \$2.9 million to the customers of the eight divisions over a two-year period starting no later than July 1, 2015, and allows the flow-through treatment of the repair deduction as of January 1, 2014. In addition, Maine Water agreed not to file a general rate case during the two-year refund period in any of the eight divisions that were allowed the refund.

On June 22, 2015, the MPUC approved a settlement agreement between Maine Water and the Office of the Public Advocate that allowed for the amortization of the deferred tax liabilities over a one to nine year period, depending on the division. Maine Water commenced amortization per the agreed upon schedule.

With the completion of these two dockets, Maine Water recorded in the quarter ended June 30, 2015 the retroactive benefit associated with the flow-through of the Repair Regulations from January 1, 2014. The 2014 benefit, reflected in the second quarter of 2015, was approximately \$931,000, or \$0.09 per basic share outstanding.

A newly passed water revenue adjustment mechanism law in Maine became available to regulated water utilities in Maine on October 15, 2015. Maine Water is currently precluded from seeking new rates in certain divisions due to various agreements with the MPUC, but is evaluating how and when this new mechanism can be implemented.

USE OF ESTIMATES – The preparation of financial statements in conformity with GAAP 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 revenue and expenses during the reporting period. Actual results could differ from these estimates.

REVENUES – The Company's accounting policies regarding revenue recognition by segment are as follows:

Water Operations – Most of our water customers are billed quarterly, with the exception of larger commercial and industrial customers, as well as certain public and private fire protection customers who are billed monthly. Most customers, except fire protection customers, are metered. Revenues from metered customers are based on their water usage multiplied by approved, regulated rates and are earned when water is delivered. Public fire protection revenues are based on the length of the water main, and number of hydrants in service and are earned on a monthly basis. Private fire protection charges are based on the diameter of the connection to the water main. Our Regulated Companies accrue an estimate for metered customers for the amount of revenues earned relating to water delivered but unbilled at the end of each quarter, which is reflected as "Accrued Unbilled Revenues" in the accompanying Consolidated Balance Sheets. Beginning in 2013, Connecticut Water began to record deferred revenue to represent under collection from customers based upon allowed revenues as approved by PURA. More detailed information, including revenues, costs and income taxes associated with the segment can be found in Note 14, "Segment Reporting".

Real Estate Transactions – Revenues are recorded when a sale or other transaction has been completed and title to the real estate has been transferred. Net income from the Real Estate Transactions segment is shown net in the "Other Income

(Deductions), Net of Taxes” portion of the Company’s Consolidated Statements of Income. More detailed information, including revenues, costs and income taxes associated with the segment can be found in Note 14, “Segment Reporting”.

Services and Rentals – Revenues are recorded when the Company has delivered the services called for by contractual obligation. Net income from the Services and Rentals segment is shown net in the “Other Income (Deductions), Net of Taxes” portion of the Company’s Consolidated Statements of Income. More detailed information, including revenues, costs and income taxes associated with the segment can be found in Note 14, “Segment Reporting”.

UTILITY PLANT – Utility plant is stated at the original cost of such property when first devoted to public service. Utility plant accounts are charged with the cost of improvements and replacements of property including an Allowance for Funds Used During Construction (“AFUDC”). Retired or disposed depreciable plant is charged to accumulated provision for depreciation together with any costs applicable to retirement, less any salvage received. Maintenance of utility plant is charged to expense. Accounting policies relating to other areas of utility plant are listed below:

Allowance For Funds Used During Construction – AFUDC is the cost of debt and equity funds used to finance the construction of utility plant. The amount shown on the Consolidated Statements of Income relates to the equity portion. The debt portion is included as an offset to “Other Interest Income, Net”. Generally, utility plant under construction is not recognized as part of rate base for ratemaking purposes until facilities are placed into service, and accordingly, AFUDC is charged to the construction cost of utility plant. Capitalized AFUDC, which does not represent current cash income, is recovered through rates over the service lives of the assets.

Our Regulated Companies’ allowed rate of return on rate base is used to calculate AFUDC.

Customers’ Advances For Construction, Contributed Plant and Contributions In Aid Of Construction –Under the terms of construction contracts with real estate developers and others, the Regulated Companies periodically receive either advances for the costs of new main installations or title to the main after it is constructed and financed by the developer. Refunds are made, without interest, as services are connected to the main, over periods not exceeding fifteen years and not in excess of the original advance. Unrefunded balances, at the end of the contract period, are credited to contributions in aid of construction (“CIAC”) and are no longer refundable.

Utility Plant is added in two ways. The majority of the Company’s plant additions occur from direct investment of Company funds that originated through operating or financings activities. The Company manages the construction of these plant additions. These plant additions are part of the Company’s depreciable utility plant and are generally part of rate base. The Company’s rate base is a key component of how its regulated rates are set, and is recovered through the depreciation component of the Company’s rates. The second way in which plant additions occur are through developer advances and contributions. Under this scenario either the developer funds the additions through payments to the Company, who in turn manages the construction of the project, or the developer pays for the plant construction directly and contributes the asset to the Company after it is complete. Plant additions that are financed by a developer, either directly or indirectly, are excluded from the Company’s rate base and not recovered through the rates process, and are also not depreciated.

The components that comprise net additions to Utility Plant during the last three years ending December 31 are as follows:

<i>(in thousands)</i>	2016	2015	2014
Additions to Utility Plant:			
Company Financed	\$ 66,339	\$ 47,774	\$ 44,969
Allowance for Funds Used During Construction	1,198	530	518
Subtotal – Utility Plant Increase to Rate Base	67,537	48,304	45,487
Advances from Others for Construction	350	251	699
Net Additions to Utility Plant	<u>\$ 67,887</u>	<u>\$ 48,555</u>	<u>\$ 46,186</u>

Depreciation – Depreciation is computed on a straight-line basis at various rates as approved by the state regulators on a company by company basis. Depreciation allows the Company to recover the investment in utility plant over its useful life. The overall consolidated company depreciation rate, based on the average balances of depreciable property, was 1.9%, 1.9%, and 1.9% for 2016, 2015, and 2014, respectively.

INCOME TAXES – The Company provides income tax expense for its utility operations in accordance with the regulatory accounting policies of the applicable jurisdictions. The Company’s income tax provision is calculated on a separate return

basis. The Connecticut PURA requires the flow-through method of accounting for most state tax temporary differences as well as for certain federal temporary differences. The MPUC requires the flow-through method of accounting for most state temporary differences and normalized accounting for most federal temporary differences. However, in its approvals of the stipulation agreements between Maine Water and the Office of the Public Advocate, issued in 2015, the MPUC has allowed flow-through method of accounting stemming from Maine Water's adoption of the IRS' Repair Regulations in all of its divisions.

The Company computes deferred tax liabilities for all temporary book-tax differences using the liability method prescribed in FASB ASC 740 "Income Taxes" ("FASB ASC 740"). Under the liability method, deferred income taxes are recognized at currently enacted income tax rates to reflect the tax effect of temporary differences between the financial reporting and tax bases of assets and liabilities. Such temporary differences are the result of provisions in the income tax law that either require or permit certain items to be reported on the income tax return in a different period than they are reported in the financial statements. Deferred tax liabilities that have not been reflected in tax expense due to regulatory treatment are reflected as "Unfunded Future Income Taxes", and are expected to be included in future years' rates.

The Company believes that deferred income tax assets, net of provisions, will be realized in the future. The majority of unfunded future income taxes, prior to 2013, relate to deferred state income taxes regarding book to tax depreciation differences. Beginning in 2013, basis differences resulting from the repair tax deduction contribute to the change in unfunded income taxes.

Deferred Federal and State Income Taxes include amounts that have been provided for accelerated depreciation subsequent to 1981, as required by federal income tax regulations, as well as the basis differences associated with expenditures qualifying for repair tax deduction as clarified by the IRS in regulations issued in 2013. Deferred taxes have also been provided for temporary differences in the recognition of certain expenses for tax and financial statement purposes as allowed by regulatory ratemaking policies.

MUNICIPAL TAXES – Municipal taxes are reflected as "Taxes Other Than Income Taxes" and are generally expensed over the twelve-month period beginning on July 1 following the lien date, corresponding with the period in which the municipal services are provided.

UNAMORTIZED DEBT ISSUANCE EXPENSE – The issuance costs of long-term debt, including the remaining balance of issuance costs on long-term debt issues that have been refinanced prior to maturity, and related call premiums, are amortized over the respective lives of the outstanding debt, as approved by the PURA and the MPUC.

GOODWILL – As part of the purchase of regulated water companies, the Company recorded goodwill of \$30.4 million as of December 31, 2016 representing the amount of the purchase price over net book value of the assets acquired. The Company accounts for goodwill in accordance with Accounting Standards Codification 350 "Intangibles – Goodwill and Other" ("FASB ASC 350"). As a result of the rate order issued by the MPUC, the Company reduced its goodwill balance by \$1.3 million in the year ended December 31, 2015.

As part of FASB ASC 350, the Company is required to perform an annual review of goodwill for any potential impairment, which we perform as of December 31 each year. We update the assessment between the annual testing if events or circumstances occur that would more likely than not reduce the fair value of a reporting unit below its carrying value. As allowed under FASB ASC 350, the Company performed a qualitative analysis of its goodwill for the year ended December 31, 2016. A qualitative analysis includes a review of internal and external factors that could have an impact on a reporting unit's fair value when compared to its carrying amount. These factors included a review of macroeconomic conditions, industry and market considerations, cost factors, overall financial performance, company specific events, changes in reporting units and a review of the Company's stock price.

The last quantitative analysis of impairment was performed as of December 31, 2015, which concluded that the estimated fair value of the Water Operations reporting unit, which has goodwill recorded, exceeded the reporting unit's carrying amount by at least 71% as of December 31, 2015. Additionally, the Company believes that no event has occurred which would trigger impairment since the last quantitative test performed. Based on these factors and other factors considered in its qualitative analysis, the Company believes that it is more likely than not that the fair market value is more than the carrying value of the Water Operation Segment and therefore, no goodwill impairment was recognized in 2016 and 2015.

We may be required to recognize an impairment of goodwill in the future due to market conditions or other factors that are beyond our control and unrelated to our performance. Those market events could include a decline in the forecasted results in our business plan, significant adverse rate case results, changes in capital investment budgets or changes in interest rates that

could permanently impair the fair value of a reporting unit. Recognition of impairments of a significant portion of goodwill would negatively impact our reported results of operation and total capitalization, the effects of which could be material and could make it more difficult to maintain our credit ratings, secure financing on favorable terms, maintain compliance with debt covenants and meet expectations of our regulators.

EARNINGS PER SHARE – The following is a reconciliation of the numerators and denominators of the basic and diluted earnings per share for the years ended December 31:

<i>Years ended December 31,</i>	<u>2016</u>	<u>2015</u>	<u>2014</u>
<i>Numerator (in thousands)</i>			
Basic Net Income Applicable to Common Stock	\$ 23,349	\$ 22,723	\$ 21,281
Diluted Net Income Applicable to Common Stock	\$ 23,349	\$ 22,723	\$ 21,281
<i>Denominator (in thousands)</i>			
Basic Weighted Average Shares Outstanding	11,009	10,958	10,893
Dilutive Effect of Stock Awards	219	206	198
Diluted Weighted Average Shares Outstanding	<u>11,228</u>	<u>11,164</u>	<u>11,091</u>
<i>Earnings per Share</i>			
Basic Earnings per Share	\$ 2.12	\$ 2.07	\$ 1.95
Dilutive Effect of Stock Awards	0.04	0.03	0.03
Diluted Earnings per Share	<u>\$ 2.08</u>	<u>\$ 2.04</u>	<u>\$ 1.92</u>

NEW ACCOUNTING PRONOUNCEMENTS – In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2014-09, “Revenue from Contracts with Customers,” (“ASU No. 2014-09”) which amends its guidance related to revenue recognition. ASU No. 2014-09 requires an entity to recognize revenue as performance obligations are met, in order to reflect the transfer of promised goods or services to customers in an amount that reflects the consideration the entity is entitled to receive for those goods or services. The following steps are applied in the updated guidance: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when, or as, the entity satisfies a performance obligation. ASU No. 2014-09 is effective for public companies for fiscal years, and interim periods within those years, beginning after December 15, 2016, and can be adopted either retrospectively to each prior reporting period presented or as a cumulative-effect adjustment as of the date of adoption, however early adoption is not permitted. On April 1, 2015, the FASB voted for a one-year deferral of the effective date of ASU No. 2014-09, making ASU No. 2014-09 effective for public companies for fiscal years, and interim periods within those years, beginning after December 15, 2017. The Company is currently determining its implementation approach, retrospectively to each prior reporting period presented or retrospectively with a cumulative effect adjustment to retained earnings for initial application, and assessing the impact that this guidance may have on our consolidated financial position, including its impact on the Company’s contracted services provided to water utilities and the impact ASU No. 2014-09 will have on the Company’s accounting surrounding Contributions in Aid of Construction.

In April 2015, the FASB issued ASU No. 2015-03, “Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs” (“ASU No. 2015-03”). The update requires debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the related debt liability instead of being presented as an asset. Debt disclosures will include the face amount of the debt liability and the effective interest rate. ASU No. 2015-03 requires retrospective application and represents a change in accounting principle. The update became effective for the Company on January 1, 2016, which had the effect of reducing the December 31, 2015 “Long-Term Debt” and “Total Regulatory and Other Long-Term Assets” balances by \$5,786,000 on the Consolidated Balance Sheet.

In July 2015, the FASB issued ASU No. 2015-11, “Inventory (Topic 330): Simplifying the Measurement of Inventory” (“ASU No. 2015-11”), which applies to inventory that is measured using first-in, first-out (“FIFO”) or average cost. Under the updated guidance, an entity should measure inventory that is within scope at the lower of cost or net realizable value, which is the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. Subsequent measurement is unchanged under the updated guidance for inventory that is measured using last-in, last-out (“LIFO”). This ASU is effective for annual and interim periods beginning after December 15, 2016, and should be applied prospectively with early adoption permitted at the beginning of an interim or annual reporting period. The Company uses average cost to value its inventory and, therefore, ASU No. 2015-11 will not have an impact on the Company.

In September 2015, the FASB issued ASU No. 2015-16, “Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments” (“ASU No. 2015-16”) which eliminates the requirement for an acquirer in a business combination to account for measurement-period adjustments retrospectively. Acquirers would now recognize measurement-period adjustments during the period in which they determine the amount of the adjustment. ASU No. 2015-16 is effective for the Company on January 1, 2017 and will be adopted on a prospective basis. The adoption is not expected to have a material impact on our consolidated financial position.

In November 2015, the FASB issued ASU No. 2015-17, “Income Taxes (Topic 740), Balance Sheet Classification of Deferred Taxes” (“ASU No. 2015-17”). ASU No. 2015-17 requires net deferred tax assets and liabilities to be classified as non-current on the Company’s Consolidated Balance Sheets. Prior to adoption of the new standard, net deferred tax assets and liabilities were presented separately as current and non-current on the Consolidated Balance Sheets. ASU No. 2015-17 is effective for financial statements issued for annual periods beginning after December 15, 2016 and interim periods within those annual periods. The Company adopted ASU No. 2015-17, effective January 1, 2016, which had the effect of reducing the December 31, 2015 “Prepayments and Other Current Assets” and “Deferred Federal and State Income Taxes” balances by \$17,000 on the Consolidated Balance Sheet.

In February 2016, the FASB issued ASU No. 2016-02, “Leases (Topic 842)”, (“ASU No. 2016-02”), which will require lessees to recognize the following for all leases at the commencement date of a lease: a) a lease liability, which is a lessee’s obligation to make lease payments arising from a lease, measured on a discounted basis; and b) a right-of-use asset, which is an asset that represents the lessee’s right to use, or control the use of, a specified asset for the lease term. Public business entities should apply the amendments in ASU No. 2016-02 for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application is permitted for all public business entities and all nonpublic business entities upon issuance. Lessees (for capital and operating leases) and lessors (for sales-type, direct financing, and operating leases) must apply a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The modified retrospective approach would not require any transition accounting for leases that expired before the earliest comparative period presented. Lessees and lessors may not apply a full retrospective transition approach. The Company is currently assessing the impact of this standard on its consolidated financial position and results of operations, but does not expect that the adoption of this guidance will have material impact.

In March 2016, the FASB issued ASU No. 2016-09, “Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting” (“ASU No. 2016-09”). ASU No. 2016-09 impacts several aspects of the accounting for share-based payment transactions, including classification of certain items on the Consolidated Statement of Cash Flows and accounting for income taxes. Specifically, ASU No. 2016-09 requires that excess tax benefits and tax deficiencies (the difference between the deduction for tax purposes and the compensation cost recognized for financial reporting purposes) be recognized as income tax expense or benefit in the Consolidated Statements of Income, introducing a new element of volatility to the provision for income taxes. ASU No. 2016-09 is effective for fiscal years beginning after December 15, 2016, with early adoption permitted. The Company early adopted ASU No. 2016-09 during the second quarter of 2016, which had the effect of decreasing the “Other” line item on the Consolidated Statements of Income for the year ended December 31, 2016 by approximately \$19,000.

In August 2016, the FASB issued ASU No. 2016-15, “Classification of Certain Cash Receipts and Cash Payments” (“ASU No. 2016-15”). The amendments ASU No. 2016-15 clarify the classification for eight different types of activities, including debt prepayment and extinguishment costs, proceeds from insurance claims and distributions from equity method investees. For public business entities, ASU No. 2016-15 is effective for financial statements issued for fiscal years beginning after December 15, 2017. The Company is currently assessing the impact of this standard on its Consolidated Statements of Cash Flows, but does not expect that the adoption of this guidance will materially impact our consolidated financial position or results of operation.

NOTE 2: INCOME TAX EXPENSE

Under ASC 740, we must recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate resolution. From time to time, the Company is assessed interest and penalties by taxing authorities. In those cases, the charges would appear on the “Other” line item, within the “Other Income (Deductions), Net of Taxes” section of the Consolidated Statements of Income. There were no such charges or accruals for the years ending December 31, 2016, 2015, and 2014.

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On June 11, 2013, the Company was notified by the Connecticut Department of Revenue Services that its state tax filings for the years 2009 through 2011 would be reviewed beginning in the fourth quarter of 2013. On March 24, 2015, the Company was notified by the Connecticut Department of Revenue Services that the audit was expanded to include the 2012 and 2013 tax years. The State focused its review on tax credits associated with fixed capital investment. The Company and the State came to an agreement (“Closing Agreement”) regarding investments eligible for the credit. The Closing Agreement was executed on May 4, 2015. The Company had previously recorded a provision for the possible disallowance of these credits and, therefore, there was minimal impact in 2015.

On the 2012 tax return, filed in September 2013, Connecticut Water filed a change in accounting method to adopt the IRS temporary tangible property regulations. On the 2013 Federal tax return, filed in September 2014, Maine Water filed the same change in accounting method. This method change allowed the Company to take a current year deduction for expenses that were previously capitalized for tax purposes. Since the filing of the 2012 tax return, the IRS has issued final regulations. On February 11, 2014, the Company was notified by the IRS that its Federal tax filing for 2012 would be reviewed. This review, which began in the first quarter of 2014 and was completed in the first quarter of 2015, resulted in no change to the tax liability. Since the Company had previously recorded a provision for the possible disallowance of the repair deduction in prior periods, the completion of the audit resulted in the reversal of the reserves in the amount of \$1,185,000. While the Company maintains the belief that the deduction taken on its tax return is appropriate, the methodology for determining the deduction has not been agreed to by the taxing authorities. Therefore, as required by FASB ASC 740, during the year ended December 31, 2016, the Company recorded a provision of \$3.1 million for a portion of the benefit that is not being returned to customers resulting from any possible tax authority challenge. The Company had previously recorded a provision of \$6.3 million in the prior year for a cumulative total of \$9.4 million.

The Company remains subject to examination by federal tax authorities for the 2013 through 2015 tax years; the State of Maine’s tax authorities for the 2013 through 2015 tax years; and the State of Connecticut’s tax authorities for the 2014 and 2015 tax years.

Income Tax (Benefit) Expense for the years ended December 31, is comprised of the following:

<i>(in thousands)</i>	2016	2015	2014
Federal Classified as Operating (Benefit) Expense	\$ 1,782	\$ (562)	\$ 2,919
Federal Classified as Other Utility Income	385	409	424
Federal Classified as Other Income (Expense)			
Land Sales and Donations	57	(70)	26
Non-Water Sales	702	664	788
Other	(686)	(832)	(825)
Total Federal Income Tax (Benefit) Expense	<u>2,240</u>	<u>(391)</u>	<u>3,332</u>
State Classified as Operating (Benefit) Expense	788	(257)	677
State Classified as Other Utility Income	92	98	100
State Classified as Other Income (Expense)			
Land Sales and Donations	—	(287)	6
Non-Water Sales	172	196	194
Other	(126)	(128)	(82)
Total State Income Tax (Benefit) Expense	<u>926</u>	<u>(378)</u>	<u>895</u>
Total Income Tax (Benefit) Expense	<u>\$ 3,166</u>	<u>\$ (769)</u>	<u>\$ 4,227</u>

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The components of the Federal and State income tax provisions are:

<i>(in thousands)</i>	<u>2016</u>	<u>2015</u>	<u>2014</u>
Current Income Taxes			
Federal	\$ (15)	\$ 315	\$ 427
State	463	201	(306)
Total Current	<u>448</u>	<u>516</u>	<u>121</u>
Deferred Income Taxes, Net			
Federal			
Investment Tax Credit	(75)	(75)	(75)
Excess Deferred Taxes	(110)	192	—
Deferred Revenue	(353)	(754)	215
Land Donations	37	(179)	(56)
Depreciation	1,769	660	1,728
Net Operating Loss Carry-forwards	(1,258)	(1,171)	(600)
AMT Credit Carry-forwards	—	53	—
Provision for uncertain positions	2,487	874	2,177
Other	(242)	(306)	(484)
Total Federal	<u>2,255</u>	<u>(706)</u>	<u>2,905</u>
State			
Land Donations	55	41	—
Provision for uncertain positions	611	41	663
Other	(203)	(661)	538
Total State	<u>463</u>	<u>(579)</u>	<u>1,201</u>
Total Deferred Income Taxes	<u>2,718</u>	<u>(1,285)</u>	<u>4,106</u>
Total Income Tax	<u>\$ 3,166</u>	<u>\$ (769)</u>	<u>\$ 4,227</u>

Deferred income tax (assets) and liabilities are categorized as follows on the Consolidated Balance Sheets:

<i>(in thousands)</i>	<u>2016</u>	<u>2015</u>
Unrecovered Income Taxes - Regulatory Asset	\$ (93,264)	\$ (77,510)
Deferred Federal and State Income Taxes	50,558	48,036
Unfunded Future Income Taxes	90,977	74,712
Unamortized Investment Tax Credits - Regulatory Liability	1,189	1,264
Net Deferred Income Tax Liability	<u>\$ 49,460</u>	<u>\$ 46,502</u>

Net deferred income tax liability increased from December 31, 2015 to December 31, 2016 due to the current year tax effects of temporary differences mostly related to plant items and the recording of provisions for uncertain tax positions.

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Deferred income tax (assets) and liabilities are comprised of the following:

<i>(in thousands)</i>	2016	2015
Tax Credit Carry-forward (1)	\$ (968)	\$ (904)
Charitable Contribution Carry-forwards (2)	(389)	(372)
Valuation Allowance on Charitable Contributions	107	—
Prepaid Income Taxes on CIAC	58	63
Net Operating Loss Carry-forwards (3)	(5,132)	(3,730)
Valuation Allowance on Net Operating Losses	1,471	1,326
Other Comprehensive Income	(589)	(597)
Accelerated Depreciation	51,119	49,341
Provision on Repair Deductions	9,464	6,366
Long-Term Compensation Agreements	(4,416)	(4,004)
Unamortized Investment Tax Credits	1,189	1,264
Other	(2,454)	(2,251)
Net Deferred Income Tax Liability	\$ 49,460	\$ 46,502

- (1) State tax credit carry-forwards expire beginning in 2019 and ending in 2040.
- (2) Charitable Contribution carry-forwards expire with the filing of the 2016 Federal and State Tax Returns in 2017 and ending in 2021.
- (3) Net operating loss carry-forwards expire beginning in 2017 and ending in 2036.

The calculation of Pre-Tax Income is as follows:

<i>(in thousands)</i>	2016	2015	2014
Pre-Tax Income			
Net Income	\$ 23,387	\$ 22,761	\$ 21,319
Income Taxes	3,166	(769)	4,227
Total Pre-Tax Income	\$ 26,553	\$ 21,992	\$ 25,546

In accordance with required regulatory treatment, certain deferred income taxes are not provided for certain timing differences. This treatment, along with other items, causes differences between the statutory income tax rate and the effective income tax rate. The differences between the effective income tax rate recorded by the Company and the statutory federal tax rate are as follows:

	2016	2015	2014
Federal Statutory Tax Rate	34.0 %	34.0 %	34.0 %
Tax Effect Differences:			
State Income Taxes Net of Federal Benefit	2.6 %	— %	1.3 %
Property Related Items	(30.4)%	(19.2)%	(25.0)%
Performance Stock	(0.8)%	0.2 %	1.2 %
Pension Costs	(0.4)%	(1.7)%	2.9 %
Repair Regulatory Liability	(3.9)%	(11.5)%	(6.3)%
Change in Estimate of Prior Year Income Tax Expense	0.3 %	(10.6)%	(1.4)%
Provision for Uncertain Tax Positions	10.2 %	4.1 %	9.2 %
Other	0.3 %	1.2 %	0.7 %
Effective Income Tax Rate	11.9 %	(3.5)%	16.6 %

In the second quarter of 2015, the MPUC approved the flow through treatment of the repair tax deduction. The flow through treatment of the deductions taken on the Company's 2013 tax return is reflected in the change in estimate of prior year income tax expense. In addition, the adoption of the repair tax deduction allowed for a benefit which is reflected in property related

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items. Beginning in the second quarter of 2014, the return to customers of the repair tax benefit is reflected under Repair Regulatory Liability. Provisions for uncertain tax positions were recorded to reflect the possible challenge of the Company's methodology for determining its repair deduction as required by FASB ASC 740.

NOTE 3: COMMON STOCK

The Company has 25,000,000 authorized shares of common stock, no par value. A summary of the changes in the common stock accounts for the period January 1, 2014 through December 31, 2016, appears below:

<i>(in thousands, except share data)</i>	Shares	Issuance Amount	Expense	Total
Balance, January 1, 2014	11,038,232	\$ 142,681	\$ (4,090)	\$ 138,591
Stock and equivalents issued through Performance Stock Program, Net of Forfeitures	35,433	1,396	—	1,396
Dividend Reinvestment Plan	50,965	1,697	—	1,697
Balance, December 31, 2014	11,124,630	145,774	(4,090)	141,684
Stock and equivalents issued through Performance Stock Program, Net of Forfeitures	25,575	1,314	—	1,314
Dividend Reinvestment Plan	42,677	1,536	—	1,536
Balance, December 31, 2015	11,192,882	148,624	(4,090)	144,534
Stock and equivalents issued through Performance Stock Program, Net of Forfeitures	22,128	(405)	—	(405)
Dividend Reinvestment Plan	33,448	1,610	—	1,610
Balance, December 31, 2016 (1)	11,248,458	\$ 149,829	\$ (4,090)	\$ 145,739

(1) Includes 53,821 restricted shares and 217,954 common stock equivalent shares issued through the Performance Stock Programs through December 31, 2016.

The Company may not pay any dividends on its common stock unless full cumulative dividends to the preceding dividend date for all outstanding shares of Preferred Stock of the Company have been paid or set aside for payment. All such Preferred Stock dividends have been paid.

NOTE 4: RETAINED EARNINGS

The summary of the changes in Retained Earnings for the period January 1, 2014 through December 31, 2016, appears below:

<i>(in thousands, except per share data)</i>	2016	2015	2014
Balance, beginning of year	\$ 80,378	\$ 69,370	\$ 59,277
Net Income	23,387	22,761	21,319
Sub-total	103,765	92,131	80,596
Dividends declared:			
Cumulative Preferred Stock, Series A, \$0.80 per share	12	12	12
Cumulative Preferred Stock, Series \$0.90, \$0.90 per share	26	26	26
Common Stock:			
\$1.115, \$1.05 and \$1.01 per Common Share in 2016, 2015 and 2014, respectively	12,514	11,715	11,188
Total Dividends Declared	12,552	11,753	11,226
Balance, end of year	\$ 91,213	\$ 80,378	\$ 69,370

NOTE 5: ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The changes in Accumulated Other Comprehensive Income/(Loss) (“AOCI”) by component, net of tax, for the years ended December 31, 2016, 2015, and 2014, appear below:

<i>(in thousands)</i>	Unrealized Gains on Investments	Defined Benefit Items	Total
Balance as of January 1, 2014 (a)	\$ 259	\$ (374)	\$ (115)
Other Comprehensive Income (Loss) Before Reclassification	2	(1,748)	(1,746)
Amounts Reclassified from AOCI	37	221	258
Net current-period Other Comprehensive Income (Loss)	39	(1,527)	(1,488)
Balance as of December 31, 2014	\$ 298	\$ (1,901)	\$ (1,603)
Other Comprehensive (Loss) Income Before Reclassification	(195)	582	387
Amounts Reclassified from AOCI	97	184	281
Net current-period Other Comprehensive (Loss) Income	(98)	766	668
Balance as of December 31, 2015	\$ 200	\$ (1,135)	\$ (935)
Other Comprehensive Income (Loss) Before Reclassification	24	(227)	(203)
Amounts Reclassified from AOCI	11	203	214
Net current-period Other Comprehensive Income (Loss)	35	(24)	11
Balance as of December 31, 2016	\$ 235	\$ (1,159)	\$ (924)

(a) All amounts shown are net of tax. Amounts in parentheses indicate loss.

The following table sets forth the amounts reclassified from AOCI by component and the affected line item on the Consolidated Statements of Income for the for the years ended December 31, 2016, 2015, and 2014:

Details about Other AOCI Components <i>(in thousands)</i>	Amounts Reclassified from AOCI for the Year Ended December 31, 2016(a)	Amounts Reclassified from AOCI for the Year Ended December 31, 2015(a)	Amounts Reclassified from AOCI for the Year Ended December 31, 2014(a)	Affected Line Items on Income Statement
Realized Gains on Investments	\$ 17	\$ 148	\$ 55	Other
Tax expense	(6)	(51)	(18)	Other
Total Reclassified from AOCI	11	97	37	
Amortization of Recognized Net Gain from Defined Benefit Items	308	281	335	Other (b)
Tax expense	(105)	(97)	(114)	Other
Total Reclassified from AOCI	203	184	221	
Total Reclassifications for the period, net of tax	\$ 214	\$ 281	\$ 258	

(a) Amounts in parentheses indicate loss/expense.

(b) Included in computation of net periodic pension cost (see Note 12 “Long-Term Compensation Arrangements” for additional details).

NOTE 6: FAIR VALUE OF FINANCIAL INSTRUMENTS

FASB ASC 820, “Fair Value Measurements and Disclosures” (“FASB ASC 820”) provides enhanced guidance for using fair value to measure assets and liabilities and expands disclosure with respect to fair value measurements.

FASB ASC 820 establishes a fair value hierarchy that distinguishes between assumptions based on market data (observable inputs) and the Company’s assumptions (unobservable inputs). The hierarchy consists of three broad levels, as follows:

Level 1 – Quoted market prices in active markets for identical assets or liabilities.

Level 2 – Inputs other than Level 1 that are either directly or indirectly observable.

Level 3 – Unobservable inputs developed using the Company’s estimates and assumptions, which reflect those that the Company believes market participants would use.

The following tables summarize our financial instruments measured at fair value on a recurring basis within the fair value hierarchy as of December 31, 2016 and 2015. These instruments are included in “Other Property and Investments” on the Company’s Consolidated Balance Sheets:

December 31, 2016

(in thousands)

	Level 1	Level 2	Level 3	Total
Asset Type:				
Money Market Fund	\$ 122	\$ —	\$ —	\$ 122
Mutual Funds:				
Equity Funds (1)	1,662	—	—	1,662
Fixed Income Funds (2)	534	—	—	534
Total	\$ 2,318	\$ —	\$ —	\$ 2,318

December 31, 2015

(in thousands)

	Level 1	Level 2	Level 3	Total
Asset Type:				
Money Market Fund	\$ 122	\$ —	\$ —	\$ 122
Mutual Funds:				
Equity Funds (1)	1,441	—	—	1,441
Fixed Income Funds (2)	485	—	—	485
Total	\$ 2,048	\$ —	\$ —	\$ 2,048

(1) Mutual funds consisting primarily of equity securities.

(2) Mutual funds consisting primarily of fixed income securities.

The fair value of Company Owned Life Insurance is based on the cash surrender value of the contracts. These contracts are based principally on a referenced pool of investment funds that actively redeem shares and are observable and measurable and are presented on the Other Property and Investments line item of the Company’s Consolidated Balance Sheets.

The following methods and assumptions were used to estimate the fair value of each of the following financial instruments, which are not recorded at fair value on the financial statements.

CASH AND CASH EQUIVALENTS – Cash equivalents consist of highly liquid instruments with original maturities at the time of purchase of three months or less. The carrying amount approximates fair value. Under the fair value hierarchy the fair value of cash and cash equivalents is classified as a Level 1 measurement.

RESTRICTED CASH – As part of Maine Water’s bond offerings in March and November of 2015, the Company recorded unused proceeds from these bond issuances as restricted cash as the funds can only be used for certain capital expenditures. The Company used the remainder of the proceeds during 2016, as the approved capital expenditures were completed. The carrying amount of restricted cash as of December 31, 2015 approximates fair value. Under the fair value hierarchy the fair value of restricted cash is classified as a Level 1 measurement.

COMPANY OWNED LIFE INSURANCE – The fair value of Company Owned Life Insurance is based on the cash surrender value of the contracts. These contracts are based principally on a referenced pool of investment funds that actively redeem shares and are observable and measurable and are presented on the “Other Property and Investments” line item of the Company’s Consolidated Balance Sheets. The value of Company Owned Life Insurance at December 31, 2016 and 2015 was \$3,075,000 and \$2,909,000, respectively.

LONG-TERM DEBT – The fair value of the Company’s fixed rate long-term debt is based upon borrowing rates currently available to the Company and similar marketable securities. As of December 31, 2016 and 2015, the estimated fair value of the Company’s long-term debt was \$210,463,000 and \$191,616,000, respectively, as compared to the carrying amounts of \$202,365,000 and \$177,654,000, respectively. The estimated fair value of long term debt was calculated using a discounted cash flow model that uses comparable interest rates and yield curve data based on the A-rated MMD (Municipal Market Data) Index which is the benchmark of current municipal bond yields. Under the fair value hierarchy, the fair value of long term debt is classified as a Level 2 measurement.

ADVANCES FOR CONSTRUCTION – Customer advances for construction have a carrying amount of \$19,127,000 and \$21,444,000 at December 31, 2016 and 2015, respectively. Their relative fair values cannot be accurately estimated since future refund payments depend on several variables, including new customer connections, customer consumption levels and future rate increases.

The fair values shown above have been reported to meet the disclosure requirements of FASB ASC 825, “Financial Instruments” (“FASB ASC 825”) and do not purport to represent the amounts at which those obligations would be settled.

CONNECTICUT WATER SERVICE, INC.

NOTE 7: LONG-TERM DEBT

Long-Term Debt at December 31, consisted of the following:

<i>(in thousands)</i>		<u>2016</u>	<u>2015</u>
Connecticut Water Service, Inc.:			
4.09%	Term Loan Note and Supplement A, Due 2027	\$ 13,437	\$ 14,472
The Connecticut Water Company:			
Var.	2004 Series Variable Rate, Due 2029	12,500	12,500
Var.	2004 Series A, Due 2028	5,000	5,000
Var.	2004 Series B, Due 2028	4,550	4,550
5.10%	2009 A Series, Due 2039	—	19,930
5.00%	2011 A Series, Due 2021	23,115	23,303
3.16%	CoBank Note Payable, Due 2020	8,000	8,000
3.51%	CoBank Note Payable, Due 2022	14,795	14,795
4.29%	CoBank Note Payable, Due 2028	17,020	17,020
4.72%	CoBank Note Payable, Due 2032	14,795	14,795
4.75%	CoBank Note Payable, Due 2033	14,550	14,550
4.36%	CoBank Note Payable, Due May 2036	30,000	—
4.04%	CoBank Note Payable, Due July 2036	19,930	—
Total The Connecticut Water Company		<u>164,255</u>	<u>134,443</u>
The Maine Water Company:			
8.95%	1994 Series G, Due 2024	7,200	8,100
2.68%	1999 Series J, Due 2019	254	339
0.00%	2001 Series K, Due 2031	615	656
2.58%	2002 Series L, Due 2022	67	75
1.53%	2003 Series M, Due 2023	341	361
1.73%	2004 Series N, Due 2024	371	401
0.00%	2004 Series O, Due 2034	120	127
1.76%	2006 Series P, Due 2026	391	411
1.57%	2009 Series R, Due 2029	217	227
0.00%	2009 Series S, Due 2029	583	628
0.00%	2009 Series T, Due 2029	1,634	1,760
0.00%	2012 Series U, Due 2042	154	160
1.00%	2013 Series V, Due 2033	1,335	1,360
2.52%	CoBank Note Payable, Due 2017	1,965	1,965
4.24%	CoBank Note Payable, Due 2024	4,500	4,500
7.72%	Series L, Due 2018	2,250	2,250
2.40%	Series N, Due 2022	1,101	1,176
1.86%	Series O, Due 2025	790	830
2.23%	Series P, Due 2028	1,294	1,324
0.01%	Series Q, Due 2035	1,771	1,864
1.00%	Series R, Due 2025	2,250	2,488
Various	Various Capital Leases	8	17
Total The Maine Water Company		<u>29,211</u>	<u>31,019</u>
Add: Acquisition Fair Value Adjustment		321	562
Less: Current Portion		(4,859)	(2,842)
Less: Unamortized Debt Issuance Expense		(5,318)	(5,786)
Total Long-Term Debt		<u>\$ 197,047</u>	<u>\$ 171,868</u>

CONNECTICUT WATER SERVICE, INC.

The Company's required principal payments for the years 2017 through 2021 are as follows:

(in thousands)

2017	\$	4,859
2018	\$	5,342
2019	\$	3,194
2020	\$	3,186
2021	\$	3,239

There are no mandatory sinking fund payments required on Connecticut Water's outstanding bonds. However, certain fixed rate Unsecured Water Facilities Revenue Refinancing Bonds provide for an estate redemption right whereby the estate of deceased bondholders or surviving joint owners may submit bonds to the trustee for redemption at par, subject to a \$25,000 per individual holder and a 3% annual aggregate limitation.

On March 17, 2015, Maine Water completed the issuance of \$1,864,050 aggregate principal amount of its First Mortgage Bonds, Series Q, 0.01% due March 17, 2035 (the "Series Q Bonds"). The Series Q Bonds were issued by Maine Water to the Maine Municipal Bond Bank (the "Bank") and the proceeds of the issuance were loaned (the "Series Q Loan") by the Bank to Maine Water pursuant to a Loan Agreement by and between Maine Water and the Bank dated as of March 17, 2015. The proceeds of the Series Q Loan were used by Maine Water to fund various water facilities projects, including the replacement of a booster station and modifications to a treatment plant, each located in the City of Biddeford, Maine.

On November 25, 2015, Maine Water completed the issuance of \$2,487,630 aggregate principal amount of its First Mortgage Bonds, Series R, 1.0% due November 25, 2025 (the "Series R Bonds"). The Series R Bonds were issued by Maine Water to the Bank and the proceeds of the issuance were loaned (the "Series R Loan") by the Bank to Maine Water pursuant to a Loan Agreement by and between Maine Water and the Bank dated as of November 25, 2015. The proceeds of the Series R Loan were used by Maine Water to fund the construction of a 3 million gallon water storage tank, located in the City of Biddeford, Maine, which replaced an existing in-ground 7.5 million gallon reservoir.

In April 2016, Connecticut Water filed an application with PURA to issue promissory notes in the aggregate principal amount of up to \$49,930,000 with CoBank, ACB ("CoBank") under its existing Master Loan Agreement by and between Connecticut Water and CoBank dated October 29, 2012, in order for Connecticut Water to redeem its \$19,930,000 2009A Series of outstanding Water Facility Revenue Bonds previously issued by the Connecticut Development Authority (the "2009A Bonds") and to provide \$30,000,000 to partially fund its ongoing construction program. On June 1, 2016, Connecticut Water issued \$30,000,000, at 4.36%, in debt under its existing Master Loan Agreement with CoBank, with a maturity date of May 20, 2036. On July 7, 2016, Connecticut Water issued \$19,930,000, at 4.04%, in debt under its existing Master Loan Agreement with CoBank, with a maturity date of July 7, 2036. Connecticut Water used the proceeds to immediately pay off the \$19,930,000 2009A Bonds.

On January 10, 2017, Maine Water executed and delivered to CoBank a new Promissory Note and Single Advance Term Loan Supplement, dated January 10, 2017 (the "Third Promissory Note"). On the terms and subject to the conditions set forth in the Third Promissory Note issued pursuant to the Agreement, CoBank agreed to make an unsecured loan (the "Loan") to Maine Water in the principal amount of \$5,000,000 at 4.18%, due December 30, 2026. The proceeds of the Loan will be used to finance new capital expenditures and refinance existing debt owed to the Company, incurred in connection with general water system improvements.

In addition to paying off the 2009A Bonds, Due 2039 using the proceeds of the July CoBank issuance discussed above, during the year ending December 31, 2016, the Company paid approximately \$1,035,000 related to Connecticut Water Service's Term Note Payable issued as part of the 2012 acquisition of Maine Water and approximately \$1,808,000 in sinking funds related to Maine Water's outstanding bonds.

Financial Covenants – The Company is required to comply with certain covenants in connection with various long term loan agreements. The most restrictive of these covenants is to maintain a consolidated debt to capitalization ratio of not more than 60%. Additionally, Maine Water has restrictions on cash dividends paid based on restricted net assets. The Company was in compliance with all covenants at December 31, 2016.

NOTE 8: PREFERRED STOCK

The Company's Preferred Stock at December 31, consisted of the following:

<i>(in thousands, except share data)</i>	<u>2016</u>	<u>2015</u>
Connecticut Water Service, Inc.		
Cumulative Series A Voting, \$20 Par Value; Authorized, Issued and Outstanding 15,000 Shares	\$ 300	\$ 300
Cumulative Series \$0.90 Non-Voting, \$16 Par Value; Authorized 50,000 Shares, Issued and Outstanding 29,499	472	472
Total Preferred Stock	<u>\$ 772</u>	<u>\$ 772</u>

All or any part of any series of either class of the Company's issued Preferred Stock may be called for redemption by the Company at any time. The per share redemption prices of the Series A and Series \$0.90 Preferred Stock, if called by the Company, are \$21.00 and \$16.00, respectively.

The Company is authorized to issue 400,000 shares of an additional class of Preferred Stock, \$25 par value, the general preferences, voting powers, restrictions and qualifications of which are similar to the Company's existing Preferred Stock. No shares of the \$25 par value Preferred Stock have been issued.

The Company is also authorized to issue 1,000,000 shares of \$1 par value Preference Stock, junior to the Company's existing Preferred Stock in rights to dividends and upon liquidation of the Company. 150,000 of such shares have been designated as "Series A Junior Participating Preference Stock".

NOTE 9: BANK LINES OF CREDIT

The Company maintains a \$15 million line of credit agreement with CoBank, ACB, that is currently scheduled to expire on July 1, 2020. The Company maintains an additional line of credit of \$45 million with RBS Citizens, N.A., with an expiration date of April 25, 2021. As of December 31, 2016 the total lines of credit available to the Company were \$60 million. As of December 31, 2016 and 2015, the Company had \$33.0 million and \$16.1 million of "Interim Bank Loans Payable", respectively. As of December 31, 2016, the Company had \$27.0 million in unused lines of credit. Interest expense charged on interim bank loans will fluctuate based on market interest rates.

At December 31, 2016 and 2015, the weighted average interest rates on these short-term borrowings outstanding was 2.7% and 2.4%, respectively.

NOTE 10: UTILITY PLANT

The components of utility plant and equipment at December 31, were as follows:

<i>(in thousands)</i>	<u>2016</u>	<u>2015</u>
Land	\$ 13,724	\$ 13,615
Source of supply	36,405	35,973
Pumping	38,902	37,110
Water treatment	84,594	81,544
Transmission and distribution	530,716	490,489
General	75,438	66,341
Held for future use	432	432
Acquisition Adjustment	(2,351)	(3,057)
Total	<u>\$ 777,860</u>	<u>\$ 722,447</u>

The amounts of depreciable utility plant at December 31, 2016 and 2015 included in total utility plant were \$719,070,000 and \$664,415,000, respectively. Non-depreciable plant is primarily funded through CIAC.

NOTE 11: TAXES OTHER THAN INCOME TAXES

Taxes Other than Income Taxes consist of the following:

<i>(in thousands)</i>	2016	2015	2014
Municipal Property Taxes	\$ 8,501	\$ 7,896	\$ 7,659
Payroll Taxes	1,295	1,398	1,372
Total Taxes Other than Income Taxes	<u>\$ 9,796</u>	<u>\$ 9,294</u>	<u>\$ 9,031</u>

NOTE 12: LONG-TERM COMPENSATION ARRANGEMENTS

The Company has accrued for long-term compensation arrangements as of December 31 as follows:

<i>(in thousands)</i>	2016	2015
Defined Benefit Pension Plan	\$ 16,628	\$ 19,232
Post-Retirement Benefit Other than Pension	5,246	5,041
Supplemental Executive Retirement Plan	8,688	7,915
Deferred Compensation	2,932	2,131
Other Long-Term Compensation	46	70
Total Long-Term Compensation Arrangements	<u>\$ 33,540</u>	<u>\$ 34,389</u>

Investment Strategy – The Corporate Finance and Investment Committee (the “Committee”) reviews and approves the investment strategy of the investments made on behalf of various pension and post-retirement benefit plans provided by the Company and certain of its subsidiaries. The Company uses a variety of mutual funds, managed by different fund managers, to achieve its investment goals. The Committee wants to ensure that the plans establish a target mix that is expected to achieve investment objectives, by assuring a broad diversification of investment assets among investment types, while avoiding short-term changes to the target asset mix, unless unusual market conditions make such a move appropriate to reduce risk.

The targeted asset allocation ratios for those plans as set by the Committee at December 31:

	2016	2015
Equity	65%	65%
Fixed Income	35%	35%
Total	<u>100%</u>	<u>100%</u>

The Committee recognizes that a variation of up to 5% in either direction from its targeted asset allocation mix is acceptable due to market fluctuations.

Our expected long-term rate of return on the various benefit plan assets is based upon the plan’s expected asset allocation, expected returns on various classes of plan assets as well as historical returns. The expected long-term rate of return on the Company’s pension plan assets is 7.25%.

PENSION

Defined Benefit Plan – The Company and certain of its subsidiaries have a noncontributory defined benefit pension plan covering qualified employees. In general, the Company’s policy is to fund accrued pension costs as permitted by federal income tax and The Employee Retirement Income Security Act of 1974 regulations. The Company amortizes actuarial gains and losses over the average remaining service period of active participants. A contribution of \$5,525,000 was made in 2016 for the 2015 plan year. The Company expects to make a contribution of approximately \$2,971,000 in 2017 for the 2016 plan year.

The Company has amended its pension plan to exclude employees hired after January 1, 2009. The Company’s pension plan was amended by the Board of Directors in 2012 primarily to admit current Maine Water and former Aqua Maine employees that were hired before April 1, 2013 to participate under the terms and provisions in effect for Aqua Maine upon the purchase of Maine Water by the Company. The pension plan was also amended in 2014 to reflect the changed definition of spouse under Federal law. Effective January 1, 2015, the Pension Plan was further amended and restated to consolidate prior amendments,

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and to comply with various legislative and regulatory developments. The amended and restated Plan was submitted to the IRS with the Company's application for a Determination Letter on January 29, 2016.

The following tables set forth the benefit obligation and fair value of the assets of the Company's defined benefit plans at December 31, the latest valuation date:

Pension Benefits <i>(in thousands)</i>	2016	2015
Change in benefit obligation:		
Benefit obligation, beginning of year	\$ 75,845	\$ 79,815
Service cost	1,895	2,152
Interest cost	3,212	3,114
Actuarial loss (gain)	2,017	(4,350)
Benefits paid	(3,553)	(4,806)
Administrative expenses	(109)	(80)
Benefit obligation, end of year	<u>\$ 79,307</u>	<u>\$ 75,845</u>
Change in plan assets:		
Fair value, beginning of year	\$ 56,613	\$ 61,635
Actual return on plan assets	4,203	(136)
Employer contributions	5,525	—
Benefits paid	(3,553)	(4,806)
Administrative expenses	(109)	(80)
Fair value, end of year	<u>\$ 62,679</u>	<u>\$ 56,613</u>
Funded Status	<u>\$ (16,628)</u>	<u>\$ (19,232)</u>
Amount Recognized in Consolidated Balance Sheets Consisted of:		
Non-current asset	\$ —	\$ —
Current liability	—	—
Non-current liability	(16,628)	(19,232)
Net amount recognized	<u>\$ (16,628)</u>	<u>\$ (19,232)</u>

The accumulated benefit obligation for all defined benefit pension plans was approximately \$70,748,000 and \$66,818,000 at December 31, 2016 and 2015, respectively.

Weighted-average assumptions used to determine benefit obligations at December 31:	2016	2015
Discount rate	4.10%	4.30%
Rate of compensation increase	4.00%	4.00%

Weighted-average assumptions used to determine net periodic cost for years ended December 31:	2016	2015	2014
Discount rate	4.30%	3.95%	4.90%
Expected long-term return on plan assets	7.25%	7.25%	7.25%
Rate of compensation increase	4.00%	4.00%	4.00%

The Company based its discount rate assumptions the Citigroup Above Median AA Pension Discount Curve.

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The following table shows the components of periodic benefit costs:

Pension Benefits <i>(in thousands)</i>	2016	2015	2014
Components of net periodic benefit costs			
Service cost	\$ 1,895	\$ 2,152	\$ 1,829
Interest cost	3,212	3,114	3,087
Expected return on plan assets	(4,080)	(3,847)	(3,567)
Amortization of:			
Prior service cost	16	16	73
Net loss	2,049	2,979	1,319
Net Periodic Pension Benefit Costs	\$ 3,092	\$ 4,414	\$ 2,741

The following table shows the other changes in plan assets and benefit obligations recognized as a regulatory asset:

Pension Benefits <i>(in thousands)</i>	2016	2015
Change in net (gain) loss	\$ 1,866	\$ (429)
Change in prior service cost	—	—
Other - regulatory action	—	2,050
Amortization of prior service cost	(16)	(16)
Amortization of net loss	(1,998)	(2,904)
Total recognized to Regulatory Asset	\$ (148)	\$ (1,299)

The following table shows the other changes in plan assets and benefit obligations recognized in Other Comprehensive Income ("OCI"):

Pension Benefits <i>(in thousands)</i>	2016	2015
Change in net (gain) loss	\$ 28	\$ 62
Change in prior service cost	—	—
Amortization of prior service cost	—	—
Amortization of net loss	(51)	(75)
Total recognized to OCI	\$ (23)	\$ (13)

Amounts Recognized as a Regulatory Asset at December 31: <i>(in thousands)</i>	2016	2015
Prior service cost	\$ 70	\$ 86
Net loss	12,196	12,328
Total Recognized as a Regulatory Asset	\$ 12,266	\$ 12,414

Amounts Recognized in OCI at December 31: <i>(in thousands)</i>	2016	2015	2014
Transition obligation	\$ —	\$ —	\$ —
Prior service cost	—	—	—
Net loss	315	338	2,401
Total Recognized in Other Comprehensive Income	\$ 315	\$ 338	\$ 2,401

Estimated Net Periodic Benefit Cost Amortizations for the periods January 1 - December 31,: <i>(in thousands)</i>	2017
Amortization of transition obligation	\$ —
Amortization of prior service cost	15
Amortization of net loss	2,030
Total Estimated Net Periodic Benefit Cost Amortizations	\$ 2,045

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Plan Assets

The Company's pension plan weighted-average asset allocations at December 31, 2016 and 2015 by asset category were as follows:

	2016	2015
Equity	65%	64%
Fixed Income	35%	36%
Total	100%	100%

See Note 6, "Fair Value of Financial Instruments", for discussion on how fair value is determined. The fair values of the Company's pension plan assets at December 31, 2016 and 2015 were as follows:

2016
(in thousands)

	Level 1	Level 2	Level 3
Asset Type:			
Money Market Fund	\$ 1,174	\$ —	\$ —
Mutual Funds:			
Fixed Income Funds (1)	21,070	—	—
Equity Funds (2)	40,435	—	—
Total	\$ 62,679	\$ —	\$ —

2015
(in thousands)

	Level 1	Level 2	Level 3
Asset Type:			
Money Market Fund	\$ 805	\$ —	\$ —
Mutual Funds:			
Fixed Income Funds (1)	19,609	—	—
Equity Funds (2)	36,199	—	—
Total	\$ 56,613	\$ —	\$ —

(1) Mutual funds consisting primarily of fixed income securities.

(2) Mutual funds consisting primarily of equity securities.

The plan's expected future benefit payments are:

(in thousands)

2017	\$ 3,928
2018	4,339
2019	4,846
2020	4,746
2021	4,973
Years 2021 – 2025	26,452

POST-RETIREMENT BENEFITS OTHER THAN PENSION ("PBOP") – In addition to providing pension benefits, Connecticut Water and Maine Water, provide certain medical, dental and life insurance benefits to retired employees partially funded by a 501(c)(9) Voluntary Employee Beneficiary Association Trust. Covered employees may become eligible for these benefits if they retire on or after age 55 with 10 years of service. The contribution for calendar years 2016 and 2015 was \$12,000 and \$13,000, respectively.

CONNECTICUT WATER SERVICE, INC.

The Company has amended its PBOP to exclude employees hired after January 1, 2009. In addition, effective April 1, 2009, the Company will no longer provide prescription drug coverage for its retirees age 65 and over. Those retirees, who are entitled to Medicare coverage, will continue to receive the current non-prescription medical coverage.

The Company amortizes actuarial gains and losses over the average remaining service period of active participants. Connecticut Water has elected to recognize the transition obligation on a delayed basis over a period equal to the plan participants' 21.6 years of average future service.

Another subsidiary company, Barnstable Holding, also provides certain health care benefits to eligible retired employees. Employees of Barnstable Holding, became eligible for these benefits if they retired on or after age 65 with at least 15 years of service. Post-65 medical coverage is provided for retired employees up to a maximum coverage of \$500 per quarter. Barnstable Holding's PBOP currently is not funded. Barnstable Holding no longer has any employees; therefore, no new participants will be entering Barnstable Holding's PBOP. The tables below do not include Barnstable Holding's PBOP. Barnstable Holding's PBOP had a Benefit Obligation of \$49,000 and \$52,000 at December 31, 2016 and 2015, respectively. Additionally, this plan did not hold any assets as of December 31, 2016 and 2015. Barnstable Holding's PBOP's net periodic benefit costs were less than \$1,000 in 2016 and 2015.

The following tables set forth the benefit obligation and fair value of the assets of Connecticut Water and Maine Water's PBOP at December 31, the latest valuation date:

PBOP Benefits (in thousands)	<u>2016</u>	<u>2015</u>
Change in benefit obligation:		
Benefit obligation, beginning of year	\$ 13,192	\$ 15,533
Service cost	376	458
Interest cost	541	562
Plan participant contributions	151	156
Actuarial (gain)	(351)	(3,115)
Benefits paid	(367)	(402)
Benefit obligation, end of year	<u>\$ 13,542</u>	<u>\$ 13,192</u>
Change in plan assets:		
Fair value, beginning of year	\$ 8,203	\$ 8,429
Actual return on plan assets	346	7
Employer contributions	12	13
Plan participant contributions	151	156
Benefits paid	(367)	(402)
Fair value, end of year	<u>\$ 8,345</u>	<u>\$ 8,203</u>
Funded Status	<u>\$ (5,197)</u>	<u>\$ (4,989)</u>
Amount Recognized in Consolidated Balance Sheets Consisted of:		
Non-current asset	\$ —	\$ —
Current liability	—	—
Non-current liability	(5,197)	(4,989)
Net amount recognized	<u>\$ (5,197)</u>	<u>\$ (4,989)</u>

Weighted-average assumptions used to determine benefit obligations at December 31:	<u>2016</u>	<u>2015</u>
Discount rate	3.95%	4.15%

Weighted-average assumptions used to determine net periodic cost for years ended December 31:	<u>2016</u>	<u>2015</u>	<u>2014</u>
Discount rate	4.15%	3.80%	4.80%
Expected long-term return on plan assets	4.50%	4.50%	4.50%

The Company based its discount rate assumptions the Citigroup Above Median AA Pension Discount Curve.

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The following table shows the components of periodic benefit costs:

PBOP Benefits (in thousands)	2016	2015	2014
Components of net periodic benefit costs			
Service cost	\$ 376	\$ 458	\$ 494
Interest cost	541	562	625
Expected return on plan assets	(341)	(324)	(305)
Other	225	225	225
Amortization of:			
Prior service credit	(400)	(571)	(806)
Recognized net loss	39	388	344
Net Periodic Post Retirement Benefit Costs	\$ 440	\$ 738	\$ 577

The following table shows the other changes in plan assets and benefit obligations recognized as a regulatory liability:

PBOP Benefits (in thousands)	2016	2015
Change in net gain	\$ (356)	\$ (2,797)
Amortization of prior service cost	400	571
Amortization of net loss	(39)	(388)
Other regulatory amortization	(236)	(236)
Total recognized to Regulatory Liability	\$ (231)	\$ (2,850)

Amounts Recognized as a Regulatory Liability Asset at December 31: (in thousands)	2016	2015
Transition obligation	\$ —	\$ —
Prior service cost	(182)	(583)
Net loss	(531)	(135)
Other regulatory asset	254	494
Total Recognized as a Regulatory Liability	\$ (459)	\$ (224)

The “Other regulatory amortization” and “Other regulatory asset” shown above refers to costs whose recovery was authorized by the PURA and MPUC with the adoption of Statement of Financial Accounting Standard 106, “Employers’ Accounting for Post-Retirement Benefits Other than Pension”, now ASU No. 715. There were no other changes in plan assets and benefit obligations recognized as a regulatory asset.

Estimated Benefit Cost Amortizations for the periods January 1 - December 31: (in thousands)	2017
Amortization of transition obligation	\$ —
Amortization of prior service credit	(181)
Amortization of net loss	(30)
Total Estimated Net Periodic Benefit Cost Amortizations	\$ (211)

Assumed health care cost trend rates at December 31:	2016		2015	
	Medical	Dental	Medical	Dental
Health care cost trend rate assumed for next year ⁽¹⁾	8.25%	8.25%	8.5%	8.5%
Rate to which the cost trend rate is assumed to decline	4.75%	4.75%	5.00%	5.00%
Year that the rate reaches the ultimate trend rate	2024	2024	2023	2023

⁽¹⁾ – Twenty-five basis point declining trend rate from 2015 to 2016.

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Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage-point change in assumed health care cost trend rates would have the following effects on Connecticut Water and Maine Water’s plan and would have no impact on the Barnstable Holding plan:

<i>(in thousands)</i>	1 Percentage-Point	
	Increase	Decrease
Effect on total of service and interest cost components	\$ 49	\$ (45)
Effect on post-retirement benefit obligation	\$ 665	\$ (627)

Plan Assets

Connecticut Water and Maine Water’s other post-retirement benefit plan weighted-average asset allocations at December 31, 2016 and 2015 by asset category were as follows:

	2016	2015
Equity	64%	63%
Fixed Income	36%	37%
Total	100%	100%

See Note 6, “Fair Value of Financial Instruments”, for discussion on how fair value is determined. The fair values of the Company’s PBOP assets at December 31, 2016 and 2015 were as follows:

2016

<i>(in thousands)</i>	Level 1	Level 2	Level 3
Asset Type:			
Money Market	\$ 222	\$ —	\$ —
Mutual Funds:			
Fixed Income Funds (1)	2,770	—	—
Equity Funds (2)	5,353	—	—
Total	\$ 8,345	\$ —	\$ —

2015

<i>(in thousands)</i>	Level 1	Level 2	Level 3
Asset Type:			
Money Market	\$ 239	\$ —	\$ —
Mutual Funds:			
Fixed Income Funds (1)	2,810	—	—
Equity Funds (2)	5,154	—	—
Total	\$ 8,203	\$ —	\$ —

- (1) Mutual funds consisting primarily of fixed income securities.
- (2) Mutual funds consisting primarily of equity securities.

Cash Flows

The Company contributed \$12,000 to its other post-retirement benefit plan in 2016 for plan year 2016. The Company does not expect to make a contribution in 2017 for plan year 2017.

Expected future benefit payments are:

(in thousands)

2017	\$	447
2018		510
2019		572
2020		645
2021		712
Years 2021 – 2025		4,441

SUPPLEMENTAL EXECUTIVE RETIREMENT PLAN (“SERP”) – The Company and certain of its subsidiaries provide additional pension benefits to senior management through supplemental executive retirement contracts. The additional pension supplement from the SERP results in participants receiving the same overall benefit as other eligible employees enrolled in the Company’s pension plan. At December 31, 2016 and 2015, the actuarial present values of the projected benefit obligation of these contracts were \$8,570,000 and \$7,759,000, respectively. Expense associated with these contracts was approximately \$1,012,000 for 2016, \$1,034,000 for 2015, and \$899,000 for 2014 and is reflected in “Other Income (Deductions), Net of Taxes” in the Consolidated Statements of Income.

Included in “Other Property and Investments” at December 31, 2016 and 2015 is \$5,393,000 and \$4,957,000 of investments purchased by the Company to fund these obligations, primarily consisting of life insurance contracts. The remaining assets are carried at fair value and are considered Level 1 within the fair value hierarchy as outlined under FASB ASC 820 and are included in the table shown in Note 6, “Fair Value of Financial Instruments”.

SAVINGS PLAN (“401(k)”) – The Company and certain of its subsidiaries maintain an employee savings plan which allows participants to contribute from 1% to 50% of pre-tax compensation, plus for those aged 50 years and older, catch-up contributions as allowed by law. Effective January 1, 2009, the Company changed its 401(k) plan to meet the requirements of a special IRS safe harbor. Under the provisions of this safe harbor plan, the Company will make an automatic contribution of 3% of compensation for all eligible employees, even if employees do not make their own contributions. For employees hired after January 1, 2009 and ineligible to participate in the Company’s pension plan, the Company will contribute an additional 1.5% of compensation. The savings plan was amended by the Board of Directors effective January 1, 2012 to admit eligible Maine Water employees and effective January 1, 2014 to admit eligible employees who were previously employed by BSWC. The plan was further amended and restated, effective as of January 1, 2016, as required to comply with IRS rules regarding pre-approved volume submitter plans. The Company contribution charged to expense in 2016, 2015, and 2014 was \$663,000, \$601,000, and \$583,000, respectively.

NOTE 13: STOCK BASED COMPENSATION PLANS

The Company follows FASB ASC 718, “Compensation – Stock Compensation” (“FASB ASC 718”) to account for all share-based payments to employees.

For purposes of calculating the fair value of each option at the date of grant, the Company used the Black Scholes Option Pricing model. For other share based awards, the Company uses the market price the day before the stock grant to value awards. The Company has not issued any stock options since 2003, and does not anticipate issuing any for the foreseeable future.

The Company’s 2014 Performance Stock Program (“2014 PSP”), approved by shareholders in 2014, authorizes the issuance of up to 450,000 shares of Company Common Stock. As of December 31, 2016, there were 388,626 shares available for grant and payment of dividend equivalents on shares previously awarded under the 2014 PSP. There are five forms of awards available under the 2014 PSP: Restricted Stock, Performance Shares, Cash Units, Stock Appreciation Rights (“SAR”) and Other Awards.

The Company’s 2004 Performance Stock Program (“2004 PSP”), approved by shareholders in 2004, authorized the issuance of up to 700,000 shares of Company Common Stock. As of December 31, 2016, there were 263,388 shares available for payment of dividend equivalents on shares previously awarded under the 2004 PSP.

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Under the original Plan (“1994 PSP”) there were 700,000 shares authorized for issuance and 218,462 shares available for payment of dividend equivalents on shares previously awarded under the 1994 PSP as performance shares at December 31, 2016.

Under the 2014 PSP, restricted shares of Common Stock, common stock equivalents, cash units, SAR or other awards may be awarded annually to officers and key employees. Based upon the occurrence of certain events, including the achievement of goals established by the Compensation Committee, the restrictions on the stock can be removed. Amounts charged to expense on account of restricted shares of Common Stock, common stock equivalents or cash units pursuant to the 2014 PSP, 2004 PSP and 1994 PSP were \$948,000, \$1,677,000, and \$1,957,000, for 2016, 2015, and 2014, respectively.

RESTRICTED STOCK AND COMMON STOCK EQUIVALENTS – Prior to May 2014, the Company granted restricted shares of Common Stock and Performance Shares to key members of management under the 2004 PSP. All grants made after May 2014 are being made under the 2014 PSP. These Common Stock share awards provide the grantee with the dividend rights of a shareholder, but not the right to sell or otherwise transfer the shares during the restriction period. Restricted shares also have the voting rights of a shareholder, while the Performance Shares do not. The value of these restricted shares is based on the market price of the Company’s Common Stock on the date of grant and compensation expense is recorded on a straight-line basis over the awards’ vesting periods.

Restricted Stock and Common Stock Equivalents (Performance-Based) – The following tables summarize the performance-based restricted stock amounts and activity for the years ended December 31, 2016 and 2015:

	2016		2015	
	Number of Shares	Grant Date Weighted Average Fair Value	Number of Shares	Grant Date Weighted Average Fair Value
Non-vested at beginning of year	39,997	\$ 34.59	40,969	\$ 32.63
Granted	21,110	39.70	26,828	35.81
Vested	(19,077)	34.16	(16,548)	31.71
Forfeited	(6,888)	35.81	(11,252)	34.70
Non-vested at end of year	<u>35,142</u>	<u>\$ 37.66</u>	<u>39,997</u>	<u>\$ 34.59</u>

Upon meeting specific performance targets, approximately 21,000 shares, reduced for actual performance targets achieved in 2016, will begin vesting in the first quarter of 2017 and the remaining earned shares will vest over two years. The cost is being recognized ratably over the vesting period. The aggregate intrinsic value of performance-based restricted stock as of December 31, 2016 was \$1,084,000.

NOTE 14: SEGMENT REPORTING

Our Company operates principally in three segments: water operations, real estate transactions, and services and rentals. The water segment is comprised of our core regulated water operations to supply water to our customers. Our real estate transactions segment involves selling or donating for income tax benefits our limited excess real estate holdings. Our services and rentals segment provides services on a contract basis and also leases certain of our properties to third parties. The accounting policies of each reportable segment are the same as those described in the summary of significant accounting policies.

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Financial data for reportable segments is as follows:

<i>(in thousands)</i>	<u>Revenues</u>	<u>Depreciation</u>	<u>Other Operating Expenses</u>	<u>Other Income (Deductions)</u>	<u>Interest Expense (net of AFUDC)</u>	<u>Income Taxes</u>	<u>Net Income (Loss)</u>
For the year ended December 31, 2016							
Water Operations	\$ 100,001	\$ 13,905	\$ 54,100	\$ (1,822)	\$ 5,718	\$ 2,234	\$ 22,222
Real Estate Transactions	8	—	4	—	—	58	(54)
Services and Rentals	5,307	25	3,189	—	—	874	1,219
Total	<u>\$ 105,316</u>	<u>\$ 13,930</u>	<u>\$ 57,293</u>	<u>\$ (1,822)</u>	<u>\$ 5,718</u>	<u>\$ 3,166</u>	<u>\$ 23,387</u>
For the year ended December 31, 2015							
Water Operations	\$ 97,472	\$ 12,871	\$ 57,474	\$ (1,158)	\$ 6,206	\$ (1,255)	\$ 21,018
Real Estate Transactions	14	—	22	—	—	(357)	349
Services and Rentals	5,602	3	3,362	—	—	843	1,394
Total	<u>\$ 103,088</u>	<u>\$ 12,874</u>	<u>\$ 60,858</u>	<u>\$ (1,158)</u>	<u>\$ 6,206</u>	<u>\$ (769)</u>	<u>\$ 22,761</u>
For the year ended December 31, 2014							
Water Operations	\$ 95,516	\$ 11,784	\$ 53,614	\$ (1,096)	\$ 5,997	\$ 3,227	\$ 19,798
Real Estate Transactions	243	—	161	—	—	32	50
Services and Rentals	5,784	5	3,340	—	—	968	1,471
Total	<u>\$ 101,543</u>	<u>\$ 11,789</u>	<u>\$ 57,115</u>	<u>\$ (1,096)</u>	<u>\$ 5,997</u>	<u>\$ 4,227</u>	<u>\$ 21,319</u>

The Revenues shown in Water Operations above consist of revenues from water customers of \$98,667,000, \$96,041,000 and \$94,020,000 in the years 2016, 2015, and 2014, respectively. Additionally, there were revenues associated with utility plant leased to others of \$1,334,000, \$1,431,000 and \$1,496,000 in the years 2016, 2015, and 2014, respectively which are reflected in “Other Utility Income, Net of Taxes” on the Consolidated Statements of Income. The revenues from water customers for the the years ended December 31, 2016, 2015, and 2014 include \$1,132,000, \$1,583,000 and \$3,700,000 in additional revenues related to the implementation of the WRA, respectively.

The table below shows assets by segment at December 31:

<i>in thousands):</i>	<u>2016</u>	<u>2015</u>
Total Plant and Other Investments:		
Water	\$ 609,508	\$ 553,773
Non-Water	959	637
Total Plant and Other Investments	<u>610,467</u>	<u>554,410</u>
Other Assets:		
Water	171,674	154,090
Non-Water	2,361	2,215
Total Other Assets	<u>174,035</u>	<u>156,305</u>
Total Assets	<u>\$ 784,502</u>	<u>\$ 710,715</u>

NOTE 15: SUBSEQUENT EVENTSHeritage Village Water Company Acquisition

On May 10, 2016, the Company announced that it had reached an agreement to acquire The Heritage Village Water Company ("HVWC"), pending a vote of HVWC shareholders, approval by PURA and MPUC and the satisfaction of other various closing conditions, pursuant to the terms of that certain Agreement and Plan of Merger dated May 10, 2016 between and among HVWC, the Company, and HAC, Inc., the Company's wholly-owned Maine subsidiary (the "Merger Agreement"). HVWC serves approximately 4,700 water customers in the Towns of Southbury, Middlebury, and Oxford, Connecticut and approximately 3,000 wastewater customers in the Town of Southbury, Connecticut.

Under the Merger Agreement, the acquisition was agreed to be executed through a stock-for-stock merger transaction valued at approximately \$16.1 million. Holders of HVWC common stock will receive shares of the Company's common stock in a tax-free exchange. In addition the transaction reflects a total enterprise value of HVWC of approximately \$20.7 million.

The Company received regulatory approval from MPUC on September 28, 2016 and from PURA on December 5, 2016, to proceed with the transaction. The shareholders of HVWC voted to approve the acquisition at a special meeting of HVWC's shareholders held on February 27, 2017.

On February 27, 2017, the Company completed the acquisition of HVWC by completing the merger of Connecticut Water's wholly-owned subsidiary HAC, Inc. with and into HVWC, with HVWC as the surviving corporation, pursuant to the terms of the Merger Agreement and Connecticut corporate law. Upon the effective time of the Merger, the holders of HVWC's 1,620 issued and outstanding shares of common stock became entitled to receive an aggregate of 300,445 shares of the Company's common stock in a tax-free exchange, which exchange was commenced promptly by the issuance of a letter of transmittal and related materials by Connecticut Water's exchange agent.

NOTE 16: COMMITMENTS AND CONTINGENCIES

Water Supply – Connecticut Water has an agreement with the South Central Connecticut Regional Water Authority ("RWA") to purchase water from RWA. The agreement was signed April 2006 and became effective upon the receipt of all regulatory approvals in 2008 and remains in effect for a minimum of fifty years upon the effective date. Connecticut Water will pay RWA \$75,000 per year, for a total of 14 years, starting on the effective date of the agreement. In addition, Connecticut Water is able, but under no obligation, to purchase up to one million gallons of water per day at the then current wholesale rates per the agreement. Connecticut Water has an agreement with The Metropolitan District ("MDC") to purchase water from MDC to serve the Unionville system. The agreement became effective on October 6, 2000 and has a term of fifty years beginning May 19, 2003, the date the water supply facilities related to the agreement were placed in service. Connecticut Water agrees to purchase 283 million gallons of water annually from MDC. Connecticut Water has an agreement with Avon Water ("Avon") to purchase twelve million gallons per year from Avon. The agreement became effective on October 3, 2008 and has a term of 10 years. Connecticut Water has a 99 year lease with 19 Perry Street to obtain well water for its public water supply system. The agreement became effective in 1975 and is based on current water rates in effect each year. There is no limitation on the amount of water that can be withdrawn from the leased property. Maine Water has an agreement with the Kenebec Water District for potable water service. The agreement was extended and became effective on November 7, 2015 for a new term of 5 years. Water sales to Maine Water are billed at a flat rate per gallon plus the monthly minimum tariff rate for a 4-inch metered service. During 2016, 2015, and 2014, the Company spent \$1,556,000, \$1,112,000 and \$3,700,000, respectively, on these agreements. The Company's expected payments related to these agreements for the years 2017 through 2021 will be as follows:

(in thousands)

2017	\$	1,562
2018	\$	1,601
2019	\$	1,643
2020	\$	1,601
2021	\$	1,546

Reviews by Taxing Authorities – On June 11, 2013, the Company was notified by the Connecticut Department of Revenue Services that its state tax filings for the years 2009 through 2011 would be reviewed beginning in the fourth quarter of 2013. On March 24, 2015, the Company was notified by the Connecticut Department of Revenue Services that the audit was

expanded to include the 2012 and 2013 tax years. The State focused its review on tax credits associated with fixed capital investment. The Company and the State came to an agreement (“Closing Agreement”) regarding investments eligible for the credit. The Closing Agreement was executed on May 4, 2015. The Company had previously recorded a provision for the possible disallowance of these credits and, therefore, there was minimal impact in 2015.

On the 2012 tax return, filed in September 2013, Connecticut Water filed a change in accounting method to adopt the IRS’s temporary tangible property regulations. On the 2013 Federal tax return, filed in September 2014, Maine Water filed the same change in accounting method. This method change allowed the Company to take a current year deduction for expenses that were previously capitalized for tax purposes. Since the filing of the 2012 tax return, the IRS has issued final regulations. On February 11, 2014, the Company was notified by the IRS that its Federal tax filing for 2012 would be reviewed. This review, which began in the first quarter of 2014 and was completed in the first quarter of 2015, resulted in no change to the tax liability. Since the Company had previously recorded a provision for the possible disallowance of the repair deduction in prior periods, the completion of the audit resulted in the reversal of the reserves in the amount of \$1,185,000. While the Company maintains the belief that the deduction taken on its tax return is appropriate, the methodology for determining the deduction has not been agreed to by the taxing authorities. Therefore, as required by FASB ASC 740, during the year ended December 31, 2016, the Company recorded a provision of \$3.1 million for a portion of the benefit that is not being returned to customers resulting from any possible tax authority challenge. The Company had previously recorded a provision of \$6.3 million in the prior year for a cumulative total of \$9.4 million.

The Company remains subject to examination by federal tax authorities for the 2013 through 2015 tax years; the State of Maine’s tax authorities for the 2013 through 2015 tax years; and the State of Connecticut’s tax authorities for the 2014 and 2015 tax years.

Environmental and Water Quality Regulation – The Company is subject to environmental and water quality regulations. Costs to comply with environmental and water quality regulations are substantial. We are presently in compliance with current regulations, but the regulations are subject to change at any time. The costs to comply with future changes in state or federal regulations, which could require us to modify current filtration facilities and/or construct new ones, or to replace any reduction of the safe yield from any of our current sources of supply, could be substantial.

Legal Proceedings – We are involved in various legal proceedings from time to time. Although the results of legal proceedings cannot be predicted with certainty, there are no pending legal proceedings to which we, or any of our subsidiaries are a party, or to which any of our properties is subject, that presents a reasonable likelihood of a material adverse impact on the Company’s financial condition, results of operations or cash flows.

Rate Relief – Connecticut Water and Maine Water are regulated public utilities, which provide water services to their customers. The rates that Regulated Companies charge their water customers are subject to the jurisdiction of the regulatory authority of the PURA in Connecticut and the MPUC in Maine. Connecticut Water’s allowed rate of return on equity and return on rate base are currently 9.75% and 7.32%, respectively. Maine Water’s average allowed return on equity and return on rate base, as of December 31, 2016 were 9.50% and 7.96%, respectively.

Land Dispositions – The Company and its subsidiaries own additional parcels of land in Connecticut and Maine, which may be suitable in the future for disposition or for further protection through conservation easements, through sale or by donation to municipalities, other local governments or private charitable entities such as local land trusts. In Connecticut, these additional parcels would include certain Class I and II parcels previously identified for long term conservation by the Connecticut Department of Energy and Environmental Protection (“DEEP”), which have restrictions on development and resale based on provisions of the Connecticut General Statutes. In Maine, these parcels include primarily company-owned land used for water supply protection, and a permanent conservation easement may be appropriate for some parcels to ensure the permanent protection of the watersheds, while balancing the appropriate community and recreational use of the land.

Capital Expenditures – The Company has received approval from its Board of Directors to spend \$55.4 million on capital expenditures in 2017, in part to fund improvements to water treatment plants and increased spending related to infrastructure improvements.

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NOTE 17: QUARTERLY FINANCIAL DATA (Unaudited)

Selected quarterly financial data for the years ended December 31, 2016 and 2015 appears below:

(in thousands, except for per share data)

	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
	2016	2015	2016	2015	2016	2015	2016	2015
Operating Revenues	\$ 21,552	\$ 20,030	\$ 26,055	\$ 26,624	\$ 29,477	\$ 28,444	\$ 21,583	\$ 20,943
Total Utility Operating Income	4,178	4,320	11,217	9,954	10,939	9,709	2,615	3,456
Net Income	3,148	3,103	9,943	8,675	9,535	8,755	761	2,228
Basic Earnings per Common Share	0.29	0.28	0.90	0.79	0.86	0.80	0.07	0.20
Diluted Earnings per Common Share	0.28	0.28	0.89	0.77	0.84	0.79	0.07	0.20

Exhibit Number	Description
2.1	Merger Agreement between and among Connecticut Water Service, Inc., The Avon Water Company, and WC-A I, Inc., dated October 11, 2016 (Exhibit 2.1 to Form 8-K filed on October 12, 2016)
3.1	Amended and Restated Certificate of Incorporation of Connecticut Water Service, Inc. dated May 11, 1998 (Exhibit 3.1 to Form 10-K for year ended December 31, 1998).
3.2	Certificate of Amendment to the Amended and Restated Certificate of Incorporation of Connecticut Water Service, Inc. dated August 27, 1998 (Exhibit 3 to Form 8-K filed September 25, 1998).
3.3	Certificate of Amendment to the Amended and Restated Certificate of Incorporation of Connecticut Water Service, Inc. dated August 6, 2001.
3.4	Certificate of Amendment to the Amended and Restated Certificate of Incorporation of Connecticut Water Service, Inc. dated April 23, 2004. (Exhibit 3.5 to Form 10-Q for the quarter ended March 31, 2003).
3.5	Certification of Incorporation of The Connecticut Water Company effective April, 1998. (Exhibit 3.3 to Form 10-K for the year ended 12/31/98).
3.6	By-Laws, as amended, of Connecticut Water Service, Inc. as amended and restated as of August 16, 2007. (Exhibit 3.1 to Form 8-K filed on August 21, 2007).
4.1	Bond Purchase Agreement dated as of March 12, 2004, among The Connecticut Water Company and A.G. Edwards & Sons, Inc. (Exhibit 4.18 to Form 10-Q for the quarter ended 3/31/04).
4.2	Indenture of Trust, dated as of March 1, 2004, between The Connecticut Water Company and U.S. Bank National Association, as Trustee. (Exhibit 4.19 to Form 10-Q for the quarter ended 3/31/04).
4.3	Reimbursement and Credit Agreement, dated as of March 1, 2004, between The Connecticut Water Company and Citizen's Bank of Rhode Island. (Exhibit 4.20 to Form 10-Q for the quarter ended 3/31/04).
4.4	Letter of Credit issued by Citizen's Bank of Rhode Island, dated as of March 4, 2004. (Exhibit 4.21 to Form 10-Q for the quarter ended 3/31/04).
4.5	Agreement No. DWSRF 200103-C Project Loan Agreement between the State of Connecticut and Unionville Water Company under the Drinking Water State Revolving Fund (DWSRF) Program, dated as of April 19, 2004. (Exhibit 4.22 to Form 10-Q for the quarter ended 6/30/04).
4.6	Collateral Assignment of Water Service Charges and Right to Receive Water Service Expense Assessments and Security Agreement between Unionville Water Company and the State of Connecticut, dated as of June 3, 2004. (Exhibit 4.23 to Form 10-Q for the quarter ended 6/30/04).
4.7	Bond Purchase Agreement, dated September 1, 2004, among The Connecticut Water Company, Connecticut Development Authority, and A.G. Edwards & Sons, Inc. (Exhibit 4.24 to Form 10-Q for the quarter ended 9/30/04).
4.8	Indenture of Trust, dated August 1, 2004, between The Connecticut Water Company and U.S. Bank National Association, as Trustee, 2004A Series. (Exhibit 4.25 to Form 10-Q for the quarter ended 9/30/04).
4.9	Indenture of Trust, dated August 1, 2004, between The Connecticut Water Company and U.S. Bank National Association, as Trustee, 2004B Series. (Exhibit 4.26 to Form 10-Q for the quarter ended 9/30/04).
4.10	Loan Agreement, dated August 1, 2004, between The Connecticut Water Company and Connecticut Development Authority for 2004 Series. (Exhibit 4.27 to Form 10-Q for the quarter ended 9/30/04).
4.11	Loan Agreement, dated August 1, 2004, between The Connecticut Water Company and Connecticut Development Authority for 2004B Series. (Exhibit 4.28 to Form 10-Q for the quarter ended 9/30/04).
4.12	Reimbursement and Credit Agreement, dated as of August 1, 2004, between The Connecticut Water Company and Citizen's Bank of Rhode Island, 2004A Series. (Exhibit 4.29 to Form 10-Q for the quarter ended 9/30/04).
4.13	Reimbursement and Credit Agreement, dated as of August 1, 2004, between The Connecticut Water Company and Citizen's Bank of Rhode Island, 2004B Series. (Exhibit 4.30 to Form 10-Q for the quarter ended 9/30/04).
4.14	Letters of Credit, each dated September 2, 2004, between The Connecticut Water Company and Citizen's Bank of Rhode Island, with respect to each of the 2004A and 2004B Series Bonds. (Exhibit 4.31 to Form 10-Q for the quarter ended 9/30/04).
4.15	First Amendment to Reimbursement and Credit Agreement, dated as of April 28, 2006, between The Connecticut Water Company and Citizen's Bank of Rhode Island, 2004A Series. (Exhibit 10.1 to Form 10-Q for the period ending 3/31/06).
4.16	First Amendment to Reimbursement and Credit Agreement, dated as of April 28, 2006, between The Connecticut Water Company and Citizen's Bank of Rhode Island, 2004B Series. (Exhibit 10.2 to Form 10-Q for the period ending 3/31/06).

- 4.17 First Amendment to Reimbursement and Credit Agreement, dated as of April 28, 2006, between The Connecticut Water Company and Citizen's Bank of Rhode Island, 2004 Series Variable Rate, due 2029. (Exhibit 10.3 to Form 10-Q for the period ending 3/31/06).
- 4.18 Second Amendment to Reimbursement and Credit Agreement, dated as of August 23, 2007 between The Connecticut Water Company and Citizen's Bank of Rhode Island 2004 A Series. (Exhibit 10.2 to the Form 10-Q for the period ending June 30, 2009).
- 4.19 Second Amendment to Reimbursement and Credit Agreement, dated as of August 23, 2007 between The Connecticut Water Company and Citizen's Bank of Rhode Island 2004 B Series. (Exhibit 10.3 to the Form 10-Q for the period ending June 30, 2009).
- 4.20 Second Amendment to Reimbursement and Credit Agreement, dated as of August 23, 2007 between The Connecticut Water Company and Citizen's Bank of Rhode Island 2004 Series Variable Rate, due 2009. (Exhibit 10.4 to the Form 10-Q for the period ending June 30, 2009).
- 4.21 Third Amendment to Reimbursement and Credit Agreement, dated as of August 23, 2007 between The Connecticut Water Company and Citizen's Bank of Rhode Island 2004 A Series. (Exhibit 10.5 to the Form 10-Q for the period ending June 30, 2009).
- 4.22 Third Amendment to Reimbursement and Credit Agreement, dated as of August 23, 2007 between The Connecticut Water Company and Citizen's Bank of Rhode Island 2004 B Series. (Exhibit 10.6 to the Form 10-Q for the period ending June 30, 2009).
- 4.23 Third Amendment to Reimbursement and Credit Agreement, dated as of August 23, 2007 between The Connecticut Water Company and Citizen's Bank of Rhode Island 2004 Series Variable Rate, due 2009. (Exhibit 10.7 to the Form 10-Q for the period ending June 30, 2009).
- 4.24 Bond Purchase Agreement among The Connecticut Water Company, the Connecticut Development Authority and Edward D. Jones & Co., L.P., as underwriter dated December 2, 2009. (Exhibit 4.42 to Form 10-K for the year ended December 31, 2009).
- 4.25 Loan Agreement between The Connecticut Water Company and the Connecticut Development Authority, dated as of December 1, 2009. (Exhibit 4.43 to Form 10-K for the year ended December 31, 2009).
- 4.26 Indenture of Trust for the Bonds between the Connecticut Development Authority and U.S. Bank National Associations, as Trustee, dated December 1, 2009. (Exhibit 4.44 to Form 10-K for the year ended December 31, 2009).
- 4.27 Bond Purchase Agreement among CWC, the Connecticut Development Authority and Janney Montgomery Scott LLC, as underwriter, dated as of December 6, 2011. (Exhibit 4.45 to Form 10-K for the year ended December 31, 2011).
- 4.28 Loan Agreement between CWC and the Authority, dated as of December 1, 2011. (Exhibit 4.46 to Form 10-K for the year ended December 31, 2011).
- 4.29 Indenture of Trust for the Bonds between the Authority and U.S. Bank National Association, as Trustee, dated as of December 1, 2011. (Exhibit 4.47 to Form 10-K for the year ended December 31, 2011).
- 10.1 Directors Deferred Compensation Plan, effective as of January 1, 1980, as amended as of January 1, 2008. (Exhibit 10.7 to Form 8-K filed on January 30, 2008).
- 10.2 Second Amended and Restated Dividend Reinvestment and Common Stock Purchase Plan, as amended and restated as of August 22, 2014. (Exhibit 4 to Form S-3, Registration Statement No. 333-198593, filed on September 5, 2014).
- 10.3 Trust Agreement for The Connecticut Water Company Welfare Benefits Plan (VEBA) dated January 1, 1989. (Exhibit 10.21 to Form 10-K for year ended 12/31/89).
- 10.4 2004 Performance Stock Program, as of April 23, 2004. (Appendix A to Proxy Statement dated 3/12/04).
- 10.5 First Amendment to The Connecticut Water Service, Inc. 2004 Performance Stock Program, dated January 7, 2004. (Exhibit 10.23f to Form 10-K for the year ended 12/31/05).
- 10.6 Second Amendment to The Connecticut Water Service, Inc. 2004 Performance Stock Program, dated January 1, 2008. (Exhibit 10.6 to Form 8-K filed on 1/30/08).
- 10.7 Connecticut Water Service, Inc. 2014 Performance Stock Program (filed as Appendix A to Company's definitive proxy statement (DEF 14A) filed on March 28, 2014).
- 10.8* Form of Restricted Share Award Agreement for non-employee Directors under the Company's 2014 Performance Stock Program.
- 10.9* Form of Performance Unit Award Agreement (short-term vesting form) under the Company's 2014 Performance Stock Program.
- 10.10* Form of Performance Unit Award Agreement (long-term vesting form) under the Company's 2014 Performance Stock Program.

- 10.11 Form of Amended Restated Employment Agreement with the Company's executive officers (Exhibit 10.19 to Form 10-K for year ended December 31, 2008), including:
a) Peter J. Bancroft
b) David C. Benoit
c) Eric W. Thornburg
d) Maureen P. Westbrook
- 10.12 Form of Amended Restated Employment Agreement with the Company's executive officers (Exhibit 10.20 to Form 10-K for year ended December 31, 2008), including:
a) Kristen A. Johnson
b) Nicholas A. Rinaldi
- 10.13 First Amendment to Amended and Restated Employment Agreement between the Company, The Connecticut Water Company and Kristen A. Johnson, dated March 8, 2013 (Exhibit 10.17 to Form 10-K for the year ended December 31, 2012).
- 10.14 First Amendment to Employment Agreement between the Company, the Maine Water Company and Judy E. Wallingford, dated March 8, 2013 (Exhibit 10.18 to Form 10-K for the year ended December 31, 2012).
- 10.15 Form of First Amendment to Amended and Restated Employment Agreement, is filed herewith (Messrs. Thornburg, Benoit and Bancroft, and Ms. Westbrook) (Exhibit 10.1 to Form 8-K filed on 4/3/14).
- 10.16 Form of Second Amendment to Employment Agreement, is filed herewith (Ms. Johnson and Ms. Wallingford) (Exhibit 10.2 to Form 8-K filed on 4/3/14).
- 10.17 Form of Amended and Restated Supplemental Executive Retirement Agreement with the Company's executive officers (Exhibit 10.21 to Form 10-K for year ended December 31, 2008), including:
a) Peter J. Bancroft
b) David C. Benoit
c) Kristen A. Johnson
d) Nicholas A. Rinaldi
e) Eric W. Thornburg
f) Maureen P. Westbrook
- 10.18 Form of Amended and Restated Deferred Compensation Agreement with the Company's executive officers (effective January 1, 2011) (Exhibit 10.20 to Form 10-K for the year ended December 31, 2010), including:
a) Peter J. Bancroft
b) David C. Benoit
c) Kristen A. Johnson
d) Nicholas A. Rinaldi
e) Eric W. Thornburg
f) Maureen P. Westbrook
- 10.19 Deferred Compensation Agreement between The Connecticut Water Company and Eric W. Thornburg, dated December 30, 2011 (Exhibit 10.4 to Form 8-K filed on 1/3/12).
- 10.20 Form of amendment to Deferred Compensation Agreement, dated as of December 30, 2011, with the following Company officers (Exhibit 10.20b to Form 10-K for the year ended December 31, 2011):
a) David C. Benoit
b) Maureen P. Westbrook
c) Kristen A. Johnson
- 10.21 Deferred Compensation agreement between The Connecticut Water Company and Robert J. Doffek, dated December 10, 2015, effective December 31, 2015 (Exhibit 10.1 to Form 10-Q filed on May 9, 2016).
- 10.22 Deferred Compensation Agreement between The Connecticut Water Company and Eric W. Thornburg, dated December 30, 2011. (Exhibit 10.4 to Form 8-K filed on January 3, 2012).
- 10.23 Connecticut Water Company Deferred Compensation Plan, effective January 1, 2017 (Exhibit 10.1 to Form 8-K filed on Dec. 16, 2016).
- 10.24 Form of amendment to Deferred Compensation Agreement, between the Connecticut Water Company and certain executive officers of the Company (Exhibit 10.2 to Form 8-K filed on Dec. 16, 2016).
- 10.25 Deferred Compensation Agreement between Connecticut Water Service, Inc. and Judy E. Wallingford, dated December 11, 2011, effective January 3, 2012. (Exhibit 20.d of the Form 10-K for the year ended December 31, 2011).
- 10.26 Employment agreement among the Company, The Connecticut Water Company and Craig J. Patla, dated April 1, 2014 (Exhibit 10.2 to Form 10-Q filed on 5/8/14).
- 10.27 Deferred compensation agreement among the Company, The Connecticut Water Company and Craig J. Patla, dated April 1, 2014 (Exhibit 10.3 to Form 10-Q filed on 5/8/14).
- 10.28 Master Loan Agreement and Promissory Note between Connecticut Water Service, Inc. and CoBank, ACB, dated June 29, 2009. (Exhibit 10.1 to Form 8-K filed on July 2, 2009)

- 10.29 First Amendment to Promissory Note and Supplement, dated July 26, 2011, between Connecticut Water Service, Inc. and CoBank ACB (Exhibit 10.1 to Form 8-K filed on July, 29 2011).
- 10.30 Amendment to the Master Loan Agreement between Connecticut Water Service, Inc. and CoBank, ACB, dated January 1, 2012 (Exhibit 10.1 to Form 8-K filed on January, 3 2012).
- 10.31 Promissory Note and Single Advance Term Loan Supplement (Loan 1) between Connecticut Water Service, Inc. and CoBank, ACB, dated January 1, 2012 (Exhibit 10.2 to Form 8-K filed on January 3, 2012).
- 10.32 Promissory Note and Single Advance Term Loan Supplement (Loan 2) between Connecticut Water Service, Inc. and CoBank, ACB, dated January 1, 2012 (Exhibit 10.3 to Form 8-K filed on January 3, 2012).
- 10.33 Amended and Restated Promissory Note and Supplement, by and between the Company and CoBank, ACB, dated August 6, 2014 (filed as Exhibit 10.2 to Form 10-Q filed on 8/8/14).
- 10.34 Line of credit agreement dated August 12, 2009 between RBS Citizens, National Association and Connecticut Water Service, Inc. (Exhibit 10.2 to Form 10-Q for the quarter ending September 30, 2009)
- 10.35 Letter Amendment dated May 5, 2010 between RBS Citizens, National Association and Connecticut Water Service, Inc. (Exhibit 10.2 to Form 10-Q filed on 5/7/10).
- 10.36 Second Amendment to RBS Citizens Line of Credit Agreement, dated June 1, 2011. (Exhibit 10.22 of the Form 10-K for the year ended December 31, 2011)
- 10.37 Letter Agreement between Connecticut Water Service, Inc. and RBS Citizens, National Association, dated April 25, 2016 (Exhibit 10.1 to Form 8-K filed on April 28, 2016).
- 10.38 Fourth Allonge to Demand Promissory Note, dated April 25, 2016 (Exhibit 10.2 to Form 8-K filed on April 28, 2016).
- 10.39 Third Amendment to 2009 Promissory Note and Supplement, between Connecticut Water Service, Inc. and CoBank, dated September 4, 2012 (Exhibit 10.1 to current report on Form 8-K filed on Sept. 10, 2012).
- 10.40 First Amendment to 2012 Promissory Note and Supplement, between Connecticut Water Service, Inc. and CoBank, ACB, dated September 4, 2012 (Exhibit 10.2 to current report on Form 8-K filed on Sept. 10, 2012)
- 10.41 Letter Agreement between Connecticut Water Service, Inc. and RBS Citizens, National Association, dated October 12, 2012 (Exhibit 10.1 to current report on Form 8-K dated Oct. 18, 2012).
- 10.42 Third Allonge to Demand Promissory Note, dated October 12, 2012 (Exhibit 10.2 to current report on Form 8-K dated Oct. 18, 2012).
- 10.43 Master Loan Agreement between The Connecticut Water Company and CoBank, ACB, dated October 29, 2012 (Exhibit 10.1 to current report on Form 8-K filed on Nov. 2, 2012).
- 10.44 Promissory Note and Single Advance Term Loan Supplement (Loan 1) between The Connecticut Water Company and CoBank, ACB, dated October 29, 2012 (Exhibit 10.2 to Form 8-K filed on Nov. 2, 2012).
- 10.45 Promissory Note and Single Advance Term Loan Supplement (Loan 2) between The Connecticut Water Company and CoBank, ACB, dated October 29, 2012 (Exhibit 10.3 to Form 8-K filed on Nov. 2, 2012).
- 10.46 Promissory Note and Single Advance Term Loan Supplement (Loan 3) between The Connecticut Water Company and CoBank, ACB, dated October 29, 2012 (Exhibit 10.4 to Form 8-K filed on Nov. 2, 2012).
- 10.47 Promissory Note and Single Advance Term Loan Supplement (Loan 4) between The Connecticut Water Company and CoBank, ACB, dated October 29, 2012 (Exhibit 10.5 to Form 8-K filed on Nov. 2, 2012).
- 10.48 Promissory Note and Single Advance Term Loan Supplement between The Connecticut Water Company and CoBank, ACB, dated June 1, 2016 (Exhibit 10.1 to Form 8-K filed on June 2, 2016).
- 10.49 Second Amendment to Guarantee of Payment (Limited) by Connecticut Water Service, Inc., dated June 1, 2016 (Exhibit 10.2 to Form 8-K filed on June 2, 2016).
- 10.50 Promissory Note and Single Advance Term Loan Supplement between The Connecticut Water Company and CoBank, ACB, dated July 7, 2016 (Exhibit 10.1 to Form 8-K filed on July 13, 2016).
- 10.51 Third Amendment to Guarantee of Payment (Limited) by Connecticut Water Service, Inc., dated July 7, 2016 (Exhibit 10.2 to Form 8-K filed on July 13, 2016).
- 10.52 Guarantee of Payment (Limited) by Connecticut Water Service, Inc., dated October 29, 2012 (Exhibit 10.6 to Form 8-K filed on Nov. 2, 2012).
- 10.53 Amended and Restated Master Loan Agreement between the Maine Water Company and CoBank, ACB, dated December 1, 2012 and entered into on December 7, 2012 (Exhibit 10.1 to Form 8-K filed on Dec. 7, 2012).
- 10.54 Amendment to Amended and Restated Master Loan Agreement by and between the Maine Water Company and CoBank, ACB, dated as of December 22, 2014 (filed as Exhibit 10.2 to Form 8-K filed on 12/30/14).
- 10.52 Promissory Note and Single Advance Term Loan Supplement between the Maine Water Company and CoBank, ACB, dated as of December 22, 2014 (filed as Exhibit 10.3 to Form 8-K filed on 12/30/14).

- 10.56 Promissory Note and Single Advance Term Loan Supplement between the Maine Water Company and CoBank, ACB, dated December 1, 2012 and entered into on December 7, 2012 (Exhibit 10.2 to Form 8-K filed on Dec. 7, 2012).
- 10.57 Promissory Note and Single Advance Term Loan Supplement between the Maine Water Company and CoBank, ACB, dated as of January 10, 2017 (Exhibit 10.3 to Form 8-K filed on Jan. 11, 2017).
- 10.58 Promissory Note and Single Advance Term Loan Supplement between The Connecticut Water Company and CoBank, ACB, dated March 5, 2013 (Exhibit 10.1 to Form 8-K filed on March 6, 2013).
- 10.59 Amendment to Guarantee of Payment (Limited) by Connecticut Water Service, Inc., dated March 5, 2013 (Exhibit 10.2 to Form 8-K filed on March 6, 2013).
- 10.60 Loan Agreement by and between The Maine Water Company and Maine Municipal Bond Bank dated June 3, 2013 (Exhibit 10.1 to the Company's Form 8-K filed on June 4, 2013).
- 10.61 Settlement Agreement between and among The Connecticut Water Company, Office of Consumer Counsel and the Attorney General for the State of Connecticut, dated June 28, 2013 (Exhibit 10.1 to the Company's Form 8-K filed on July 2, 2013).
- 10.62 Loan Agreement by and between The Maine Water Company and Maine Municipal Bond Bank dated March 17, 2015 (Exhibit 10.1 to the Company's Form 8-K filed on March 18, 2015).
- 10.63 Loan Agreement by and between The Maine Water Company and Maine Municipal Bond Bank dated November 25, 2015 (Exhibit 10.1 to the Company's Form 8-K filed on November 30, 2015).
- 10.64 Purchase and Sale Agreement The Maine Water Company and the Coastal Mountains Land Trust, dated March 10, 2016 (Exhibit 10.58 to the Company's 2015 Form 10-K filed on March 14, 2016).
- 10.65 Nonstandardized Adoption Agreement Prototype Cash or Deferred Profit Sharing Plan, effective as of January 1, 2016 (Exhibit 10.59 to the Company's 2015 Form 10-K filed on March 14, 2016).
- 10.66 Base Plan Document for Defined Contribution Plan, effective as of January 1, 2016 (Exhibit 10.60 to the Company's 2015 Form 10-K filed on March 14, 2016).
- 16.1 Letter From ParenteBeard LLC to the Securities and Exchange Commission, dated October 2, 2014 (filed as Exhibit 16.1 to Form 8-K filed on 10/2/14).
- 21* Connecticut Water Service, Inc. Subsidiaries Listing.
- 23.1* Consent of Baker Tilly Virchow Krause, LLP, the Company's current Independent Registered Public Accounting Firm.
- 24.1* Power of Attorney of the directors of Connecticut Water Service, Inc.
- 31.1* Rule 13a-14 Certification of Eric W. Thornburg, Chief Executive Officer.
- 31.2* Rule 13a-14 Certification of David C. Benoit, Chief Financial Officer.
- 32.1** Certification of Eric W. Thornburg, Chief Executive Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2** Certification of David C. Benoit, Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS** XBRL Instance Document
- 101.SCH** XBRL Taxonomy Extension Schema
- 101.CAL** XBRL Taxonomy Extension Calculation Linkbase
- 101.DEF** XBRL Taxonomy Extension Definition Linkbase
- 101.LAB** XBRL Taxonomy Extension Label Linkbase
- 101.PRE** XBRL Taxonomy Extension Presentation Linkbase
- Note: Exhibits 10.1 through 10.27, 10.65 and 10.66 set forth each management contract or compensatory plan or arrangement required to be filed as an exhibit to this Form 10-K.

* = filed herewith

** = furnished herewith

ITEM 16. FORM 10-K SUMMARY

None

SIGNATURES

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

CONNECTICUT WATER SERVICE, INC.
Registrant

March 13, 2017

By /s/ Eric W. Thornburg
Eric W. Thornburg
Chairman, President and Chief Executive Officer

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

Signature	Title	Date
<u>/s/ Eric W. Thornburg</u> Eric W. Thornburg	Chairman, President, and Chief Executive Officer (Principal Executive Officer)	March 13, 2017
<u>/s/ David C. Benoit</u> David C. Benoit	Senior Vice President – Finance, Chief Financial Officer and Treasurer (Principal Financial Officer)	March 13, 2017
<u>/s/ Robert J. Doffek</u> Robert J. Doffek	Controller (Principal Accounting Officer)	March 13, 2017

Signature	Title	Date
<u>/s/ Richard H. Forde</u> Richard H. Forde	Director	March 10, 2017
<u>/s/ Mary Ann Hanley</u> Mary Ann Hanley	Director	March 10, 2017
<u>/s/ Heather Hunt</u> Heather Hunt	Director	March 10, 2017
<u>/s/ Bradford A. Hunter</u> Bradford A. Hunter	Director	March 10, 2017
<u>/s/ Lisa J. Thibdaue</u> Lisa J. Thibdaue	Director	March 10, 2017
<u>/s/ Carol P. Wallace</u> Carol P. Wallace	Director	March 10, 2017
<u>/s/ Ellen C. Wolf</u> Ellen C. Wolf	Director	March 10, 2017

CONNECTICUT WATER SERVICE, INC. and SUBSIDIARIES
SCHEDULE II – VALUATION AND QUALIFYING ACCOUNTS

(in thousands)

Description	Balance Beginning of Year	Additions Charged to Income	Deductions from Reserves⁽¹⁾	Balance End of Year
Allowance for Uncollectible Accounts				
Year Ended December 31, 2016	\$ 947	\$ 558	\$ 405	\$ 1,100
Year Ended December 31, 2015	\$ 1,202	\$ 158	\$ 413	\$ 947
Year Ended December 31, 2014	\$ 1,127	\$ 549	\$ 474	\$ 1,202

⁽¹⁾ Amounts charged off as uncollectible after deducting recoveries.

Shareholder/Investor Information

Shareholder & Investor Contact

Laurie I. Felleman
Assistant Corporate Secretary
Connecticut Water Service, Inc.
93 West Main Street
Clinton, Connecticut 06413
Tel.: 860-664-6015
Fax: 860-669-5579
Website: www.ctwater.com
E-mail: lfelleman@ctwater.com

Annual Meeting

Thursday, May 11, 2017
Madison Beach Hotel
94 West Wharf Road
Madison, Connecticut 06443

Independent Public Accountants

Baker Tilly Virchow Krause, LLP
Philadelphia, Pennsylvania 19103

Transfer Agent and Internet Access for Registered Shareholder Accounts

Broadridge Corporate Issuer Solutions (Broadridge)
P.O. Box 1342
Brentwood, New York 11717
Toll-Free: 888-205-0681
International: 720-358-3608
Fax: 215-553-5402
Website: <http://shareholder.broadridge.com/ctwater>
E-mail: shareholder@broadridge.com

Number of Registered Shareholders

Accounts as of March 1, 2017: 3,100

Legal Counsel

Murtha Cullina LLP
Hartford, Connecticut 06103

Stock Trading, Dividends, Preferred Stock

- Common Stock of Connecticut Water Service, Inc. is traded on NASDAQ; symbol CTWS.
- Projected dividend dates are 6/15/17, 9/15/17, 12/15/17 and 3/15/18.
- Cumulative Preferred A; symbol CTWSO. The current quarterly dividend is \$0.20 per share.
- Preferred 90; symbol CTWSP. The current quarterly dividend is \$0.225 per share.

Dividend Tax Status

- The Company estimates that all common stock dividends paid in 2016 are taxable as dividend income. Registered shareholders received the appropriate tax forms from Broadridge in January for dividends received in the previous year.

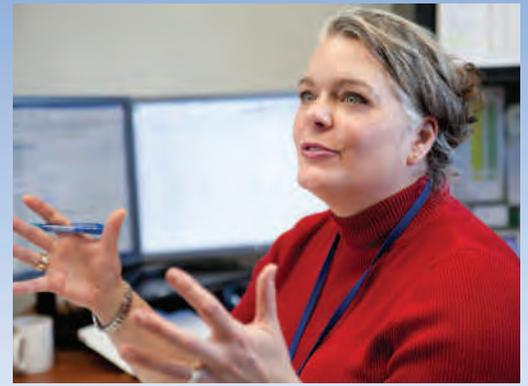
Features of the CTWS Dividend Reinvestment and Common Stock Purchase Plan

- \$25 minimum/\$3,333 maximum optional monthly reinvestment.
- Optional cash purchases automatically withdrawn from a bank account.
- Optional cash purchases are made on the 15th of every month. (Checks for reinvestment should be payable to Broadridge and received by Broadridge five business days before the 15th.) Plan Prospectus available at www.ctwater.com.
- Flat fee to sell shares (no per share fee).
- Purchase additional shares with no commissions or fees.

Connecticut Water and Subsidiaries at a Glance (as of March 1, 2017)

Connecticut Water Service, Inc. has four principal subsidiaries.

Madalyne
Human Resources



Lauren
Payroll Administrator

The Connecticut Water Company,

which is regulated by the Connecticut Public Utilities Regulatory Authority (PURA), supplies water to 93,000 customers, or approximately 325,000 people, for residential, commercial, industrial and municipal purposes in 56 Connecticut communities.

Sources: 18 surface supplies and more than 200 wells

Service Area: Connecticut Water's service area is predominantly suburban and rural. Approximately 90% of its customers are classified as residential, and about 7% are classified as commercial or industrial.

The Maine Water Company,

which is regulated by the Maine Public Utilities Commission (MPUC), supplies water to more than 32,000 customers, or nearly 80,000 people, for residential, commercial, industrial and municipal purposes in 21 Maine communities.

Sources: seven surface supplies and 14 wells

Service Area: Maine Water's service area is a mix of urban, suburban and rural. Approximately 88% of customers are classified as residential, and about 10% are classified as commercial or industrial.

The Heritage Village Water Company,

which is regulated by PURA, supplies water to 4,700 water customers and 3,000 wastewater customers, or more than 16,000 people, for residential, commercial, industrial and municipal purposes in three Connecticut communities.

Sources: five wells

Service Area: Heritage Village Water's service area is predominantly suburban and rural. Approximately 90% of its customers are classified as residential, and about 7% are classified as commercial or industrial.

New England Water Utility Services, Inc. (NEWUS)

provides a wide variety of water- and wastewater-related services to residential, commercial, industrial and municipal clients throughout Connecticut. NEWUS is not regulated by the public utilities agencies in any of the New England states.

Services provided by NEWUS include:

- Contract operation of water systems for other utilities, businesses, municipalities and the University of Connecticut's Storrs campus.
- The Linebacker® program in Connecticut and Maine.



CONNECTICUT WATER SERVICE, INC.

WWW.CTWATER.COM

NASDAQ:CTWS