

Charter of the Audit Committee of the Board of Directors

Southwest Water Company

I. Purpose

The purpose of the Audit Committee (the “Committee”) is to oversee the accounting and financial reporting processes of Southwest Water Company (the “Company”) and the audits of the financial statements of the Company.

The Committee has the responsibilities, duties, and powers set forth in this Charter. The Committee shall be given full and direct access to the Company’s internal audit function, the Chair of the Board of Directors, Company executives and independent accountants as necessary to carry out these responsibilities. However, the Committee’s function is one of oversight only and shall not relieve the Company’s management of its responsibilities for preparing financial statements that accurately and fairly present the Company’s financial results and condition, or the responsibilities of the independent accountants relating the audit or review of financial statements.

II. Composition of the Audit Committee

The Committee shall comprise no fewer than three (3) directors, each of whom will be independent as required by Section 10A(3)(b)(i) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”) and the rules of the National Association of Securities Dealers, Inc. (“NASD”) provided, that if a member of the Committee ceases to be independent for reasons outside the member’s reasonable control, then the member may remain on the Committee until the earlier of the Company’s next annual stockholders meeting or one year from the occurrence of the event that caused the member to cease to be independent. Each appointed Committee member shall be subject to annual reconfirmation and may be removed by the Board at any time.

Each Committee member must be able to read and understand fundamental financial statements, including a company’s balance sheet, income statement and cash flow statement. At least one member of the Committee shall have past employment experience in finance or accounting, requisite professional certification in accounting, or any other comparable experience or background which results in the individual’s financial sophistication, including being or having been a chief executive officer, chief financial officer or other senior officer with financial oversight responsibilities.

III. Responsibilities and Duties

The Committee shall have the following responsibilities, duties and powers in carrying out its oversight functions (in addition to any others that the Board may from time to time delegate to the Committee):

1. Review and evaluate the performance of the independent accountants who are accountable to the Committee. Appoint, and, where appropriate, terminate and replace the independent accountants to audit the Company's financial statements.
2. Consider the Company's process for reviewing internal controls and financial reporting and disclosure.
3. The Committee shall discuss with management and the independent accountants, a) the adequacy of the Company's internal accounting controls and the financial reporting process; b) the status of internal control recommendations made by the independent accountants; and c) significant financial risk exposures and the steps management has taken to monitor, control and report such exposures.
4. Approve the engagement of the independent accountants to perform all services, considering both the types of services and the projected fees.
5. Review the Company's hiring policies for retaining employees or former employees of the independent accountants.
6. Review the significant accounting principles, policies and practices followed by the Company in accounting for and reporting its financial results of operations in accordance with generally accepted accounting principles ("GAAP").
7. Review the Company's annual audited financial statements and related disclosures, including the MD&A portion of the Company's filings, and discuss with the independent accountants the matters required to be discussed by Auditing Standard No. 61, including: (a) the quality as well as acceptability of the accounting principles applied in the financial statements, and (b) new or changed accounting policies.
8. Review any management letters or internal control reports prepared by the independent accountants or the Company's internal auditors and responses to prior management letters, and review with the independent accountants the Company's internal

financial controls, including the budget, staffing and responsibilities of the Company's internal audit function.

9. Review the effectiveness of the independent audit effort, including approval of the scope of, and fees charged in connection with, the annual audit, quarterly reviews and any non-audit services being provided.
10. Be directly responsible for the appointment, compensation, retention and oversight of the work of the independent accountants (including resolution of disagreements between the independent accountants and Company management regarding financial reporting) for the purpose of preparing or issuing an audit report or related work or performing other audit, review or attest services for the Company.
11. Obtain on an annual basis a formal written statement from the independent accountants delineating all relationships between the accountants and the Company consistent with Independence Standards Board Standard No. 1, and actively engage in a dialogue with the accountants with respect to any disclosed relationships or services that may impact the objectivity and independence of the accountants. Take, or recommend that the full Board take, appropriate action to oversee the independence of the independent accountants.
12. For each of the first three fiscal quarters and at year end, at a Committee meeting, review with management the financial results, the proposed earnings press release and formal guidance which the Company may plan to offer, and review with the independent accountants the results of their review of the interim financial information and audit of the annual financial statements.
13. Review management's analysis of any significant accounting issues, changes, estimates, judgments or unusual items relating to the financial statements and the selection, application and effects of critical accounting policies applied by the Company (including an analysis of the effect of alternative GAAP methods) and review with the independent accountants the reports on such subjects delivered pursuant to Section 10A(k) of the Exchange Act.
14. Following completion of the annual audit, review separately with the independent accountants and management any significant issues encountered during the course of the audit. Discuss with independent accountants the communications regarding the

conduct of the audit required of the independent accountants under applicable auditing standards.

15. Report to the Board on a regular basis on events covered by the Committee and make recommendations to the Board and management concerning these matters.
16. Review the accounting and disclosure of significant matters that may have a material impact on the financial statements.
17. Approve the report required by the SEC to be included in the Company's annual proxy statement.
18. Approve all transactions between the Company and a Related Party, as defined by applicable NASD Rules.
19. Review major changes to the Company's auditing and accounting principles and practices as suggested by the independent accountants, internal auditors or management.
20. On at least an annual basis, the Committee shall discuss with the independent accountants the results of their discussion with the Company's counsel concerning legal matters that could have a significant impact on the organization's financial statements, the Company's compliance with applicable laws and regulations, and inquiries received from regulators or governmental agencies.
21. Review and assess the adequacy of the Committee Charter annually and recommend any proposed changes to the Board for approval.
22. Perform any other activities consistent with this charter, the Company's Bylaws and governing law as the Committee or the Board deems necessary or appropriate.
23. Establish procedures for: (a) the receipt, retention, and treatment of complaints received by the Company regarding accounting, internal accounting controls, or auditing matters and (b) the confidential, anonymous submission by employees of the Company regarding concerns related to questionable accounting, reporting or auditing matters.
24. Engage independent counsel and other advisers, as the Committee determines necessary to carry out its duties. The Company shall provide for appropriate funding, as determined by the Committee, for payment of compensation to the independent

accountants for the purpose of preparing or issuing an audit report or performing other audit, review or attest services, for payment of compensation to any advisers employed by the Committee and for ordinary administrative expenses of the Committee that are necessary or appropriate in carrying out its duties.

IV. Audit Committee Meetings

The Committee will meet on a regular basis at least four (4) times each year, and will hold special meetings as circumstances require. The Committee shall determine the timing of the meetings. However, the Committee will meet at any time that the independent accountants believe communication to the Committee is required. At each regular meeting the Committee shall meet privately in executive session. At each regular meeting the Committee will meet separately with representatives of the independent accountants and management. The Committee may ask members of management or others to attend meetings and provide pertinent information as necessary.

At all Committee meetings a majority of the total members shall constitute a quorum. A majority of the members of the Committee shall be empowered to act on behalf of the Committee. Minutes shall be kept of each meeting of the Committee and periodically report to the Board significant results of the foregoing activities.