



**NATURAL ENERGY UTILITY CORPORATION**

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**INDEPENDENT AUDITOR'S REPORT  
AND  
FINANCIAL STATEMENTS**

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**DECEMBER 31, 2011 AND 2010**

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### INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of  
Natural Energy Utility Corporation  
Ashland, Kentucky

We have audited the accompanying balance sheets of Natural Energy Utility Corporation, a Kentucky corporation, as of December 31, 2011 and 2010, and the related statements of income, stockholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Natural Energy Utility Corporation as of December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

*Smith, Goolsby, Artis & Reams, P.S.C.*

Ashland, Kentucky  
February 13, 2012

**NATURAL ENERGY UTILITY CORPORATION  
BALANCE SHEETS  
DECEMBER 31, 2011 AND 2010**

<b>ASSETS</b>	<b><u>2011</u></b>	<b><u>2010</u></b>
<b>CURRENT ASSETS</b>		
Cash in bank-checking	\$ 61,955	\$ 112,813
Trading Securities	-	9,927
Accounts receivable, net of allowance for doubtful accounts of \$1,600.	283,050	375,607
Prepaid expenses	61,485	44,525
Inventory	<u>5,000</u>	<u>5,000</u>
<b>TOTAL CURRENT ASSETS</b>	<b>411,490</b>	<b>547,872</b>
 <b>PROPERTY AND EQUIPMENT, NET</b>	 659,731	 866,773
 <b>OTHER ASSETS</b>		
Advances to shareholders	<u>379,365</u>	<u>37,000</u>
<b>TOTAL OTHER ASSETS</b>	<u>379,365</u>	<u>37,000</u>
 <b>TOTAL ASSETS</b>	 <u>\$ 1,450,586</u>	 <u>\$ 1,451,645</u>
 <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES</b>		
Line of credit	\$ 500,000	\$ -
Current portion of long-term debt	-	297,337
Accounts payable	119,253	97,461
Accrued liabilities	95,743	113,426
Customer deposits	13,412	13,672
Gas imbalance payable	<u>965</u>	<u>23,577</u>
<b>TOTAL CURRENT LIABILITIES</b>	<b>729,373</b>	<b>545,473</b>
 <b>LONG-TERM DEBT</b>		
Long-term debt, net of current portion	<u>-</u>	<u>422,592</u>
<b>TOTAL LIABILITIES</b>	<u>729,373</u>	<u>968,065</u>
 <b>STOCKHOLDERS' EQUITY</b>		
Common stock, \$1 par; 1,000 shares authorized, issued and outstanding	1,000	1,000
Additional paid-in capital	320,000	320,000
Retained earnings	<u>400,213</u>	<u>162,580</u>
<b>TOTAL STOCKHOLDERS' EQUITY</b>	<u>721,213</u>	<u>483,580</u>
 <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	 <u>\$ 1,450,586</u>	 <u>\$ 1,451,645</u>

See accompanying notes.

**NATURAL ENERGY UTILITY CORPORATION  
STATEMENTS OF INCOME  
YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
<b>REVENUES</b>		
Gas sales and transportation income	\$ 2,879,649	\$ 2,781,492
Other income	<u>16,048</u>	<u>14,099</u>
<b>TOTAL REVENUES</b>	<u>2,895,697</u>	<u>2,795,591</u>
 <b>COST OF SALES</b>		
Gas purchases	178,528	289,484
Transportation costs	<u>18,151</u>	<u>14,510</u>
<b>TOTAL COST OF SALES</b>	<u>196,679</u>	<u>303,994</u>
<b>GROSS PROFIT</b>	<u>2,699,018</u>	<u>2,491,597</u>
 <b>OPERATING EXPENSES</b>		
Salaries and wages	1,695,318	1,555,770
Employee retirement plan contributions	20,859	9,109
Depreciation	217,763	261,065
Operations expense	91,019	93,376
Professional fees	43,429	54,861
Taxes and licenses	89,786	88,168
Employee insurance	70,850	59,228
Travel expenses	33,024	22,354
Payroll tax expense	53,610	49,980
Other insurance	44,884	42,175
Rent and lease expense	10,985	10,723
Telephone and communications	23,304	21,529
Repairs and maintenance	21,834	17,219
Bad debt provision	1,817	585
Office supplies and expense	5,800	5,192
Postage and shipping	8,507	6,257
Miscellaneous expenses	8,189	6,450
Utilities	6,424	5,707
Advertising	<u>1,414</u>	<u>2,056</u>
<b>TOTAL OPERATING EXPENSES</b>	<u>2,448,816</u>	<u>2,311,804</u>
<b>NET OPERATING INCOME</b>	<u>250,202</u>	<u>179,793</u>
 <b>OTHER INCOME (EXPENSE)</b>		
Other income	262	1,610
Interest expense, net of interest income of \$655 and \$3,831 respectively	<u>(12,831)</u>	<u>(28,635)</u>
<b>TOTAL OTHER INCOME (EXPENSE)</b>	<u>(12,569)</u>	<u>(27,025)</u>
<b>NET INCOME</b>	<u>\$ 237,633</u>	<u>\$ 152,768</u>

See accompanying notes.

**NATURAL ENERGY UTILITY CORPORATION  
 STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY  
 YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>COMMON STOCK</u>	<u>ADDITIONAL PAID IN CAPITAL</u>	<u>RETAINED EARNINGS</u>	<u>TOTAL</u>
<b>BALANCE, JANUARY 1, 2010</b>	\$ 1,000	\$ 320,000	\$ 174,146	\$ 495,146
Net income	-	-	152,768	152,768
Distributions to stockholders	-	-	(164,334)	(164,334)
<b>BALANCE, DECEMBER 31, 2010</b>	1,000	320,000	162,580	483,580
Net income	-	-	237,633	237,633
<b>BALANCE, DECEMBER 31, 2011</b>	<u>\$ 1,000</u>	<u>\$ 320,000</u>	<u>\$ 400,213</u>	<u>\$ 721,213</u>

See accompanying notes.

**NATURAL ENERGY UTILITY CORPORATION  
STATEMENTS OF CASH FLOWS  
YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 237,633	\$ 152,768
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	217,763	261,065
Provision for bad debts	1,817	585
Unrealized gain on trading securities	-	(1,610)
Realized gain on trading securities	(262)	-
Proceeds from sales of trading securities	10,188	-
Net changes in operating assets and liabilities:		
(Increase) decrease in:		
Accounts receivable	90,740	(69,237)
Prepaid expenses	(16,960)	2,074
(Decrease) increase in:		
Accounts payable	21,792	28,128
Accrued liabilities	(17,683)	(2,245)
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<u>545,028</u>	<u>371,528</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchases of premises and equipment	(10,720)	(5,607)
Decrease (increase) in advances to shareholders	(342,365)	126,844
<b>NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES</b>	<u>(353,085)</u>	<u>121,237</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from long-term debt	642,636	-
Payments and reclassifications on long-term debt	(1,362,565)	(605,436)
Proceeds from line of credit	500,000	-
Distributions to shareholders	-	(164,334)
Gas imbalance repayments	(22,612)	14,942
Decrease in customer deposits	(260)	(380)
<b>NET CASH USED BY FINANCING ACTIVITIES</b>	<u>(242,801)</u>	<u>(755,208)</u>
<b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>	(50,858)	(262,444)
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	<u>112,813</u>	<u>375,256</u>
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<u>\$ 61,955</u>	<u>\$ 112,812</u>
<b>SUPPLEMENTAL INFORMATION:</b>		
Cash paid during the year for interest	\$ 13,526	\$ 32,466

See accompanying notes.

**NATURAL ENERGY UTILITY CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2011 AND 2010**

**NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Date of Management Review

Subsequent events have been evaluated through February 13, 2012, which is the date the financial statements were available to be issued.

Nature of Operations

Natural Energy Utility Corporation (the Corporation) owns and operates a natural gas pipeline in Boyd and Greenup County, Kentucky. The Corporation provides transportation services and sells natural gas to governmental, industrial and residential customers in its market area consisting primarily of Boyd and Greenup County, Kentucky. The Corporation is subject to regulation by the Kentucky Public Service Commission.

Use of Estimates

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

Cash and Cash Equivalents

For the purposes of the statements of cash flows, the Corporation considers cash on deposit with banks and all highly liquid debt instruments, purchased with an original maturity of three months or less to be cash equivalents.

Trading Securities

Trading securities are classified at their fair values. Unrealized gains and losses on trading securities are included in other income.

Income Taxes

The Corporation, with the consent of its shareholders, has elected under the Internal Revenue Code to be an S-Corporation. In lieu of corporation income taxes, the shareholders of an S Corporation are taxed on their proportionate share of the Corporation's taxable income. Therefore, no provision or liability for federal income taxes has been included in the financial statements.

Accounts Receivable

Accounts receivable are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a charge to earnings and

**NATURAL ENERGY UTILITY CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2011 AND 2010**

**NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

credit to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. Changes in the valuation allowance consisted of provisions of \$1,817 and \$585, and net charge-offs of \$1,817 and \$685 for the years 2011 and 2010, respectively.

Property and Equipment

Land is carried at cost. Property, furniture and equipment are carried at cost less accumulated depreciation computed principally by the straight-line method over the estimated useful lives of the assets. Expenditures for maintenance, repairs and improvements which do not materially extend the useful lives of the assets are charged to operations in the periods incurred.

Advertising

Advertising costs are expensed when incurred.

**NOTE B: PROPERTY AND EQUIPMENT**

Property and equipment at December 31, 2011 and 2010, by major classifications are as follows:

	<u>2011</u>	<u>2010</u>
Land	\$ 5,000	\$ 5,000
Buildings and improvements	74,553	74,553
Furniture, fixtures & equipment	166,278	155,557
Autos and trucks	259,896	259,896
Pipelines and projects	<u>2,829,865</u>	<u>2,829,865</u>
	3,335,592	3,324,871
Accumulated depreciation	<u>(2,675,861)</u>	<u>(2,458,098)</u>
	<u>\$ 659,731</u>	<u>\$ 866,773</u>

Depreciation expense charged to operations for the years ended December 31, 2011 and 2010 totaled \$217,763 and \$261,065, respectively.

**NOTE C: LINE OF CREDIT**

The Corporation has available a \$850,000 line of credit expiring August 5, 2012, interest to be paid monthly at the Wall Street prime interest rate (currently 3.25%), secured by the Corporation's assets and a personal guarantee by the principal shareholder. There was \$500,000 outstanding on this line of credit as of December 31, 2011.

**NATURAL ENERGY UTILITY CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2011 AND 2010**

**NOTE D: OTHER LIABILITIES**

The Corporation's long-term debt at December 31, 2011 and 2010 consisted of the following:

	<u>2011</u>	<u>2010</u>
Note payable to the Poca Valley Bank dated October 23, 2009, refinanced February 11, 2011. Interest on the note was Wall Street prime (3.25%) during 2011. Monthly principal payments were \$23,333, with a balloon payment for the unpaid balance due January 25, 2013. This note was collateralized with the Corporation's property and equipment, accounts receivable, inventory, and a personal guarantee by the principal shareholder.		
Unpaid balance at December 31,	\$ -	\$ 699,703
Note payable to Kubota Credit Corporation dated March 5, 2009, due in 36 monthly principal payments of \$1,445 beginning April 5, 2009. This note was collateralized with a Kubota excavator.		
Unpaid balance at December 31,	-	20,226
Total long-term debt at December 31,	-	719,929
Less: current portion	-	(297,337)
Long-term debt, net of current portion	<u>\$ -</u>	<u>\$ 422,592</u>

**NOTE E: CONCENTRATIONS**

Cash Balance

The Corporation maintains its cash in bank deposit accounts. The Corporation's depository institution, in accordance with a repurchase agreement, sweeps excess cash into an interest-bearing account that matures daily. The sweep account is collateralized with investment securities of the depository institution.

Major Customers

Three major customers accounted for 78.63% of total sales for 2011. Accounts receivable from these three customers comprised 86.33% of total accounts receivable at December 31, 2011. The same three major customers accounted for 72.00% of total sales for 2010. Accounts receivable from these three customers comprised 72.02% of total accounts receivable at December 31, 2010.

**NATURAL ENERGY UTILITY CORPORATION**  
**NOTES TO FINANCIAL STATEMENTS**  
**December 31, 2011 AND 2010**

**NOTE F: OPERATING LEASES**

The Corporation entered into a lease agreement for a vehicle under an operating lease which expires at July 2014. The following table summarizes minimum payments due under the lease agreement by year:

Due in:	
2012	\$ 8,202
2013	8,202
2014	<u>4,785</u>
	<u>\$ 21,189</u>

Total rental expense under operating leases was \$9,110 for the year ended December 31, 2011.

**NOTE G: RETIREMENT PLAN**

Effective October 1, 2007, the Corporation adopted a 401-K retirement plan covering all eligible employees. The Corporation has elected to make safe harbor contributions of 3.0% of all qualifying employee compensation. Contributions to the plan totaled \$20,859 and \$9,109 for the years ended December 31, 2011 and 2010, respectively.