Project Drake
Draft Due Diligence Findings

January 23, 2017

This written communication is solely for PNG Companies, LLC's benefit (the "Client") and is not intended to be relied upon by any other person or entity.

This written communication has been prepared on the basis set out in the Scope and Basis of Engagement on Page 2 and in the Appendices attached hereto.

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Scope and Basis of Engagement

Scope of Services

Pursuant to the engagement letter, dated January 3, 2017, PNG Companies, LLC. (the "Client") has engaged Deloitte & Touche LLP ("Consultant") to perform certain services in connection with Client's evaluation of a proposed acquisition of a company code-named Project Drake ("Target") (the "Proposed Transaction").

This written communication summarizes Consultants significant findings and observations resulting from the performance of the services described in *Appendix 1 – Scope of Services* through January 22, 2017 (the "Services"), which were primarily comprised of:

- To the extent relevant to our scope, read and analyzed publicly available information in the Target's SEC filings and on its website (including Target's 10-K through FY16 and 10-Qs through Q1-17), and information provided in the Target's virtual data room ("VDR"), in an effort to identify potential deal issues.
- Prepared a supplemental data request list based on potential key diligence areas identified during our diligence process.
- Reviewed the 2015 and 2016 audited working papers, including the tax provisions, of Deloitte & Touche LLP, the Target's independent auditors, to the extent made available to us.
- Held telephonic meetings and conducted high-level inquiries of certain members of Target's management, including John Brown, Chief Financial Officer, Matthew Wesolosky, Controller, and Brian Ramsey, Vice President (collectively, "Management") on January 20, 2017.
- Participated in an initial tax due diligence call on January 17, 2017 primarily discussing open data requests and initial diligence questions with Management.
- Participated in a tax due diligence call on January 20, 2017 with Management to discuss income and non-income taxes.

Issue Focus

This written communication is limited based on our preliminary scope focused on publicly available data and limited information in the data room and focuses on those matters that, based on Consultant's discussions with Client, Consultant believes would be of significance or interest to Client or might warrant further consideration by Client including:

- Quality of earnings
- High level working capital trend analysis
- Potential exposures
- Tax exposures
- Tax basis in assets and other tax attributes

Neither we nor this written communication will express an opinion or any other form of assurance with respect to any matters as a result of the performance of the Services, including, without limitation, concerning the feasibility or achievability of any forward-looking information.

This written communication may not encompass all communications, whether in writing or otherwise, made by Consultant to Client in connection with the Services or the Proposed Transaction. Other factors not discussed or referred to in this written communication should be considered in evaluating the merits of the Proposed Transaction, including, among other things, the consideration to be paid and the future operations or prospects of the Target.

We have not discussed in detail our specific observations with management of the Target or its representatives, or provided them with a copy of this written communication.

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Scope and Basis of Engagement

Scope Limitations

Given the short time frame and limited access to Target personnel and information, our analyses and inquires were substantially less comprehensive than we may have otherwise performed; therefore, our observations to date are preliminary and subject to further due diligence analyses and inquiries, if any. Had the scope of Services not been restricted, we may have identified additional matters that you may consider relevant to Client's investment decision.

See Appendix 2 – Scope Exclusions and Limitations for a description of services that were specifically excluded from the scope of our engagement and additional scope limitations.

Subsequent Events

Our findings and observations are based on financial and other information through September 30, 2016. Significant events and circumstances affecting such information may have occurred since the periods listed above and such events or circumstances might be considered material by Client or any third party. We have no responsibility for performing any services or procedures beyond those agreed to with Client, or for updating the Services.

Restrictions on Use and Distribution

This written communication was prepared solely for Client's benefit, and is not intended to be relied upon by any other person or entity. Neither the Services, nor this written communication, may be disclosed to any person or entity other than Client, or in any written materials related to the Proposed Transaction, including, without limitation, any publicly filed documents, without our prior written consent.

The observations described in this written communication do not constitute in any way a recommendation by us for Client or any other person or entity to participate in the Proposed Transaction or any related transaction and are not part of or being made available in connection with any prospectus, offering circular, or otherwise part of any soliciting, promoting, marketing, underwriting, recommending, or selling of securities or other interests.

Matters for Follow Up

This draft written communication contains certain outstanding matters identified by square brackets ("[ ]") that may warrant further consideration, clarification, or confirmation. Accordingly, this written communication may be subsequently modified. See *Appendix 3 – Matters for Follow Up* for a detailed listing of all open items.

Certain Terms of Engagement

The Services are subject to the terms and limitations set forth in *Appendix 4 – Certain Terms of Engagement*.

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Financial Due Diligence Key Findings

Key finding	Observations	Implications
Executive Summary Note	*The following presents a brief summary of key observations noted in the course of our due diligence efforts. Please note that this executive summary is not intended to be read on a stand-alone basis. The main body of this memorandum contains a more detailed discussion of key observations, as well as other matters, and should be read together with the executive summary.*	

We have identified potential adjustments to normalize EBITDA for certain non-cash items as well as non-recurring items for LTM Sep-16.

Observations

- The following is a high level summary of EBITDA after considering diligence adjustments. Management does not actively track or prepare potential non-recurring adjustments to reported EBITDA.
- Preliminary diligence adjusted EBITDA totaled $18.3m during LTM Sep-16, a 9% decrease from FY15.
- The Target's regulated and non-regulated business have been impacted by a warmer than normal winter and a decline in natural gas prices during FY16 as compared with FY15. The regulated segment has certain recovery mechanisms in place that insulate earnings from the impact of weather and prices. Refer to subsequent key findings for additional discussion on the regulated and non-regulated segments.

Preliminary Normalized EBITDA

US$000	FY15	FY16	LTM Sep-16
Revenue	86,188	64,130	64,245
% Growth		*(26)%*	*0%*
Operating income	12,964	11,434	11,306
As a % of revenue	*15%*	*18%*	*18%*
Net income	6,496	5,529	5,596
Reported EBITDA	**19,367**	**17,854**	**17,828**
As a % of revenue	*22%*	*28%*	*28%*
Potential diligence adjustments	913	553	471
Diligence Adjusted EBITDA	**20,280**	**18,407**	**18,299**

Source: Management information and Deloitte analysis

Implications

- Potential diligence adjustments relate to the following:
  - Add-back of non-cash share-based compensation ($471k in LTM Sep-16)
  - Normalization of bad debt expense ($100k in FY16)
  - Potential cost synergies related to public company costs (not quantified)
  - Potential transaction-related costs (not-quantified)
  - Potential non-recurring benefits from the non-regulated business (not quantified)
- Refer to *Quality of Earnings* section for additional information on preliminary diligence adjusted EBITDA.
- The Target recovers net periodic pension cost in rates based on the calendar 2009 test year amount of ~$1.2m annually. Because the Target does not maintain a tracking account for the difference between actual net periodic cost and the amount assumed in rates, each subsequent years' earnings have benefited or suffered by amount which actual cost is under or over $1.2m. Refer to *Appendix 5: Supplemental Schedules : Projected Pension Expense* for further details.
- Although we have not proposed a normalization adjustment related to the difference between actual net periodic cost and the $1.2m assumed in rates, Client should note that the difference resulted in a ~$700k benefit in FY15 and a ~$390k benefit in FY16. The FY17F net periodic pension cost of $1.3m implies that the Target will not recover $100k of cost in rates.

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Financial Due Diligence Key Findings

Key finding

Client should consider declining return on equity over the last three years, noting that it has been six years since the Target filed a rate case.

Observations

- The Target's regulated segment provides distribution and transportation service to 36,000 customers and is regulated by the Kentucky Public Service Commission ("KYPSC") under cost-of-service ratemaking. In FY16, the regulated segment accounted for 64% of total revenues. The regulatory structure in Kentucky appears to generally operate under similar constructs as in other states in that the regulators approve an authorized return on rate base and authorized return on equity as established under periodic rate cases.
- The Target's last rate case with KYPSC was filed in 2010 and based on a calendar 2009 test year. It resulted in a revenue requirement of $51.4m and a rate base of $110m with an allowed operating income of $8.8m,which was calculated by applying 8% WACC to rate base. At the time of the filing, the Target's capital structure was 44.5% equity ($56.5m) and 55.5% debt ($70.5m) and the allowed return equated to 10.4% return on equity ("ROE").
- The table below calculates actual ROE as net income from the regulated segment divided by total equity, and is based on amounts presented in the Target's Form 10k filings. As shown, actual ROE has declined from 8.5% in FY14 to 6.6% in FY16, which is below the ROE of 10.4% allowed by regulators (actual ROE amounts below were not obtained from any regulatory filings or reports):

US$000s	FY14	FY15	FY16
Equity	74,728	77,222	77,727
Long term debt	53,500	52,000	50,423
Short term debt	1,500	1,500	1,500
Total capital	**129,728**	**130,722**	**129,650**
Net income - regulated segment	6,379	5,748	5,144
Actual ROE	8.5%	7.4%	6.6%
Allowed ROE	*10.4%*	*10.4%*	*10.4%*

Source: Case No. 2010-00116; FY14 - 16 Form 10ks

- The Target has various riders and clauses which it recovers in rate cases, such as Weather Normalization ("WNA"), Gas Cost Rider ("GCR"), Pipe Replacement Rider ("PRP"), and Conservation / Efficiency Program ("CEP"). The Target has not recognized any new or unprecedented regulatory assets since the last rate case. Refer to *Other Quality of Earnings* section for additional information regarding the Target's rate *recovery* mechanisms.

Implications

- Management indicates that it has a favorable relationship with KYPSC. The primary reason for the six year gap since the last rate case has been adequate recovery under the PRP and GCR mechanisms. During FY16, the Company's revenue requirement was calculated based on a calendar 2015 test year to determine sufficiency of rates. Based on this analysis, Management determined that the Target's rates are currently designed to recover its cost of service and provide current recovery of regulatory assets not recovered through periodic filings.
- The decrease in actual ROE in FY15 and FY16 shown at left may indicate that the Target needs to file for additional returns in rates, however, other factors appear to mitigate this. Client should consider that the Target's capital structure has shifted from 44.5% equity and 55.5% debt in its 2010 rate case to 59% equity and 41% debt as of Sep-16.
- Management indicated it will likely end up with a lower rate base if it goes back to the KYPSC. Client should consider the potential capital needs of the business and long-term growth trends based on the target's recent investment opportunities and downward trends in net rate base.
- Client should perform a detailed examination of each regulatory program to identify further benefits and exposure associated with the Target's rate regulated operations; as well as differences to Client's current regulatory construct.
- Management indicated that it has recently started exploring opportunities to rebalance its capital structure, such as special dividends or share buyback programs.

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Financial Due Diligence Key Findings

Key finding	Observations	Implications
Warmer than normal temperatures led to a 22% decline in revenues from the Target's regulated segment in FY16.	• The Target's regulated segment sold lower than normal volumes of natural gas due to a warm winter during FY16. Overall regulated revenues decreased 22% from the prior year. Over the same period, heating degree days were 17% warmer than the thirty year average (compared with 10% colder than the average in the previous year). The decline in volumes sold during FY16 was partially offset by increased bill rates passed to customers through the Target's weather normalization and pipe replacement tariffs, though management indicated that the WNA does not fully offset the impacts of actual weather variance.	• The Target's weather normalization tariff only partially mitigates the Target's risk due to weather as it only covers December through April billing cycles. To the extent the dip in ROE in FY15 and FY16 was caused by weather not covered in the WNA period, it would not be included in rates.
The Target's net working capital needs vary seasonally with increased working capital commitments during the winter months.	• The Target's definitional adjusted net working capital averaged $7.5m over the last four quarters ending Sep-16, which removes non-operating items such as cash and cash equivalents, current portion of long-term debt, accrued interest, and deferred income taxes. Due to our limited scope of services, we have not performed comprehensive diligence procedures on the Target's working capital nor have we identified potential normalizing working capital adjustments. • The Target may have certain capital expenditures recorded in accounts payable or accrued liabilities. To the extent these are included, we would remove them from working capital as these do not reflect the recurring operations of the business. • The Target appears to maintain cash balances in excess of its working capital needs. Further, Target has a $40m line of credit available that it has not historically used. Refer to *Net Working Capital* section for additional discussion on the Target's preliminary adjusted net working capital.	• The Target has negative operating earnings from June to September. Deviations from normal weather conditions and the seasonal nature of the Target's business can create fluctuations in earnings and short-term cash requirements. Client should consider the impact on working capital requirements during these periods. • Consideration should be given to the potential impact of increasing natural gas and other fuel prices on the Target's working capital needs. • Client should consider appropriate financing necessary to meet Target's working capital needs and continuing capital investments. There may be opportunities to increase efficiency in this area post close by optimizing cash balances.

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Financial Due Diligence Key Findings

Key finding	Observations	Implications
Revenue of the Target's non-regulated segment declined by $10.6m, or 31.7%, from FY15 to FY16, as a result of falling natural gas prices and reduced demand due to warmer than normal weather.	• Revenue of the Target's non-regulated segment declined by $10.6m, or 31.7%, from FY15 to FY16, as a result of falling natural gas prices and reduced demand due to warmer than normal weather. Non-regulated gross margin remained relatively consistent, increasing from 20% to 23% over the same period, as the majority of the Target's non-regulated contracts are based on a index-plus-margin rate. There are no sales to the regulated segment. • For variable priced contracts, the Target will purchase at an index rate and add a margin (i.e. a percentage of the purchased gas costs) to the contract. For fixed priced contracts, the Target will lock in a price to purchase supply at the same time as the customer's requested delivery, limiting exposure to lost margins due to price risk. The majority of such fixed contracts last for only one month, however, certain customers may negotiate contracts longer than one month. • The Target earns a small portion of its non-regulated revenue through natural gas liquid sales ($1.1m in FY15 and $250k in FY16). The processing facility that removes the natural gas liquids from gas in storage and pipelines is owned by the Target's regulated segment. • The Target purchases substantially all of its non-regulated and regulated natural gas supply from only two suppliers: Midwest and Atmos. For the non-regulated segment, the underlying agreements with these suppliers do not include minimum purchase quantities or requirements to purchase natural gas for any period longer than one month at a time. Purchases from Midwest are based on index prices or mutually agreed upon fixed prices that are based on forward contracts. As of Sep-16, the Target has $685k committed under forward purchase obligations through Dec-17. The Atmos agreement provides for spot purchases on a month-to-month basis. • The non-regulated segment has no employees and limited fixed assets. The regulated segment allocates it a share of its G&A costs and charges it a variable charge for storage proportional to volumes injected / withdrawn. The variable storage charge is based solely on variable storage and O&M costs and excludes fixed costs and capital charges. The non-regulated segment also pays the regulated segment for transportation services at tariff rates, which eliminate through consolidation.	• Client should consider the risk that further declines in the price of natural gas could impact non-regulated revenues and gross margins. Refer to *Other Quality of Earnings* section for additional information on the Target's price volume changes in revenue from FY15 to FY16. • As the Target's non-regulated customers are primarily industrial and large-volume customers, there is a risk that these customers will obtain their natural gas supply by purchasing directly from interstate suppliers, local producers or marketers which would impact non-regulated profitability. • The Target's gas supply is highly concentrated with only two providers. Any interruption of service from these providers could have a substantial impact on its business. • Client should consider the recurring treatment of natural gas liquid sales, as well as the fully burdened cost of natural gas storage services utilized by the non-regulated business and any potential related exposures in its valuation. • Client should consider performing further analysis on the Target's cost allocation policies, including requesting formal cost allocation manuals, to better understand the allocations between the regulated and non-regulated business.

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Financial Due Diligence Key Findings

Key finding	Observations	Implications
The Target had reported net debt of $39.8m at Sep-16.	• The Target had reported net debt of $39.8m at Sep-16, made up of cash and cash equivalents, current and long-term debt obligations, and accrued interest. Potential debt and debt-like items include change in control payments ($14.8m), asset retirement obligations ($4m), the unfunded portion of the Target's pension ($1.2m), and other items. • The Target has employment agreements with key executives which provide future payments and specified benefits following a change in ownership. At Sep-16, Management estimates that the lump sum value of such payments in the event they were exercised totals $14.8m. • The Target has a potential $2.2m payout to its transaction advisors due at the close of the Proposed Transaction, contingent upon a successful sale. • The Target is considering adding an additional storage well in FY17 to further enhance the value and capabilities of its storage operations. To date, the Target has not recorded a liability associated with the cost to retire its wells because it considers them to have indeterminate useful lives.	• At Client's request, we performed only high-level due diligence procedures on potential unrecorded obligations, commitments and contingencies and net debt. Additional diligence procedures may result in identification of additional obligations. These may include unrecorded obligations on any non-regulated operations and, as appropriate, such obligations should be considered net debt in the Proposed Transaction. Refer to *Net Working Capital & Net Debt* section for additional discussion on the Target's preliminary net debt and debt-like items at Sep-16. Amounts are presented for informational purposes only. • Client should consider potential exposures to environmental and asset retirement obligations in future periods. Such obligations related specifically to the regulated operations may be recoverable in rates. • Client should consult with your legal advisors regarding any potential change in control exposure and the impact on the Proposed Transaction. • The Client should reflect any transaction expenses as a reduction in the enterprise value (or increase in net debt) of the acquired business.

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Pension Due Diligence Key Findings

Key finding	Observations	Implications
While the Target recovers the U.S. GAAP pension expense as part of the rates charged to regulated customers, the rates have been locked in since the last rate case in 2009, and there is no mechanism to true-up recovery to the actual annual expense.	• The Target sponsors a US qualified pension plan that covers all eligible employees hired prior to May 9, 2008 (approximately 150 employees). The pension plan does not include employees of the non-regulated business. The net balance sheet (liability) was ($1.9m) as of Jun-16 and ($1.2m) as of Sep-16 on a U.S. GAAP basis. • Current cost-of-service ratemaking in Kentucky allows recovery of net periodic pension cost ("NPPC") as determined under U.S. GAAP. However, rates have last been set to reflect NPPC booked in calendar 2009 and adjusted in calendar 2010 to reflect subsequent increases in FY10 NPPC. The pension NPPC reflected in rates since 2010 is $1.2m which has been greater than actual NPPC in all years until calendar year 2016. There is no mechanism to true-up the rate recovery and thus the Target bears the risk and benefit of variance between the annual pension expense and that included in the rates. • The NPPC includes amortization of unrecognized net loss and amortization of prior service cost. These unrecognized balances and amortizations fluctuate based on actual plan experience (e.g. asset returns and changes in discount rates). The Target records a regulatory asset equal to the full amount of unrecognized balances ($10.9m as of Jun-16) representing the probable recovery of the unrecognized balances in future net periodic benefit cost. • Based on standard acquisition accounting methodology, the Target would recognize the full unfunded liability on the balance sheet as of the closing date, with no unrecognized balances. This would result in lower NPPC as the amortization amounts (which have historically been positive) would be eliminated. • The Target has not had a minimum required contribution in several years. The Target policy has been to contribute $0.5m per year, and has contributed up to $1m based on broader Target cash and tax planning considerations in several recent years. The Company continues to be overfunded on a statutory basis and carries a "credit balance" of $1.0m which can be used to offset any future statutory minimum required contributions. • The Target confirmed that there are no other pension plans, and no other postretirement employee benefits (OPEB).	• In general, the plan is very well funded and would likely not require a contribution for at least a few years. The plan should continue to provide the Target flexibility in cash management and planning. • Assuming that a new rate case will need to be filed in conjunction with the transaction, the Client will need to consider the impact of NPPC on future rates. Current rates include approximately $0.4m of amortizations which would be eliminated in the case of purchase accounting. Furthermore, we estimate FY18 expense of $1.0m on an ongoing basis (at 4.0% discount rate), which includes approximately $0.4m of amortization which would be eliminated in purchase accounting. The Target should work with regulators to understand the alternatives for setting rates given the circumstances. • Historically, the Target has held the full amount of unrecognized pension costs as a regulatory asset on the basis that it would eventually be recovered through NPPC. Client should evaluate this regulatory accounting policy given that there appears to be no process to reconcile the actual NPPC with the amount allowed in rates and therefore no ability to recover higher pension costs between rate filings. Future pension expense for regulatory rates will likely be computed on a pre-acquisition basis, thus potentially making this asset still recoverable. However, an assessment will be required and could also result in a conclusion that the asset should be valued at zero, which would result in a change to future earnings as compared to historical given the loss of the amortization of this asset.

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Tax Due Diligence Key Findings

Key finding	Observations
Tax Profile	• The Target was incorporated in 1949 and is headquartered in Winchester, Kentucky. The Target distributes or transports natural gas to both residential and industrial customers throughout central and southeastern Kentucky. The Target, through wholly owned subsidiaries, also participates in the extraction and storage of natural gas. Target wholly owns three operating subsidiaries, Delta Resources, Inc. (“Resources”), Delgasco, Inc. (“Delgasco”), and Enpro, Inc. (“Enpro”). • Refer to the organizational structure chart located Appendix 5. • All federal and state income tax returns are prepared internally by Management and various accounting staff and reviewed by Deloitte Tax LLP (“Deloitte”). The tax provision of the Target is also prepared internally. • Tax Advisor stated that they are not aware of any waivers to the statute of limitations for federal or state income tax purposes. • Management stated that no income or non-income tax reserves are currently recorded for uncertain tax positions. The Target recorded an approximately $66k reserve in June-2013 related to repair and maintenance deductions taken on the FY09 tax return. The reserve was written off during FY14 due to the statute of limitations expiring with respect to FY09. • No audits for federal or state income or non-income tax matters has been performed in the last five years and there are currently no known or pending examinations. The last audit was conducted by the IRS of the FY2008 and FY2009 federal tax returns. The audit resulted in an additional tax assessment of approximately $107k related to Target failing to limit its deduction for the vacation accrual to the portion of the vacation accrual applicable to vacation time taken within 2 1/2 months of year end.
Federal Income Taxes	• The Target is classified as a C corporation for federal income tax purposes and has historically filed a fiscal year July 1 through June 30 Form 1120, US Corporation Income Tax Return. Subsidiaries Resources, Delgasco, and Enpro are included with Delta Natural Gas Company, Inc. on Target’s consolidated federal income tax return. • Refer to Appendix 5 for the Target’s book income to taxable income reconciliation. • The Target currently has tax basis of approximately $23m and $3.8m in depreciable and non-depreciable property, respectively, remaining on its tax basis balance sheet. Refer to Appendix 5 for Target’s rollout of tax depreciation deductions.
State Income Taxes	• In FY2015, the Target filed a consolidated Kentucky state income tax return as well as a consolidated Tennessee Franchise/Excise Tax Return. All of Target’s operations, assets, and revenue are derived from Kentucky with the exception of approximately a half of a mile of pipe that extends into Tennessee.
Property Tax	• Property tax compliance is completed internally by Management and other accounting staff. • Property tax returns for both real and tangible personal property are filed in approximately 43 jurisdictions in Kentucky. • Management stated they annually send the Kentucky state tax authorities various documents related to the net book value of assets. The state replies with an initial assessment in which Management negotiates in subsequent weeks to a lower amount satisfactory to both the Target and tax authority. No formal valuation disputes are generally completed.

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Tax Due Diligence Key Findings

Key finding	Observations
Unclaimed Property	• Management indicated that the Target files and remits unclaimed property with various state jurisdictions on an annual basis. Unclaimed property that has been outstanding for greater than three years is typically remitted. Management was not able to recall the amount or type of unclaimed property typically remitted every year but indicated it was not generally material.
Sales and Use Taxes	• Sales and use tax compliance is generally handled internally by Management and accounting staff at the Target. • Monthly sales and use tax returns are filed by the Target in the state of Kentucky. Management stated that no sales tax returns are filed in Tennessee since there are no customers in Tennessee • Management stated gas sales to end users other than residential customers is typically subject to sales tax. Formal queries are established in the billing department to ensure the proper customers are charged sales tax (i.e., everyone except for residential customers) and amounts are remitted to the state on a monthly basis.
Payroll Tax	• Payroll tax compliance (e.g., withholding and quarterly return filing) is generally handled internally by the Target's payroll department. • We received a summary document that indicated the Target paid 4 individuals on a Form 1099 totaling $60k (i.e., approximately $15k per person) in calendar year 2016. Management stated these individuals are former employees who are generally paid as consultants for a short period following their departure from the Target. While we did not receive actual copies of the 1099s, based on Management's assertions and the size of the payments, we did not pursue the matter further.
Transfer Taxes	• Due to the structure of the Proposed Transaction (i.e., a purchase of stock), we do not foresee the state of Kentucky imposing material transfer taxes on tangible personal property or real estate being indirectly transferred.
Regulatory Matters	• No tax-related regulatory assets exist. Deferred taxes are normalized for all temporary differences (i.e., the flow-through method is not used). • The only tax-related regulatory liability relates to the increase in Kentucky income tax rate in 2005 (i.e., state excess deferred taxes). The liability is amortized over the remaining book lives of the property with depreciation-related deferred taxes as of 2005 and is expected to be completely settled in August 2026. • Investment tax credit claimed in prior years is completely amortized. • The last rate case was completed at the end of 2009. The test year was a historical period. Management indicated that there were not significant issues involving accounting for income taxes. • We inquired regarding the treatment of pre-acquisition deferred tax liabilities related to the Target's asset acquisitions in the 1990s. Management described regulatory accounting that complies with the normalization requirements. • According to Management, the Target has not received any government grants in recent years. Reimbursements for relocations of gas mains received from governmental entities are treated as excludable non-shareholder contributions to capital for tax purposes, which appears appropriate based on the facts discussed with Management.

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Tax Due Diligence Key Findings

Key finding	Observations	Implications
Transaction Structure and Successor Liability	• We understand the Proposed Transaction is to be structured as an acquisition of 100% of the stock of the Target, which is classified as a C corporation for federal and state income tax purposes. • The Target's stock is publicly traded on the NASDAQ stock exchange.	• Due to the structure of the proposed acquisition (i.e., stock purchase for federal income tax purposes), any historical income and non-income tax exposures will generally remain the responsibility of the Target and indirectly Client post-closing. In addition, any adjustments to corporate taxable income proposed by tax authorities upon an examination of previously filed corporate income tax returns will be the responsibility of the Target and indirectly Client post-closing. • In a stock acquisition, the buyer generally obtains a cost basis only in the acquired company's equity. Further, the tax basis in the Target's assets is expected to carryover post-closing (i.e., no adjustment in tax basis).
Method of Accounting Changes	• The Target has filed several Form 3115s, Application for Change in Accounting Method, in the last ten years to change its methods of accounting with respect to repairs or retirements of tangible property. • In 2009, the Target changed its method of accounting to expense repair costs for expenditures related to its natural gas pipelines if the repairs neither materially add to the value or life of the pipeline. The method change resulted in an approximately $8.6m deductible IRC Section 481(a) adjustment. • In 2015, the Target made a number of automatic changes to expense items related to repairs, maintenance, and non-incidental supplies that specifically excluded natural gas transmission and distribution network property. The method change resulted in no IRC Section 481(a) adjustment.	• The Target's accounting method changes appear to be similar in nature to accounting method changes made by other regulated utilities prior to the effective date of the final tangible property regulations. Also, Management indicated the Target is waiting on further guidance from the IRS to provide "safe harbor" units of property definitions for gas transmission and distribution property and intends to adopt such guidance. • While we did not identify any material issues with respect to the Target's historical accounting method changes, we would have expected Target to have made an accounting method change in 2015 in conjunction with adoption of the final tangible property regulations with respect to the retirement of its natural gas distribution assets to correspond with the 2009 change in definitions of components used for expenditure/repair purposes. • We understand it is Management's intention to make these changes when the further guidance is released by the IRS related to the utility industry. If this is the case, the Target will have another opportunity to make the asset retirement method changes in tandem with the newly released unit of property guidance.

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Tax Due Diligence Key Findings

Key finding	Observations	Implications
Hedge Identification	• We understand from Management that Target does not have any formal policies or procedures to identify its hedges and derivatives for US federal income tax purposes. We understand that Target enters into forward purchase contracts to purchase natural gas as part of its unregulated business. • In general, a hedging contract such as a forward contract or interest rate swap, is eligible for ordinary loss treatment (i.e. not considered a capital asset) as long as the contract is clearly identified as a hedging contract for US federal income tax purposes within 35 days of the date the contract was acquired, originated, or entered into by the taxpayer.	• If a derivative or interest rate swap contract is not timely identified as a hedging contract for US federal income tax purposes, any loss recognized on the early termination of such contract is generally treated as a capital loss. Relief for failure to timely identify a hedging contract may be available if an inadvertent error can be demonstrated to the satisfaction of the IRS. • We would suggest that Target seek relief for failure to timely identify its derivative and hedging contracts in connection with the filing of its FY16 US federal income tax return. • In addition, we would suggest that Target implement formal polices and procedures going forward to ensure that its timely identifies its derivatives as hedges for US federal income tax purposes.
Section 280G "Golden Parachute" Payments	• The Proposed Transaction is expected to accelerate the vesting period for certain equity holders of the Target. These accelerated payments may be considered excess parachute payments under IRC Section 280G ("280G"). • Excess parachute payments generally exist when a disqualified individual receives total payments on a change in control that equal or exceed three-times their "base amount" (generally the individual's average W-2 earnings over the previous five years). If the total parachute payments exceed this three-times-base threshold, then only the individual's base amount is deductible (i.e., the amount in excess of the base amount is non-deductible). [redacted] • Further, the amount of the parachute payments in excess of the base amount is subject to a 20% excise tax to the individual.	• Section 280G eliminates the corporate tax deductions related to "excess parachute payments" that result from change in control payments to "disqualified individuals" (i.e., the top 1% of all employees ranked by pay, corporate officers, and certain significant shareholders) as well as imposes an excise tax of 20% on these individuals. Target identified 5 "disqualified individuals," all who are subject to agreements that provide for Target to pay a "gross-up" to eliminate the impact of the 20% excise tax on the "disqualified individuals." • [redacted] The ultimate amount of gross-up payment and lost corporate tax deduction will depend on whether and when "disqualified individuals" are terminated. • Any implications of Section 280G could potentially be reduced through various strategies and valuations, depending on post-transaction services of the "disqualified individuals." As their agreements contain a non-compete provision while receiving payments (including severance), a valuation of the non-compete could be obtained to reduce the value of the parachute payments.

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Diligence adjusted EBITDA totaled $18.3m over the last twelve months, a 9% decrease from FY15.

Normalized EBITDA

US$000	FY15	FY16	LTM Sep-16
Net income	6,496	5,529	5,596
Depreciation and amortization	6,378	6,416	6,380
Interest	2,601	2,531	2,514
Income Taxes	3,892	3,377	3,338
Reported EBITDA	**19,367**	**17,854**	**17,828**
Potential diligence adjustments			
1 Share-based compensation	1,095	453	471
2 Non-regulated customer wins & losses	(182)	-	-
3 Normalization of bad debt expense	-	100	-
4 Potential non-recurring benefits from non-regulated operations			
5 Cost synergies			
6 Transaction-related costs			
Total diligence adjustments	**913**	**553**	**471**
Diligence Adjusted EBITDA	**20,280**	**18,407**	**18,299**
KPI's			
Reported EBITDA	*22.5%*	*27.8%*	*27.7%*
Diligence Adjusted EBITDA	*23.5%*	*28.7%*	*28.5%*

Source: Management information and Deloitte analysis

Preliminary Normalized EBITDA

Our Services with respect to normalized EBITDA consisted solely of assisting Client in the identification, documentation and accumulation of potential adjustments using criteria discussed with Client. Because there is no authoritative literature or common standard with respect to the calculation of normalized EBITDA, there is no basis to state whether all appropriate and comparable adjustments have been identified. In addition, while certain adjustments may reflect the elimination of unusual or nonrecurring revenues or expenses, future periods may include revenues or expenses that would also be considered unusual or nonrecurring.

Potential diligence adjustments

1. **Share-based compensation:** Represents the non-cash charge for the Target's key personnel. Additional expenses could be incurred due to the acceleration of long term incentives by a change-in-control related to the Proposed Transaction. Refer to *Net Working Capital & Net Debt* section for further discussion.
2. **Non-regulated customer wins & losses:** Non-regulated on-system sales decreased by $1.1m because the Target lost five customers. The losses were offset by $250k of incremental sales to Custom Food Products, who expanded their facilities and is expected to continue at this higher rate of consumption. This pro forma adjustment to FY15 reflects earnings as if the wins/losses took place at the beginning of FY15.

Non-Regulated Customer Wins and Losses

US$000	FY15	FY16	Change
Custom Food Products	483	733	250
Hoffman Engineering	420	-	(420)
CTA Acoustics	397	-	(397)
Masco Builder Cabinet Group	212	35	(177)
PPG Industrial, Inc.	109	-	(109)
Tokico	46	-	(46)
Net loss in revenue			(898)
Non-regulated gross margin FY15			20%
EBITDA Adjustment			**(182)**

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Client should consider whether certain benefits provided by Target's non-regulated business will continue in future periods.

Normalized EBITDA

US$000	FY15	FY16	LTM Sep-16
Net income	6,496	5,529	5,596
Depreciation and amortization	6,378	6,416	6,380
Interest	2,601	2,531	2,514
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Diligence Adjusted EBITDA	*23.5%*	*28.7%*	*28.5%*

Source: Management information and Deloitte analysis

Potential diligence adjustments (continued)

3. **Normalization of bad debt expense:** In FY16, the Target recorded bad debt expense of approximately $100k related to a specific customer. This expense was ultimately adjusted in Q1-17 upon collection of the outstanding balance. This adjustment nets to zero over the trailing twelve month period, however, it increases earnings by $100k during FY16.
4. **Potential non-recurring benefits from non-regulated operations**: Represents a place holder for further consideration of the Target's non-regulated business activities and whether such benefits (in particular related to NGL sales and storage utilization) will continue to be recurring. Client should consider any potential related exposures for such businesses.
5. **Cost synergies:** Represents a placeholder for potential cost synergies after the close of the Proposed Transaction. Client may realize cost savings related to public company costs (i.e. SOX compliance, extensive board members, public filing costs, etc.). Additional synergies may be realized by implementing Client's processes and systems over the coming periods. Further diligence is required to quantify potential cost savings.
6. **Transaction-related costs:** In FY17, the Target is incurring transaction-related advisory costs from Tudor, Pickering, Holt and Co. ("TPH"), related to the on-going sales process. Management has incurred approximately $400k in YTD17 with the majority of such costs being charged after Sep-16 and therefore not shown in the schedule at left. To the extent the Target incurs additional costs or such costs are accrued at the close of the Proposed Transaction, these should be treated as debt-like given their non-recurring, non-operational nature. In addition, TPH has a potential $2.2m payout due at the close of the Proposed Transaction. Refer to *Net Working Capital & Net Debt* section for further discussion.

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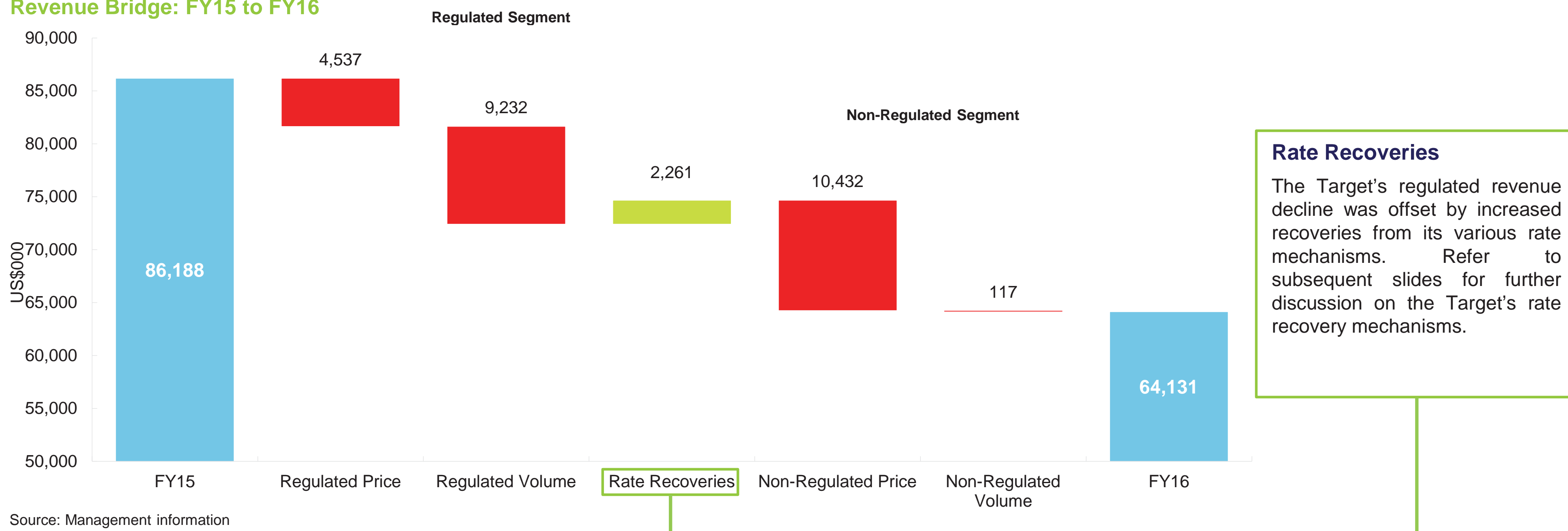
The Target's revenue declined 26% in FY16 compared FY15 due to declining natural gas prices and lower natural gas sales from a milder winter.

Other Quality of Earnings Considerations

The factors impacting the change in revenue from FY15 to FY16 are outlined below. Regulated revenues (comprised of both natural gas sales and transportation) decreased by $11.4m from FY15 to FY16, driven primarily by a decline in sales at the regulated segment due to higher than normal weather during December through April. Non-regulated revenues decreased by $10.3m primarily as a function of declining natural gas prices. Refer to the breakout below for further discussion.



Source: Management information

- Regulated sales decreased by $11.4m in FY16 compared to the prior year, made up of natural gas sales ($11.5m) offset by an increase in on-system transportation ($100k). Natural gas prices declined from $14.30/Mcf to $12.54/Mcf over the year. There was a GCR regulatory asset of $674k as of Jun-16 to be recovered in the next 12 months.
- Non-regulated off-system sales decreased by $7.8m in FY16 compared to the prior year, primarily due to the decline in natural gas prices from $4.09/Mcf to $2.76/Mcf. However, non-regulated volume was flat as sales with large customers (i.e. Atmos, Greystone, Midwest) remained consistent. The Target sold 101,000 Mcf's to a new customer, Citizens Gas Utilities, which provided additional revenue of $254k compared to FY15.
- Non-regulated on-system sales decreased by $1.9m in FY16 compared to the prior year, partially due to the decline in price from $6.49/Mcf to $5.57/Mcf and because the Target lost five customers, totaling $1.1m in lost sales. The losses were offset by $250k of incremental sales to Custom Food Products, who expanded their facilities. Refer to page 9 for further details.

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Client should consider implications on future free cash flow based on the Target's near-term capital expenditures.

Other Quality of Earnings Considerations

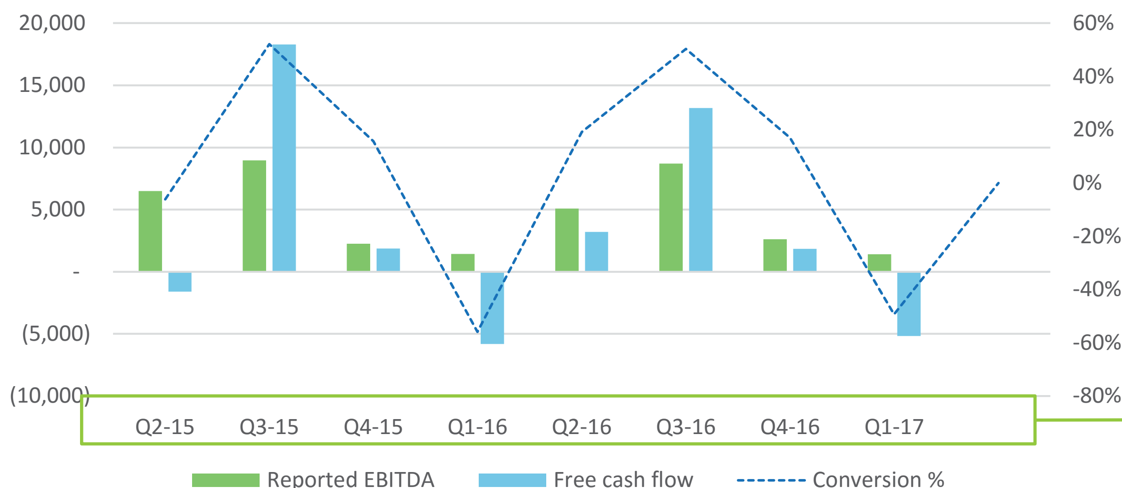
The following table and graph present the Target's free cash flow relative to reported EBITDA. For purposes of this analysis, changes in operating working capital represent changes in Reported Net Working Capital, adjusted for non-operational items such as cash, debt and debt-like items, and income tax assets and liabilities. Refer to *Net Working Capital & Net Debt* section for further discussion.

Free Cash Flow

US$000	Q2-15	Q3-15	Q4-15	Q1-16	Q2-16	Q3-16	Q4-16	Q1-17
Reported EBITDA	6,504	8,957	2,258	1,430	5,093	8,706	2,625	1,404
Change in NWC	(5,545)	10,636	2,218	(5,194)	(601)	5,770	893	(4,291)
Capital expenditures	(2,551)	(1,314)	(2,609)	(2,043)	(1,297)	(1,292)	(1,670)	(2,289)
Free cash flow	**(1,592)**	**18,279**	**1,867**	**(5,806)**	**3,195**	**13,183**	**1,848**	**(5,177)**
Total Revenues	**25,875**	**35,085**	**11,906**	**10,393**	**16,673**	**26,202**	**10,861**	**10,508**
Conversion %	*(6.2)%*	*52.1%*	*15.7%*	*(55.9)%*	*19.2%*	*50.3%*	*17.0%*	*(49.3)%*

Source: Management information and Deloitte analysis

Free Cash Flow - Quarterly



Free Cash Flow Trends

- Working capital presented herein is presented on an operating basis and excludes cash and debt-like items. The Target has historically maintained a large enough cash balance to cover periods of negative free cash flow.
- The Target's earnings and free cash flow are highest during the winter months in Q3 due to the peak heating season. Free cash flow is driven by the collection of accounts receivable and the depletion of gas in storage.
- The Target's free cash flow is negative during Q1 each year due to re-filling gas in storage and mild weather.
- The Target's capital expenditures totaled $9m in FY15 and $6.3m in FY16. Management indicated it anticipates spending approximately $8m in capex in FY17, primarily to build a new storage facility, which will be included in rate base. Management indicated that it has not incurred significant spending on this project yet as of Q1-17.

Guide to Quarters

- Q1 = July – September
- Q2 = October – December
- Q3 = January – March
- Q4 = April - June

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Client should consider the Target's regulatory environment and impacts to earnings of certain rate recovery mechanisms.

Other Quality of Earnings Considerations

Rate Summary and Recovery Mechanisms

The Target has approval from its regulators to defer certain capital and operating costs in regulatory rider mechanisms. These include various riders and clauses to recover costs and earn a return on equity. This allows the target to start earning a return on certain of its investments in advance of filing for a new rate case, thus extending the period required between rate cases. Client should consider that the Target's capital structure has shifted from 44.5% equity and 55.5% debt in its 2010 rate case to 59% equity and 41% debt as of Sep-16. The Target must either grow rate base to match the level of equity in the business capital structure or manage its equity and debt outstanding to achieve the "allowed" ROE. Management indicated that it has recently started exploring opportunities to rebalance its capital structure, such as special dividends or share buyback programs. Below is a summary of the 2010 rate order and a comparison to hypothetical Jun-16 values. Refer to *Appendix 5* for rate base calculations.

Allowed Return from 2010 Rate Case

US$000s	2010 Rate Case	Ratio	Rates	Cost	FY16 (1)	Ratio	Rates (1)	Cost
Equity	$ 56,492	44.5%	10.4%	$ 5,875	77,727	61.2%	10.4%	$ 8,084
Long term debt	58,459	46.0%	6.8%	3,993	50,423	39.7%	6.8%	3,444
Short term debt	12,016	9.5%	2.1%	252	1,500	1.2%	2.1%	31
Total	**126,967**			**10,120**	**129,650**			**11,559**
Weighted average cost of capital	8.0%				8.0%			
Rate base	109,805				100,137			
Net operating income per order	8,752				7,981			
Less interest expense	(4,245)				(3,475)			
Remaining return on equity	4,507				4,506			
Calculated ROE	8.0%				5.8%			
Projected return on equity with new rates								

Source: 7.4.12 Case No. 2010-00116 Order Recalculation.xlsx

(1) Rate base and Rates for FY16 have been assumed on a consistent basis as the 2010 rate case, however, the amounts are presented for informational purpose
Actual rate base calculations are subject to the purview of the KYPSC and may vary in the next rate case.

- **Gas Cost Rider:** The Target passes through changes in the price it pays for natural gas supply as well as any bad debt expense related to natural gas cost to its regulated customers. Under and over-recovered natural gas costs are collected or refunded through adjustments to customer bills beginning three months after the end of the quarter in which the actual costs were incurred and typically are fully recovered in 12 months. Any additional unrecovered balances after 12 months are amortized over 3 months based on a rate calculated by dividing the volume by rates from the prior year's same quarter. There are four components of the GCR mechanism:

(continued)

  - The expected gas cost component (EGC), which represents the average expected cost of gas supplies and may included fixed price, forward price and index price purchases.
  - The supplier refund adjustment (RA), which reflects refunds received from suppliers during the reporting period, plus interest at the average 90 day commercial paper rate for the calendar quarter. In the event of large or unusual refunds, the Target may apply to the Public Service Commission for the right to depart from the standard refund procedure.
  - The actual adjustment (AA), which compensates for difference between the previous quarter's expected gas cost and the actual cost of gas during that quarter.
  - The balance adjustment (BA), which compensates for any under or over collections which have occurred as a result of prior adjustments.

- **Weather Normalization:** The Target adjusts its rates for residential and small non-residential customers to reflect variations from thirty-year average weather for the December through April billing cycles. This adjustment is reflected only during the heating months and does not generate a regulatory asset as it is fully recovered in real time. The weather normalization tariff only partially mitigates the Target's risk as they will not recover all potential earnings.

- **Pipe Replacement Rider:** The Target's pipe replacement tariff allows it to recover the cost of accelerating the replacement of cast iron and bare steel distribution lines. Rates are adjusted annually to earn a return on capital expenditures incurred subsequent to its last rate case in October 2010. In addition, this tariff is designed to recover costs associated with the mandatory retirement or relocation of facilities. Management indicated the potential to accelerate such a program, however, they have not implemented that at this time.

- **Conservation / Efficiency Program:** The Target adjusts its rates for activities such as energy audits, rebates on the purchase of high-efficiency appliances, and promotion of conservation awareness. Revenue recovered from this tariff totaled $84k during FY16.

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The Target capitalized approximately 32% of its administrative time to capital projects in FY15 and FY16.

Other Quality of Earnings Considerations

Unbilled Revenue Methodology

- The Target's unbilled methodology uses billing information taken after the accounting month end or slightly before month end depending on meter read date (i.e. month ended June 30, 2016 would use billing information taken after 6/30/16 or very shortly before such as 6/29/16).
- The Target allocates the known revenue for the time period based on certain factors (pro rated fixed customer charge, variable base load and variable weather sensitive data based on degree days). For meters that do not have a full month in the last read (e.g. 6/29/16 read date) an estimate is made based on upon the previous thirty day read information and number of days left in the month and heating degree days. Such estimates represent less than 1% of the unbilled balance typically because Management does not close the books until 15 days after month end when substantially all bills are complete.
- A small percentage of regulated customers opt into budget or flat billing. It is normal for budget billing customers' accounts to be in credit positions as of the June year end due to low usage in the summer resulting the customers' flat rates being in excess of actual usage for summer months. Additionally, gas cost rates are set as of August and not adjusted quarterly with market changes. The Target actively monitors its budget billing from December to May and reduces flat rates to wind down credit balances. We observed that over the past two years, budget bill customers over paid by $632k in FY15 and $130k in FY16. Overpayments are reflected as credits to AR and Client should consider further diligence to determine if a liability should be recorded to represent a refund to these customers.

Capitalized Overhead

- The Target has historically capitalized a portion of general and administrative (“G&A”) and benefits related to overheads into capital projects. Employee time reports track time spent on construction projects via different pay types set up in its systems. In both FY15 and FY16, the company capitalized approximately 32% of its administrative time to capital projects, or $3.1m. Management indicated that this level is consistent year over year, noting that the 2010 rate case assumed $3.3m.
- The amount of fringe capitalized is calculated by taking the total applicable field hours in all departments excluding cashiers and administration and dividing total field benefits and payroll by total applicable field hours. This hourly rate is multiplied by total non operating and maintenance hours to calculate the capitalized portion. In both FY15 and FY16, the company capitalized approximately 21% of its benefits and payroll taxes to capital projects. Costs included are Employee Benefits, workers comp, gen liability, excess liability, vacation and sickness.

Bonus Expense

- The Target’s incentive compensation program is tied to meeting earnings per share targets. Annually, the results of the fiscal year are evaluated by the CEO and the Board of Directors to determine the amount of bonuses, if any, should be paid to the officers and employees. In FY15, the Target accrued bonuses of $254k and share-based compensation expense of $1.1m. In FY16 it accrued $0 in bonuses and $453k in share-based compensation.

Finance and Accounting Function

- The Target’s finance and accounting function is located in a single location which includes John Brown (CFO) as well as seven other individuals with each performing a full departmental role (e.g. payroll, property, gas cost accounting, and general ledger consolidations.) Management indicated the average tenure for its employees is 15+ years, with minimal turnover, and there no current severance packages.
- The Target’s close process begins two weeks after the end of the previous month (i.e. January 14, 2017 for a December 31, 2016 close). The close process takes, on average, two to three weeks. The two week delay in closing helps to ensure all billings are captured and month-end numbers are based on actuals rather than estimates.
- Consideration should be given to any changes necessary to meet the Client’s reporting deadlines.

Gas in Storage

- The Target operates an underground natural gas storage field in Bell County, Kentucky. During the non-heating season, the Target injects and stores natural gas and during the heating season, it withdraws the gas for delivery to its regulated distribution customers and its non-regulated customers. The field's peak capacity is 5 billion cubic feet of natural gas. The Target maintains perpetual inventory records, including a master meter of injections and withdraws. The storage field is tested annually by measurement personnel to monitor pressures and potential leaks. The Target's exposure to risks of lost gas or changes in prices between the time of injection and withdraw are largely mitigated by their ability to pass on imbalances and gas costs to their regulated customers. For non-regulated injections and storage, the Company maintains a separate lower of cost or market analysis to monitor the need for potential adjustments in value comparing the WACOG established by injections to their current market price on committed purchases. No adjustments were required in FY15 and FY16.

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Client should consider the potential change in customer rates, recovery mechanisms, or other facets of the business due to acquisition accounting.

Other Quality of Earnings Considerations

Acquisition Accounting

A regulated utility is generally required to seek approval for a business combination from its regulator. When a regulator approves a business combination involving a regulated utility, it may result in changes to customer rates, recovery mechanisms, or other facets of the regulatory relationship. Client should consider potential impacts, such as those imposed on Target upon acquisition. Specific areas of consideration with regard to acquisition accounting are outlined below.

- **Inventory**: The Target's inventories consist primarily of stored natural gas, materials and supplies. As natural gas is recovered from customers, it is possible that book value will be assumed equal to fair value as regulatory commissions may not allow the step up to be recovered in rates and decreases in value will also likely be recovered in rates. Alternatively, such amounts may be reported at their fair value with an offsetting regulatory asset or liability. Material and supplies inventories should be evaluated for possible scenarios where the net realizable value is greater than cost and potentially adjusted to fair value, with consideration to whether historical costs will be recoverable in future rates.
- **Property, Plant and Equipment ("PP&E")**: For PP&E related to rate regulated operations, fair value is typically assumed to equal carrying value based on assumptions made about current returns from the regulatory process taking precedent over other fair value assessments.
- **Regulatory Assets and Liabilities:** Assets and liabilities attributable to the rate regulated operations may receive a regulatory offset if the fair value adjustment is expected to be recovered/mitigated through future rates. Pre-existing regulatory assets that are earning higher or lower returns than market participants require for similar assets and liabilities should be adjusted (i.e., a market participant's required return may differ from the current allowed rate of return).
- **Operating leases**: Current operating leases need to be assessed to determine if they are at fair market value.
- **Debt:** Debt will be recorded at acquisition-date fair-value incorporating the reporting entity's credit and market conditions. It is common for rate-regulated entities to recorded an offsetting regulatory balance against the FV step up on debt. Non-regulated and corporate level debt would not have a regulatory offset.

Acquisition Accounting, continued

- **Pension and other postretirement employment benefits**: An acquirer recognizes an asset or liability on acquisition date for the funded status of plans assumed in the acquisition ($1.9m underfunded as of Jun-16). When measuring the funded status of these plans, the acquirer excludes the effects of expected amendments, curtailments, or terminations that the acquirer has no obligation to make in connection with the business combination. However, the measurement of the projected benefit obligation or accumulated postretirement benefit obligation and the fair value of the plan assets on the acquisition date should reflect any other necessary changes in discount rates or other assumptions based on the acquirer's assessment of relevant future events. As a result, acquiree balances for unrecognized prior service costs, actuarial gains or losses or any remaining transition obligations (i.e. accumulated other comprehensive income), which are typically recorded in accumulated OCI, should not be carried forward on the acquisition date.) For the regulated operations, the acquirer may be allowed to record offsetting regulatory balances, noting that future rates will likely be based on pension expense as if the transaction did not occur.
- The Target has a regulatory asset related to unrecovered pension costs ($10.9m as of Jun-16), which will also need to be assessed in connection with acquisition accounting. As noted above future pension expense for regulatory rates will likely be computed on a pre-acquisition basis, thus potentially making this asset still recoverable. However, an assessment will be required and could also result in a conclusion that the asset should be valued at zero, which would result in a change to future earnings as compared to historical given the loss of the amortization of this asset.

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Operating net working capital has averaged $7.5m over the last four quarters.

Preliminary Net Working Capital

Adjusted operating net working capital ("NWC"), presented below, is adjusted for non-operating items such as cash and cash equivalents, current portion of long-term debt, accrued interest, and deferred income taxes. Due to our limited scope of services, we have not performed comprehensive diligence procedures on the Target's working capital nor have we identified potential normalizing working capital adjustments. These schedules are for informational purposes only and should not be relied upon in the Client's model. Management has not presented their view on a normalized working capital, nor did we assess such in connection with our scope.

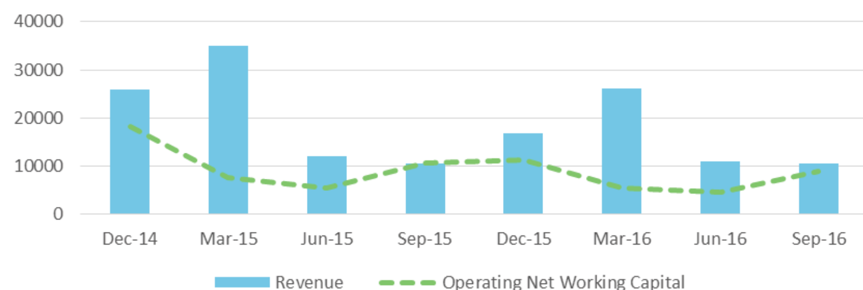
Operating Net Working Capital

US$000s	Sep-14	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	LTM Avg.
Accounts receivable, net	5,556	14,177	12,603	5,761	5,543	8,774	9,060	4,742	5,485	7,015
Natural gas in storage, at average cost	10,837	9,522	1,758	4,634	7,202	6,004	468	3,290	5,731	3,873
Deferred natural gas costs	1,875	1,478	-	-	887	1,097	367	674	1,745	971
Materials and supplies, at average cost	593	467	494	544	516	482	521	544	552	525
Prepayments	4,347	3,541	2,247	3,347	4,498	3,400	2,205	3,052	4,369	3,257
Current Assets	23,207	29,184	17,863	14,285	18,646	19,758	12,621	12,302	17,883	15,641
Accounts payable	6,183	7,030	4,881	5,426	4,535	4,422	3,654	4,200	4,917	4,298
Accrued taxes	1,880	1,760	1,727	1,472	1,550	2,198	1,473	1,585	2,061	1,829
Customers' deposits	582	740	740	601	590	724	725	618	596	666
Accrued vacation	758	629	705	749	781	655	727	756	770	727
Other current liabilities	617	460	523	610	571	539	593	585	690	602
Current Liabilities	10,472	10,904	10,219	8,860	8,026	8,538	7,171	7,745	9,035	8,122
Operating Net Working Capital	**12,735**	**18,280**	**7,644**	**5,426**	**10,620**	**11,220**	**5,450**	**4,557**	**8,848**	**7,519**
Cash and equivalents	6,861	1,163	16,102	16,924	10,459	8,985	18,408	18,607	12,267	14,567

Source: Company filings, Deloitte analysis

Capex in Payables

The Target may have certain capital expenditures recorded in accounts payable or accrued liabilities. To the extent these are included, we would remove them from working capital as these costs are one-time in nature and do not reflect the recurring operations of the business and will ultimately be funded from draws on long term debt. Further diligence is required to quantify such costs.



Cash and equivalents

While cash and equivalents are excluded from Operating NWC, consideration should be given to the fact that it appears that the Target has maintained more cash than required to meet the immediate operating needs of the business. This presents an opportunity for improvement post transaction.

Working Capital Peak

The Target's net working capital needs increase during the September to March of each year due to build of inventory and then AR related to the winter heating season. During the warmer, non-heating months, cash needed for operations and construction may be met through short-term borrowings. Client should consider the impact on working capital requirements during these months.

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The Target had $39.8m in reported net debt as of Sep-16.

Preliminary Net Debt

Presented in the table below is a summary of net debt and debt-like items as of Sep-16, obtained from management information and inquiry with Target Management. Due to our limited scope of services, we have not performed comprehensive diligence procedures on the Target's debt and debt-like items. Client should consider the following potential debt-like items when evaluating the overall purchase price of the Proposed Transaction.

Preliminary Net Debt

US$000s	Sep-16
Cash and cash equivalents	(12,267)
Current portion of long-term debt	1,500
Long-Term Debt	50,424
Accrued interest	110
Reported Net Debt	**39,768**
Potential debt and debt-like items	
1 Change in control	14,800
2 Asset retirement obligations	3,986
3 Transaction-related costs	2,200
4 Accrued Pension	1,162
5 Retention agreements	
Total potential debt and debt-like items	**22,147**
Adjusted Net Debt	**61,915**

Potential debt or debt-like items

1. **Change in control:** lient should consult with your legal advisors regarding any potential change in control exposure and the impact change in control payments will have on the overall purchase price of the Proposed Transaction.
2. **Asset retirement obligations:** At Sep-16, Target's total ARO balance was $4m. US GAAP requires companies to record the fair value of legal ARO's related to acquisition, construction, and normal operation of long-lived assets. The Target's asset retirement obligations relate primarily to natural gas well plugging, abandonment costs, and the retirement of service lines and mains. For asset retirement obligations related to regulated operations, accretion of the liability and depreciation of the asset retirement costs are recorded as regulatory assets and Target recovers the cost of removing regulated assets through depreciation rates. Accounting for asset retirement obligations typically has no cash impact until the period in which retirement occurs. Client should consider any potential impacts of future cash outflows/obligations related to asset retirement obligations. Additional retirement liabilities appear to exist off-balance sheet related to the Target's storage facilities, which Management has deemed to have indeterminate useful lives and has not recorded any AROs.
3. **Transaction-related costs:** The Target has a potential $2.2m payout due to TPH at the close of the Proposed Transaction, contingent upon a successful sale. Client should consider the impact transaction-related payments will have on the overall purchase price of the Proposed Transaction as such amounts are debt-like in nature.
4. **Accrued pension** – The Target had approximately $1.2m in pension expenses accrued at Sep-16. To the extent this is a net liability at the close of the Proposed Transaction, Client should consider these as debt-like in the SPA.
5. **Retention Agreements** – Management indicated it does not currently have retention agreements or bonuses for certain employees in leadership roles (i.e. vice presidents, directors, key accounting and finance personnel, district managers, and supervisors). To the extent any retention agreements or bonuses are agreed upon and accrued for prior to the close of the Proposed Transaction, these should be considered as debt-like and Client should consider the impact transaction-related payments will have on the overall purchase price of the Proposed Transaction.

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Scope of Services

Scope of Services - Accounting

General Procedures

- Read the audited financial statements of the Target and the Confidential Information Memorandum, to the extent available.
- Obtained and read monthly management reports for analysis of trends, non-recurring and unusual activity, to the extent available.
- Advised Client on key accounting considerations in connection with the Proposed Transaction
- Prepared questions in advance of Target management meetings and participate in meetings with Target management or advisors:
  - Inquired about significant accounting policies, with a focus on revenue recognition, regulatory accounting, cost capitalization, contingent obligations, deferred tax accounting, and differences between Client's and Target's accounting policies

Independent Auditors

- Read audit working papers for the last two fiscal years and met with audit team to discuss key findings and issues. Read Audit Committee minutes and presentations to audit committee on significant findings and deficiencies in internal controls and remediation efforts, to the extent made available.
- Read management letters for the two most recent audits; inquired of the Target's independent auditors as to matters identified for inclusion for the current year and the status of corrective actions taken by management.

Quality of Earnings

- Analyzed trends in revenues, operating expenses and EBITDA with a focus on:
  - Regulatory rates, surcharges, related process, and impacts on earnings
  - Non-recurring, non-cash, out-of-period, or other potential adjustments
  - Hedging of commodity risk and use of other derivatives
  - Other quality of earnings considerations

Quality of Earnings

- In general, inquired about:
  - Reconciliation between the audited and the internal financial statements;
  - Significant accounting policies, with a focus on revenue recognition, cost capitalization, derivatives, regulatory accounting, etc.;
  - Changes in accounting or reporting practices or procedures that could affect comparability or trends in earnings or cash flows;
  - Significant inter-company and intra-company transactions, including corporate overhead allocations
  - Nature of relationships and transactions with related parties
  - Variances and trends in revenues, expenses, profitability, and key operating metrics (i.e. pricing, volumes, and mix by line of business (regulatory vs. non-regulated) and customers)
  - Pension expense run rate, specifically inquiring as to the basis and rationale for 2017 estimated pension expense as compared with 2016 recorded pension expense which Target management indicated was expected to increase
  - Unusual fluctuations in monthly amounts, seasonality of revenue and EBITDA, discretionary or temporary reductions or deferrals of certain expenses, significant non-recurring, unusual or out-of-period charges and credits, incremental operating costs expected to result from the Proposed Transaction such as the impact of changes in vendor contractual arrangements, etc.

Working Capital

- Performed a high-level trend analysis on quarterly working capital trends with a focus on elements directly attributable to operations, which was limited primarily to publicly available information.

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Scope of Services

Scope of Services - Tax

- Read and analyzed US federal and state income/franchise tax returns and supporting working papers made available with a primary focus on:
  - Potentially significant tax exposures, including positions on tax returns for which there may be significant exposures;
  - Material tax attributes of the Target, including net operating loss carryforwards, tax credits, and potential limitations on future utilization;
  - Tax accounting methods, particularly differences between book and tax accounting methods
  - Tax credits
- Read income tax provision working papers with a primary focus on:
  - Significant permanent and temporary differences;
  - The treatment of temporary differences as normalized or flow-through with respect to federal and state deferred taxes;
  - ASC 740-10 (f/k/a FIN 48) and ASC 450 (f/k/a FAS 5) tax contingency reserves and supporting materials;
  - Specific tax-related regulatory assets and liabilities, including recovery/amortization periods and computation of tax gross-ups;
  - Tax working papers filed with or prepared in conjunction with the most recent rate case in each jurisdiction;
  - Effective tax rates and cash taxes.
- Inquired of the Target's internal and independent tax advisors about:
  - Legal entity structure of Target and tax classification of applicable entities;
  - Status of any pending examinations and results of prior examinations by tax authorities;
  - Tax rulings, changes in accounting methods, or closing agreements entered into by the Target;
  - Opinion letters, correspondence and memorandum or studies prepared by Target, any subsidiary, or its representatives regarding significant tax exposure items, if any;
  - Tax accounting methods including capitalization and environmental matters;
  - Unrecognized tax benefits, including tax contingency reserves;
- Inquired of the Target's internal and independent tax advisors about (cont.):
  - Changes in the Target structure including any merger, acquisition, divestiture, joint venture or restructuring;
  - Significant tax elections;
  - Significant tax planning initiatives entered into (or contemplated) by the Target, including status of implementation of the tangible property regulations and safe harbor unit-of-property guidance relevant to the utility industry ;
  - Tax risks and contingencies assumed including any consolidated federal income tax liabilities;
  - Other regulatory tax considerations including:
    - Regulated assets and liabilities related to income taxes
    - Normalization and flow-through accounting
    - Tax Riders or similar agreements
    - Historical normalization practices
    - Impact of taxes on rate making
    - Regulated utility or regulated asset acquisitions or dispositions
    - Tax portions of relevant rate orders and significant tax testimony for most recent rate case, as applicable
  - Tax credit positions;
  - Target's current state income /franchise and non-income tax filings and positions;
  - Risk of consolidated tax adjustment issues at state commissions due to the Target's structure;
  - Internal tax department operations including tax compliance functions;
  - Policies and procedures related to utility, franchise, property, payroll, sales and use, information reporting, and other non-income taxes;
  - Use of independent contractors;
  - Tax holidays or incentives in relevant tax jurisdictions;
  - Transfer taxes

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Scope Exclusions and Limitations

Scope Exclusions

Although not intended to be an all-inclusive list, the following services were specifically excluded from our engagement at Client's request, or included in a separate communication:

- Detailed net working capital and net debt analyses
- Evaluation of internal accounting or disclosure controls
- Review of business operations
- Assessment of commercial merits of Proposed Transaction
- Commercial or operational due diligence
- Integration assistance
- Evaluation of management information systems
- Evaluation of employee benefits or other human resource matters
- Evaluation of risk management practices (including insurance, trading and commodity activities, or security)
- Background investigations
- Foreign Corrupt Practices Act or other anti-bribery services
- Environmental assessment
- Certification of physical inventory observations
- Legal or regulatory services
- Internal accounting and disclosure controls

Scope Limitations

As of the date of this written communication, an audit of the Target's financial statements, as of any date subsequent and year end reporting period to June 30, 2016 has not been completed. Accordingly, any financial information for 2017 interim periods contained herein is subject to adjustment as a result of the completion of any audit.

We generally did not duplicate the matters that would be addressed by Client, Client's legal counsel, or other professionals engaged to assist Client with its due diligence. Our observations to date may be subject to change based upon the following: (1) obtaining certain information from management of the Target and/or unresolved matters as we have highlighted throughout this written communication, (2) obtaining access to the completed due diligence results of Client's legal and other professional advisors, and (3) obtaining access to certain individual members of the Target's management.

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Matters for Follow Up

Matters for Follow Up

Items that are not yet complete or have not been provided are summarized below:

Accounting

- Description of significant forecast changes to O&M and capital over the next 5 years, including planned staffing reductions, capital programs, facility closures, outsourcing plans, etc.
- Client should consider requesting copies of the Target's formal cost allocation manual and policies.
- Client should request details on unrecorded obligations, commitments and contingencies to consider in the Proposed Transaction as an offset against the purchase price.
- Client should consider further diligence to determine if a liability should be recorded to represent a refund to budget billed customers who have overpaid due to falling gas prices during FY15 and FY16.

Tax

- Copies of both the FY2013 and FY2016 (when completed) federal and state income tax returns

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Certain Terms of Engagement

Consultative Engagement

The Services were performed in accordance with the *Statement on Standards for Consulting Services* established by the American Institute of Certified Public Accountants (AICPA). The Services do not constitute an audit conducted in accordance with generally accepted auditing standards, an examination of or any other form of assurance with respect to internal controls, or other attestation or review services in accordance with standards or rules established by the AICPA, the Public Company Accounting Oversight Board (PCAOB), or other regulatory body.

Client Responsibilities

Client is responsible for obtaining all necessary authorizations and consents from the Target, its advisors, and its accountants, in order to permit us to perform the Services, including, without limitation, disclosure of the Target's confidential information to us in connection with the Proposed Transaction.

The Services may include advice and recommendations, but Client is responsible for making any decisions in connection with the implementation of such advice and recommendations. Furthermore, Client shall be solely responsible for, among other things: (i) making all management decisions, performing all management functions, and assuming all management responsibilities; (ii) designating a competent management member to oversee the Services; (iii) evaluating the adequacy and results of the Services; (iv) accepting responsibility for results of the Services; and (v) establishing and maintaining internal controls, including, without limitation, monitoring ongoing activities. In connection with the Services, we shall be entitled to rely on all decisions and approvals of Client.

Limitations of the Services

The Services are limited in nature and do not comprehend all matters relating to the Target that might be pertinent or necessary to the evaluation of the Proposed Transaction. Accordingly, the Services should not be taken to supplant other inquiries and procedures that an investor or any third party should undertake for the purpose described above. We have no responsibility for the sufficiency of the Services and make no representation as to the sufficiency of the Services for any purpose.

Neither we nor this written communication will express an opinion or any other form of assurance with respect to any matters as a result of the performance of the Services, including, without limitation, concerning (i) the financial statements of any entity or any financial or other information, or operating or internal controls of any entity, taken as a whole, for any date or period; (ii) the merits of any transaction, including, without limitation, the consideration to be paid; (iii) the future operations of any entity; (iv) the fairness of the contemplated terms of any transaction; or (v) any forward looking information (including, but not limited to, any models, projections, forecasts, budgets, synergies, feasibility analyses, assumptions, estimates, methodologies, or bases for support) or the feasibility or achievability of such forward-looking information.

In the performance of the Services, we did not perform any evaluation of internal controls and procedures for financial reporting upon which Client's management can base its assertions in connection with the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley") or related rules or regulations. We will make no representations or warranties and will provide no assurances that any entity's disclosure controls and procedures are compliant with the certification requirements of, or any entity's internal controls and procedures for financial reporting are effective as required by, Sarbanes-Oxley or any other standards, rules, or regulations, including, without limitation, Sections 302 and 404 of Sarbanes-Oxley.

The Target's financial statements, including, without limitation, the application of generally accepted accounting principles ("GAAP") to record the effects of the Proposed Transaction, are the responsibility of management of the Target. Accordingly, any comments made by us relating to the accounting or tax treatment of selected balances or transactions or the application of GAAP or the technical merits of the tax positions and planning strategies related to the Target or the Proposed Transaction as a whole are intended to serve only as general guidance to assist Client to better understand certain accounting or tax matters related to the Target and the potential effects of the Proposed Transaction. Such comments are necessarily based on our preliminary understanding of the pertinent facts and circumstances and on current authoritative literature, and are, therefore, subject to change. Such comments do not constitute the rendering of a tax opinion or a report on the application of accounting principles in accordance with standards or rules established by the AICPA, the PCAOB, or other regulatory body.

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Certain Terms of Engagement

The performance of the Services does not constitute (i) a recommendation regarding any transaction, including, without limitation, the acquisition or financing of any business, assets, liabilities, or securities; (ii) a market or financial feasibility study; (iii) a fairness or solvency opinion; or (iv) an examination or compilation of, or the performance of agreed upon procedures with respect to prospective financial information in accordance with standards or rules established by the AICPA, the PCAOB, or other regulatory body. The Services and this written communication are not intended to be, and shall not be construed to be, "investment advice" within the meaning of the Investment Advisers Act of 1940.

It is understood that we are not providing, nor will we be responsible for providing, legal advice. In addition, any forward-looking information is the responsibility of applicable management. In this regard, applicable management is responsible for representations about its plans and expectations and for disclosure of significant information that might affect the ultimate realization of such forward-looking information, and we have no responsibility therefor.

The performance of the Services is heavily dependent upon (i) Client's timely decisions and approvals in connection with the Services, and (ii) being provided timely access to accurate and complete versions of relevant materials and information, including, without limitation, materials and information requested, and complete and accurate answers to questions. We have no responsibility for the accuracy or completeness of the information provided by, or on behalf of, Client or the Target. We have not been engaged to detect errors or fraud and this written communication may not disclose errors or fraud should they exist.

Other Relationships

One or more of the member firms of Deloitte Touche Tohmatsu Limited, including, without limitation, Consultant, or any of its affiliates or related entities, may be engaged to provide audit, tax, consulting, or other services (including, without limitation, services in connection with the Proposed Transaction and related financing arrangements) to, and may have other business relationships with, Client, the Target, parties other than Client considering a transaction involving Target, or their respective affiliates. We have no responsibility to Client (1) relating to such services or other relationships in connection with the Proposed Transaction, or (2) to use or disclose any information, including, without limitation, the identity of such other parties, that we possess by reason of such services or other relationships.

Exemption Relating to PCAOB Rule 3522 of PCAOB Release 2005-14 and Tax Shelter Regulations under the U.S. Internal Revenue Code Sections 6011 and 6111

We acknowledge that we have not placed any limitations on Client's disclosure of the tax treatment or tax structure associated with the tax Services or transactions described in this written communication. Nothing herein shall be construed as limiting or restricting disclosure of the tax treatment or tax structure of the transaction as described in Rule 3501(c)(i) of PCAOB Release 2005-014 or Internal Revenue Code ("IRC") sections 6011 and 6111 and related Internal Revenue Service ("IRS") guidance. Client acknowledges that none of its other advisors have imposed or will impose any conditions of confidentiality with respect to the tax treatment or tax structure associated with the tax Services or transactions described herein. The Services are solely for Client's informational purposes and internal use, and this engagement does not create privity between us and any person or party other than Client ("third party"). Our engagement is not intended for the express or implied benefit of any third party. Unless otherwise agreed to in writing by us, no third party is entitled to rely, in any manner or for any purpose, on this written communication.

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Supplemental Schedule: Rate Schedule

Rate Base Mechanisms

The following represents the Target's regulatory rates at Jun-16 and example rate base calculations based on the 2010 rate case. The below is presented for informational purposes only.

Regulatory Rate Base Mechanisms

Type	Effective Dates	Residential	Small Non-Residential	Large Non-Residential	Interruptible
Customer Charge	7/27/2016	$ 20.90	$ 31.20	$ 131.00	$ 250.00
Base Rate	7/27/2016	$ 4.32	$ 4.32	*see table below*	*see table below*
PRP	7/27/2016	$ 2.21	$ 4.19	$ 31.97	$ 229.44
GCR	7/27/2016	$ 0.58	$ 0.58	$ 0.58	$ 0.58
CEPRC	7/27/2016	$ 0.015	n/a	n/a	n/a

Large Non-Residential

	Base Rate
1 - 200	$ 4.32
201-1000	$ 2.67
1001-5000	$ 1.87
5001-10000	$ 1.47
over 10000	$ 1.27

Interruptible

	Base Rate
1-1000	$ 1.60
1000-5000	$ 1.20
5000-10000	$ 0.80
over 10000	$ 0.60

Source: Approved Tariff Sheet KYPSC

Rate Base Calculation

US$000s	Rate Case	FY14 (1)	FY15 (1)	FY16 (1)
Total utility plant in service	194,819	226,771	234,183	239,227
Add				
Materials and supplies	596	575	544	544
Prepayments	1,631	3,491	3,347	3,052
Gas in storage	7,986	7,126	4,634	3,290
Unamortized debt expense (2)	4,542	90	84	78
Cash working capital allowance	1,599	1,599	1,599	1,599
Subtotal	16,355	12,881	10,208	8,563
Deduct				
Accumulated depreciation	71,888	93,552	98,741	104,193
Customer advances for construction	55	55	55	55
Accumulated deferred income taxes	29,427	40,578	42,130	43,405
Subtotal	101,370	134,184	140,926	147,653
Rate Base	**109,805**	**105,468**	**103,465**	**100,137**

Source: Management information

(1) Rate base for FY14- FY16 has been assumed on a consistent basis as the 2010 rate case, however, the am are presented for informational purposes only. Actual rate base calculations are subject to the purview of the KYPSC and may vary in the next rate case. Items in brackets were not available in public documents and have been estimated.

(2) Unamortized debt expense was reduced significantly due to debt refinancing. A non-regulated entity would recognize the losses immediately, however, ASC 980 allows amortization over a future period. In this case, the KYPSC ordered the Company to amortize unamortized costs over the life of the new Series A Notes. In a future rate case, it is possible that the KYPSC would include the regulated asset of $2.7m as of Jun-16 but we have nc included in the above.

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Supplemental Schedule: Information Technology Systems

Information Technology Systems

The following represents the Target's information technology systems, vendors, and the current operating system for each as of June 30, 2016. Information herein was obtained from the Target's audit working papers.

Information Technology Systems

System Type	System Application	Vendor	Operating System
Revenue, customer info, billing	E-CIS Billing Systems	Vertex	OS/400
Check printing	Formserver 400	Digital Design	OS/400
Financial reporting	Harris	Harris	OS/400
Fixed assets, work orders	PowerPlant	PowerPlan	Windows 2008
Accounts receivable- regulated	MV-RS	iTron	Windows 7
Accounts payable	Pinnacle	Knowledgelake	Windows 2008
Gas in storage	ClowCal	CoastalFlow	Windows 2008
AR- nonregulated	Allegro	Allegro	Windows 2008
Unbilled revenue	Cognos	IBM	Windows 2008

Source: Audit Workpapers

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Supplemental Schedule: Projected Pension Expense

Projected Pension Expense

The table below details historical U.S. GAAP NPPC and cash contributions, and the projected FYE17 balance sheet and FY18 NPPC. The key assumptions highlighted below were used for the projections:

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Discount Rate: The Company selects the discount rate of 3.50% as of Jun-16 based on a review of high quality corporate bond yields with maturities approximating the remaining life of the projected benefit obligations. The selected discount rate does not appear unreasonable given the plan benefit design and population. The 4.0% discount rate estimate as of Jun-17 is based on the movement in the Citigroup Pension Liability Index between Jun-16 and Dec-16.

Long-Term Rate of Return on Plan Assets: The current asset allocation is approximately 65% equity, 25% fixed income, and 10% real estate. The Company has elected to use a 5.50% long-term rate of return on assets for FY16. The selected long-term rate of return is below the low-end of the range of reasonable assumptions by approximately 100 basis points (which provides a higher expense). The Company indicated that they are beginning to move towards a more conservative liability driven investment approach as a justification for using a lower expected return. Assuming that the Company continues this shift towards a conservative liability driven approach, this long-term assumption is reasonable. Otherwise, the expected return on assets assumptions should be increased. Note that an increase of 50 basis points in the assumptions results in approx. $150k decrease in NPPC.

Cash Contributions: Management indicated that it judgementally determines the level of cash contributions each year but typically plans $0.5m per year. Amounts shown at right were taken from the Target's public disclosures in the Form 10k. However, Management indicated that it contributed an additional $1m shortly after the fiscal year ended Jun 30, 2016. We have not confirmed this amount as it is not disclosed publicly. Client should consider that this amount has not been reflected in the contributions at right.

Overview of Defined Benefit Obligations and P&L Costs

US$millions	Actual		Estimate [3]
	Jun-15	Jun-16	Jun-17
Funded Status			
Project Benefit Obligation	$ 28.8	$ 31.6	$ 28.6
Market Value of Assets	31.0	29.7	28.8
Funded Status, (Deficit)/Surplus	$ 2.2	$ (1.9)	$ 0.2
Regulatory Assets			
Prior Service Cost	$ (0.2)	$ (0.1)	$ (0.1)
Accumulated Net Losses	7.4	11.0	8.0
Regulatory Assets	$ 7.2	$ 10.9	$ 7.9
Discount Rate[2]	4.25%	3.50%	4.00%

US$millions	FY15	FY16	FY17	FY18 [3] w/o Pur. Acctg.	FY18 [3] w/ Pur. Acctg.
Net Periodic Pension Cost (NPPC)					
Service Cost	$ 1.0	$ 1.0	$ 1.0	$ 1.0	$ 1.0
Interest Cost	1.1	1.1	1.1	1.1	1.1
Expected Return on Plan Assets	(1.7)	(1.6)	(1.6)	(1.5)	(1.5)
Amortization of Prior Service Cost	(0.1)	(0.1)	(0.1)	(0.1)	-
Amortization of Unrecognized Net Los:	0.2	0.4	0.9	0.5	-
Total	$ 0.5	$ 0.8	$ 1.3	$ 1.0	$ 0.6
Cash Contributions	$ 1.0	$ 0.5	$ 0.5	$ 0.5	$ 0.5
Key Assumptions - P&L					
Discount Rate [2]	4.25%	4.25%	3.50%	4.00%	4.00%
Long-Term Rate of Return	6.00%	5.50%	5.50%	5.50%	5.50%

Source: Company 10-K as of June 30, 2016; Company audit workpapers

Notes:

(1) Assumes purchase occurs in Jun-17.

(2) Discount rate as of June 30, 2017 is estimated based on the movement in the Citigroup Pension Liability Index from June 30, 2015 to December 31, 2016.

(3) Assumes discount rate of 4.0% and no additional gains or losses during FY17.

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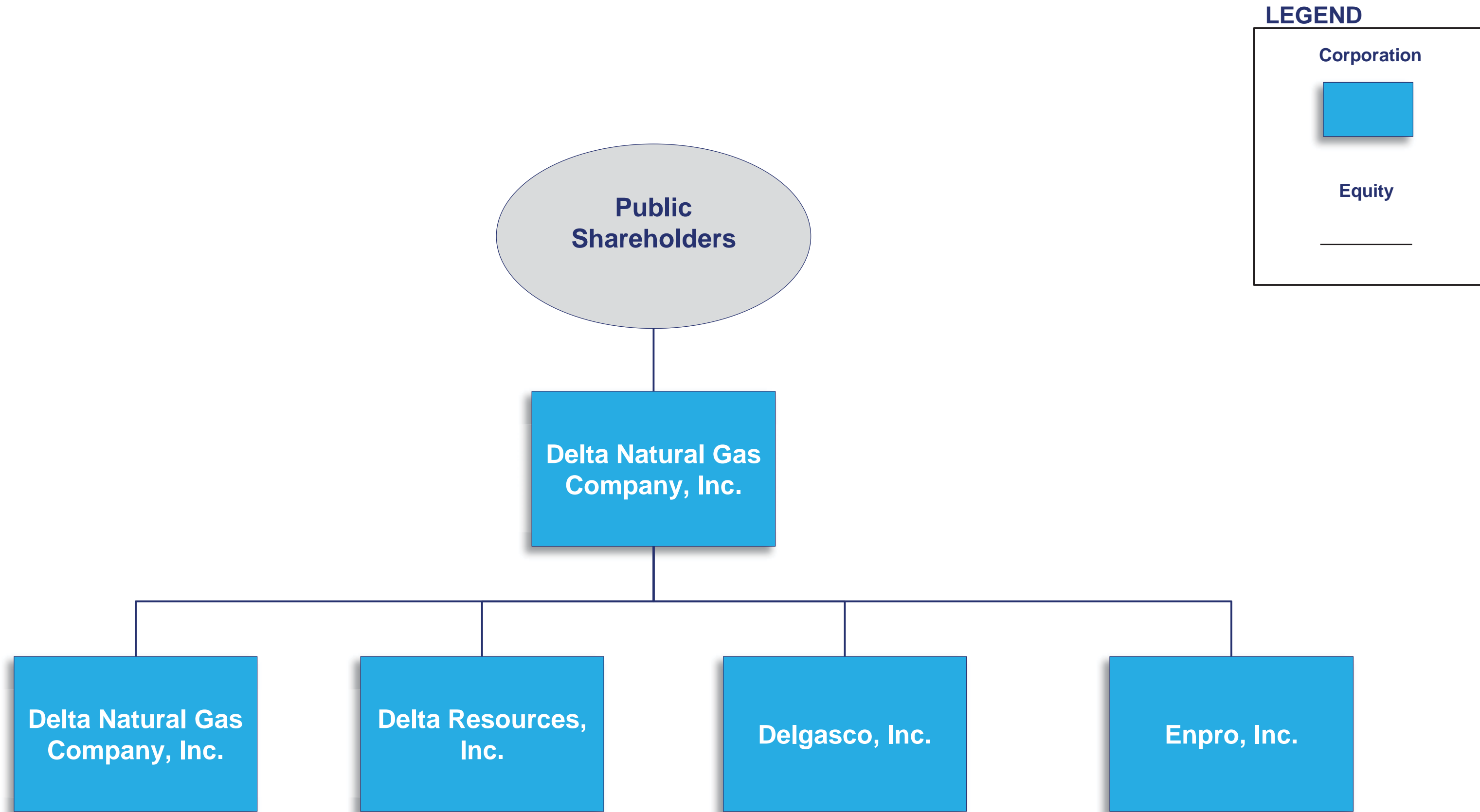
Supplemental Schedule: Current Target Structure



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Supplemental Schedule: Book Income to Taxable Income Reconciliation

U.S. Federal Taxable Income Reconciliation

US$ 000	*FY2014	*FY2015
Drake		
Book Income	**8,275**	**6,496**
Tax Adjustments		
Corporate Owned Life Insurance	(59)	(10)
Current Income Tax	4,523	1,915
Deferred Income Tax	(438)	1,454
Gain/Lass on Asset Disposition	250	161
Interest Expense	240	233
Pension and Profit Sharing	(1,011)	(7)
Meals and Entertainment	18	16
Bad Debt Expense	109	(4)
Depreciation	(2,372)	(1,372)
Other Section 263A costs	65	(41)
Purchases	3,120	726
IRC 162	(2,322)	91
Repairs and Maintenance	-	(1,413)
Other Income Items	(111)	(1,102)
Other Expense/Deduction Items	344	191
Total Adjustments	**2,356**	**838**
Federal Taxable Income	**10,631**	**7,334**

Source: Target tax returns.

*Target files federal income tax returns based on a fiscal year of July 1 through June 30.

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Supplemental Schedule: Rollout of Tax Depreciation Deductions

U.S. Federal Taxable Income Reconciliation

US$ 000	Tax Depreciation Deduction Rollout
2017	3,912
2018	3,350
2019	3,197
2020	2,525
2021	2,079
2022	1,572
2023	1,284
2024	1,054
2025	851
2026	818
2027	722
2028	523
2029	394
2030	266
2031	163
2032	123
2033	101
2034	75
2035	46
2036	14
Total Deductions:	23,069

Source: Target tax returns.

*Target also has tax basis in non-depreciable assets of $3.8m.

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Abbreviations

AICPA	American Institute of Certified Public Accountants
ARO	Asset Retirement Obligations
CAPEX	Capital Expenditure
CEO	Chief Executive Officer
CFO	Chief Financial Officer
Client	PNG Companies, LLC.
CEP	Conservation / Efficiency Program
Consultant	Deloitte & Touche LLP
EBITDA	Earnings Before Interest, Tax, Depreciation and Amortization
FASB	Financial Accounting Standards Board
G&A	General & Administrative
GAAP	Generally Accepted Accounting Principles
GCR	Gas Cost Rider
K	Thousands
KYPSC	Kentucky Public Service Commission
L12M or LTM	Last Twelve Months Ended
M	Millions
NWC	Net Working Capital
O&M	Operating And Maintenance
PCAOB	Public Company Accounting Oversight Board
PRP	Pipe Replacement Rider
ROE	Return on Equity
TPH	Tudor, Pickering, Holt & Co.
WNA	Weather Normalization Rider

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LDC Funding, LLC

Project Drake

Draft Insurance Due Diligence Report

January 23, 2017

Prepared By:
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McGRIFF, SEIBELS & WILLIAMS, INC.

Disclaimer

McGriff, Seibels & Williams, Inc. ("MSW") prepared this report from materials furnished by Steel River Partners/LDC Funding LLC, referred to hereafter as "LDC". MSW has not assumed responsibility for independent verification of any information referenced in this report. MSW assumes the accuracy of what was presented without independent verification by MSW. Any opinions, advice, statements, services, offers or other information expressed or made available by third parties, including information sources, users or others, are those of the respective author(s) and do not necessarily state or reflect those of MSW.

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LDC acknowledges and agrees that in no event shall MSW or any of MSW's officers, directors, employees, shareholders, agents, or representatives be liable to LDC, any of its affiliates, or any other party for any special, indirect, incidental, exemplary, or consequential damages or loss of goodwill in any way arising from or relating to the services provided herein. In no event shall MSW's liability for any damages to LDC, any of its affiliates, or to any third party ever exceed the amount of fees paid by LDC to MSW pursuant to the Statement of Services or Invoice to which the claim relates.

Respectfully,

McGriff, Seibels & Williams, Inc.

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SECTION I – EXECUTIVE SUMMARY

Introduction:

McGriff, Seibels & Williams, Inc. is pleased to present our insurance due diligence report concerning the purchase of Delta Natural Gas, hereafter referred to as "Delta". This report is provided to LDC Funding, LLC (LDC) for the purpose of assessing both current and historical risk management/transfer programs and address areas of operational risk and/or insurance coverage which may have been overlooked or require further analysis and make recommendations accordingly. We have based our findings on information received from LDC.

In the following pages, we outline the key findings, recommendations and coverage overviews for your review. We look forward to discussing this report in further detail and receiving your valuable commentary.

Data Sources:

- Information made available via IntraLinks data site
- Conference calls with representatives from LDC

1. Key Recommendations (Pre-Close)

A. Since closing is to occur after March 9, 2017, secure evidence of extensions or renewal on all in force insurance policies

B. D&O and Fiduciary Run-off Coverage – Within the purchase/sale agreement, include requirements for six (6) year extended reporting periods (Run-off) to be purchased prior to closing for the Directors & Officers Liability insurance (D&O) and Fiduciary Liability insurance programs. Specify that the extended reporting period endorsements explicitly cover claims that begin "in whole or in part prior to the effective date of the run-off period".

C. Employment Practices Liability (EPL) Insurance – Do not cancel the EPL policy. The EPL is a Claims Made policy that will automatically convert to run-off upon closing and remain in force for the duration of the policy period. During this time period between closing and expiration LDC will able to report Claims alleging pre-close wrongful acts but which are not reported prior to closing.

2. Key Recommendations (Post-Close)

A. Evaluate Professional Liability exposure if Delta is providing any professional services (engineering, consultative, etc.) for which it has Professional Liability coverage. This is not currently part of the existing program.

B. Execute ERM-14 for Workers Compensation experience modifier to potentially reduce the modifier due to change in ownership.

C. Bind coverage for Delta gas on either an integrated or stand-alone basis, correcting deficiencies as outlined in this report.

3. Premium Estimates

The following table outlines the annualized premium estimates for the post-closing company. *These are broker premium estimates as Delta has not clarified the March 2017 renewal exposures to be covered.*

EXPOSURE BASIS	2015	2016	% Change	Actual Change
Gross Revenue	86,188,000	64,130,000	-25.6%	(22,058,000)
Number of Vehicles	127	126	-0.8%	(1)
WC Payroll	$8,065,000	$8,350,000	3.5%	285,000
GL Payroll	$4,516,000	$4,552,000	0.8%	36,000
Customer Count	416,621	416,977	0.1%	356
Throughput	19,774,000,000	20,116,000,000	1.7%	342,000,000
Property Values:	32,735,128	33,179,634	1.4%	444,506
Inland Marine: Scheduled Equipment and EDP	7,327,609	7,386,275	0.8%	58,666

			OPTION 1 DELTA REMAINS STAND ALONE				OPTION 2[4] INTEGRATED INTO LDC PROGRAM			
ANNUALIZED PREMIUMS	2015	2016	ESTIMATED PREMIUM	ESTIMATED TAX[1]	TOTAL	Diff. from Current:	ESTIMATED PREMIUM	ESTIMATED TAX[1]	TOTAL	Diff. from Current:
General Liability	$46,110	$46,478	$47,872	$862	$48,734	$2,624	$5,986	$108	$6,094	($40,384)
Automobile Liability	$82,014	$85,752	$88,325	$1,590	$89,914	$7,900	$38,052	$685	$38,737	($47,015)
Workers' Compensation	$102,331	$105,188	$108,344	$1,950	$110,294	$7,963	$171,314	$3,084	$174,398	$69,210
Excess Liability	$205,551	$213,792	$224,482	$10,775	$235,257	$29,706	$389,555	$18,699	$408,254	$194,462
Property / Gas In Storage / Boiler & Machinery	$63,757	$63,757	$63,757	$1,148	$64,905	$1,148	$36,265	$653	$36,918	($26,839)
Equipment Floater/EDP	$19,468	$19,910	$19,910	$358	$20,268	$800	$19,910	$358	$20,268	$358
Control of Well	$8,287	$8,287	$8,287	$149	$8,436	$149	$8,287	$149	$8,436	$149
Network Security	$14,450	$35,524	$35,524	$639	$36,163	$21,713	$0	$0	$0	($35,524)
Pollution Liability[2]	$61,159	$54,498			3-year prepaid	$0			3-year prepaid	$0
Crime	$4,331	$4,546		$0	$0	($4,331)	$0	$0	$0	($4,546)
Fiduciary Liability/Excess Fiduciary	$17,102	$17,102		$0	$0	($17,102)	$0	$0	$0	($17,102)
Employment Practices Liability	$37,753	$37,753		$0	$0	($37,753)	$0	$0	$0	($37,753)
Directors & Officers Liability	$101,291	$101,291		$0	$0	($101,291)	$0	$0	$0	($101,291)
Excess Directors & Officers Liability	$50,900	$50,900		$0	$0	($50,900)	$0	$0	$0	($50,900)
Excess Directors & Officers Liability - Side A DIC	$17,306	$17,306		$0	$0	($17,306)	$0	$0	$0	($17,306)
Service Fee	$70,000	$70,000	$51,414	$0	$51,414	($18,586)	N/A	$0	$0	($70,000)
Operational Insurance Costs TOTAL:	**$901,810**	**$932,084**			**$665,385**	($175,266)			**$693,105**	($184,481)
RUN-OFF Insurance - Directors & Officers3	Not purchased	Not purchased	$175,000	$3,150	$178,150	$178,150	$175,000	$3,150	$178,150	$178,150
RUN-OFF Insurance - Fiduciary Liability3	Not purchased	Not purchased	$32,000	$576	$32,576	$32,576	$32,000	$576	$32,576	$32,576
One-Time Transactional Insurance Costs TOTAL:					**$210,726**	$210,726			**$210,726**	$210,726
Go Forward Operational Insurance and One-Time Transactional Insurance TOTAL:		**$932,084**			**$876,111**	($55,973)			**$903,831**	$27,720

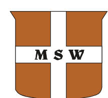
[1]Surplus Lines taxes are estimated at 1.8% Kentucky Surcharge and 3% Surplus lines tax for Option 1 (surplus lines do not apply to companies admitted to do business in the policyholder's home state).
Option 2 estimated at 3% Pennsylvania Surplus Lines Tax plus $20 stamping fee (surplus lines to not apply to cmpanies admitted to do business in the policyholder's home state.

[2]Pollution Liability - 3 year prepaid policy 2016-2019

[3]Assumes a September closing date for unearned premium consideration

[4]Option 2 notes:
General Liability deductible $1,000,000 as compared to guaranteed cost Delta program
Automobile Liability deductible $1,000,000 as compared to guaranteed cost Delta program
Workers' Compensation deductible $1,000,000 as compared to guaranteed cost Delta program. Premium shown is estimated on all employees at higher class code for Gas Workers and doesn't contemplate clerical
Excess Liability premium includes coverage to a $200,000,000 limit as compared to Delta's expiring $35M
Property SIR $100,000 except $250,000 GIS as compared to $10,000 except $25,000 GIS as provided under the Delta program

Note: *All premiums and taxes have been rounded to the nearest dollar*



4. Contractual Requirements – Summary of Insurance Requirements

We have reviewed many of the contracts provided in the data room and can comment as follows:

- We understand that there is no project financing or loans with specific covenants attributable to this transaction

- Delta's insurance program appears to meet those insurance requirements included in the contracts available to review.

SECTION II – CURRENT COVERAGE ANALYSIS – *Summary of Findings*

1. Management Liability Insurance –

A. Directors & Officers Liability Insurance

Delta carries $25MM in total D&O insurance limits; $20MM in traditional D&O and $5M in Side-A DIC. Both the traditional and Side-A DIC provide broad coverage and are placed with carrier that have strong financial ratings.

The D&O limits are well within peer benchmarks and well above security class action settlement norms for companies with similar risk profiles.

A $1,000,000 retention applies claims brought by Delta shareholders alleging inadequate consideration.

Extended Discovery Periods (Run-off) – The policies do not specify pricing for a six year Extended Discovery Period. Expect the pricing to be within market norms of 125% to 150% of annual premiums (minus unearned premium). LDC's D&O insurance will cover Delta exposure starting at closing, but will only cover acts occurring after closing.

B. Employment Practices Liability Insurance (EPL)

The EPL program is placed with Ace (same as LDC). The $15MM in limits is at the high end of peer benchmarks while the retention ($25,000) is at the low end. The terms of the policy are on par with industry norms and LDC.

The EPL program does not cover Wage-and-Hour claims, most EPL policies do not, but LDC should request a Representation confirming compliance with Fair Labor Standards Act and similar wage-and-hour laws.

LDC's EPL insurance will cover Delta exposure starting at closing, but will only cover acts occurring after closing. Delta's EPL program will remain in force for the duration of the natural policy period, but only cover acts occurring prior to closing. This is an automatic tail period and should be sufficient to know if all claims have been reported per the conditions of the policy.

C. Fiduciary Liability Insurance

The Fiduciary program is placed with Ace. The $20MM in limits is indicative of an insured with a pension. The terms of the policy are on par with industry norms.

This program should be placed into Run-off upon closing so as to protect LDC against any historic fiduciary/pension exposures. The premium ($16,800 is low by peer standards with similar limits and risk profile)

D. Crime Insurance

The Crime insurance program has $1MM in limits and a $10k deductible. The limit is lower than we generally recommend for similar risks, as is the Social Engineering limit at $50,000. LDC's Crime program will cover the Delta exposure starting at closing.

Directors & Officers Liability

Carriers:	Houston Casualty Company (HCC Tokyo Marine) Continental Casualty Company (CNA) Federal Insurance Company (Ace)
Named Insured:	Delta Natural Gas Company, Inc.
A. M. Best Rating:	A or better
Policy Term:	3/9/2016 – 3/9/2017
Limit:	$20,000,000 Traditional D&O $5,000,000 Side-A DIC
Retentions:	
• Non-indemnifiable	$0
• Indemnifiable	$250,000
• Securities (Non-M&A)	$250,000
• Bump-up Claims	$1,000,000 (claims alleging inadequate consideration in M&A transactions)
Policy Forms:	
• HCC	USSIC 991 (03/2004)
• CNA	G-22075-B 6/2010
• Chubb	14-02-133333 (ed. 11/2007)
Loss History:	None
Annual Premium:	$169,497

Key Findings and Recommendations

i. M&A retention will apply if Delta shareholder files class action or derivative alleging inadequate consideration
ii. Run-off pricing should be priced between 125% and 150% of annual premium, minus unearned premium, for a 6 year run-off period (assumes no material claims)

2. Property & Casualty Insurance

The current Delta Property & Casualty insurance program contains broad coverage in line with other gas utilities at competitive pricing. Delta's insurance program differs from LDC's in the following key ways:

1. **Risk Retention Philosophy:** Delta currently purchases its primary casualty (GL, AL, WC) coverage on a "Guaranteed Cost" or $0 deductible basis. Many companies of Delta's size purchase insurance in this manner. It also preferable for many insurers as it allows the insurer to control the claims and drive down claims costs. From a regulatory perspective, it is our understanding that Delta receives recovery in its rates for insurance premium expenses. A Guaranteed Cost program reduces cash flow volatility for Delta and helps create a more predictable total cost of risk. On the other hand, Peoples Gas, being a much larger company, takes a $1MM deductible on its primary casualty insurance programs. In the premium summary, we outline the cost savings to integrate Delta into the People's insurance program; however, Peoples' management should consider the regulatory recovery of premiums when making the decision on whether to increase Delta's deductibles.

2. **Excess Liability Limits**: Delta currently purchases only $35MM in Excess Liability coverage through AEGIS. Based on the exposure to a large gas explosion, auto liability case, or some other significant third party loss, this is relatively low when compared to other LDC's. LDC Funding carries $200MM in total casualty coverage. However, we expect that Delta can be integrated into LDC's Excess Liability policies at minimal cost upon closing.

3. **Control of Well**: Control of Well coverage is purchased to cover the costs to regain control of a well after a blowout. This includes coverage includes:

   a. Costs to bring a well back under control,
   b. Pollution cleanup costs incurred due to pollution that results from a well out of control, Legal liability for pollution-related bodily injury or property damage arising from a well out of control event, and
   c. Redrill and other extra expenses incurred to restore the well to its pre-loss condition.

   Currently Delta purchases this coverage for its Gas in Storage (GIS) operations for $8,141 in premium. We recommend continuing to purchase this coverage post-closing.

4. **Inland Marine:** This is purchased to cover scheduled equipment and Electronic Data Processing Equipment and Software. The premium to do so is relatively small ($19,124). LDC Funding's property insurance program provides coverage for this at higher deductible and we would recommend integrating this coverage post-closing.

5. **Cyber Liability Insurance:** Delta currently purchases a small ($5MM) policy with ACE for network security events. This policy does not provide the breadth and extent of coverage that LDC's does. Additionally, since Delta's IT systems and customer records will be presumably rolled into that of LDC's, it would be impractical to procure two policies for the same exposures. Therefore we recommend non-renewing this coverage upon closing and adding Delta to the LDC policy.

6. **Environmental:** Stand alone Pollution Legal Liability (PLL) coverage is purchased through XL to cover pollution exposures. This policy has a $1MM limit and $100k Self Insured Retention. AEGIS provides pollution coverage excess of $1MM for Delta. LDC does not currently purchase a PLL policy and Self Insures this for the first $1MM. The PLL policy is a fixed three-year term and premium of $53,534 was paid in full at inception.

7. **Primary General Liability, Auto Liability, and Workers Compensation**: The GL coverage is provided by Liberty Mutual in a primary package policy. For LDC, Liberty insures only the GL and AL, but Brickstreet provides the WC. In the 2016-2017 renewals, Delta's primary program was marketed to alternative insurers, and the next closest quotes were $38,000 higher than Liberty's. Due to Delta's size and operations, Delta is at or below minimum premiums for insurers underwriting this class of business. Liberty is only able to offer the coverage and pricing due to their historical relationship with the account and by writing all lines of coverage (GL, AL, and WC).

   At the 2016-2017 renewal, the GL and WC were flat, and the Auto experienced a 5% rate increase due to the $42,000 in physical damage claims (against $11,000 in premium attributable to the auto physical damage coverage). Currently LDC Funding does not purchase Auto Physical Damage coverage.

   LDC's WC insurer, Brickstreet, quoted Delta in the past but was significantly higher cost than Liberty. However, we believe that Brickstreet will be able to cover Delta employees in LDC's policy at the in-force LDC rates (and therefore higher deductible). Careful evaluation of the risk retention should be performed prior to making this decision.

Property Coverage

Carrier:	ACE American Insurance Company
Named Insured:	Delta Natural Gas Company, Inc.
A. M. Best Rating:	A++ XV
Policy Term:	3/9/2016 – 3/9/2017
Coverage:	Direct physical loss or damage to first party property
Equipment Valuation:	Building/Personal Property: $26,953,690 Gas in Storage: $5,225,944
Limit:	$33,179,634 Per Occurrence, subject to various sublimits
Deductible:	$10,000 except $50,000 Flood, $25,000 Earthquake, $25,000 Underground Gas, 12 Hours Earnings
Policy Form:	Starr Property Form
Loss History:	Loss history from 3/9/10 to 3/9/14 included a theft at the Corbin, KY location on 10/11/13 resulting in a claim of $37,528. Currently valued loss run not available to review
Annual Premium:	$63,757 including applicable Kentucky surcharge, subject to monthly reporting and annual adjustment for Gas in Storage

Key Findings and Recommendations

i. Policy provides a $100,000 limit for EDP Equipment and Media. This may provide some duplication of coverage with the Allianz policy. We suggest a thorough review to ensure no duplicate coverage exists.

ii. Covered Locations are specifically scheduled which can be onerous to maintain if new locations are acquired. Newly acquired property must be noticed to the Insurer within 30 days from acquisition (flood and earthquake excluded during this period). We would suggest trying to obtain blanket coverage for all locations of the Insured without the need for scheduling.

iii. Ingress/Egress coverage is not provided. This should be added for a radius of 5 miles from the Insured Location.

iv. Policy has a 90% coinsurance clause. We would suggest removing this requirement or having it reduced to 80% if the Insurer will not agree to remove entirely

Inland Marine

Carrier:	Allianz
Named Insured:	Delta Natural Gas Company, Inc.
A. M. Best Rating:	A+ XV
Policy Term:	3/9/2016 – 3/9/2017
Coverage:	Equipment Floater and Electronic Data Processing
Equipment Value:	Scheduled Equipment: $3,766,803; Misc. Tools $20,000 EDP: $3,619,472
Limit:	Scheduled Equipment: $3,786,803 EDP: $3,630,472
Deductible:	$2,500 except Miscellaneous Tools $500
Policy Form:	Inland Marine
Loss History:	Total losses incurred from 3/9/10-3/9/16 is $50,691. All claims a result of theft. The 2016 loss run was not available to review
Annual Premium:	$19,910 including applicable Kentucky surcharge

Key Findings and Recommendations

i. Coverage includes 100% coinsurance as respects Contractors Equipment and EDP Equipment which requires Delta insure the items covered at 100% of their value. We suggest trying to remove the coinsurance clause altogether or lower the percentage requirement to 80%.

ii. Terrorism is excluded. Reevaluate if needed.

iii. Blanket Loss Payee as respects the Contractors Equipment Coverage.

iv. Coverage is limited to $100,000 per item for equipment leased, rented or borrowed from others. Ensure this limit is sufficient to cover the standard individual items rented.

v. Coverage for Earthquake and Flood are included as respects EDP Equipment.

vi. EDP premium is auditable. Final schedule must be submitted to underwriters within 10 days following expiration. Premium will be adjusted if values exceed 10% variation from those submitted at inception.

vii. We suggest re-evaluating if the lower deductibles provided under this policy are necessary. If not, coverage could be provided under the property policy.

Casualty Coverage

General Liability

Carrier: Liberty Mutual Insurance

Named Insured: Delta Natural Gas Company, Inc.

A. M. Best Rating: A XV

Policy Term: 3/9/16 – 3/9/17

Coverage: Coverage for legal liability for third party Bodily Injury and Property Damage

Limit: $1,000,000 Per Occurrence / $10,000,000 General Aggregate / $2,000,000 Per Project Aggregate subject to General Aggregate

Deductible: Nil

Policy Form: CG 00 01 04 13

Loss History: Loss history shows 6 claims since 2011. The largest claim has a reserve of $290,000 resulting from an explosion

Annual Premium: $46,478 including applicable Kentucky surcharge, subject to audit

Key Findings and Recommendations

i. Pollution: Currently sudden and accidental pollution events are covered in the General Liability Policy subject to a $10,000 deductible. Time Element period of 10 days with 20 days to report.

ii. Blanket Additional Insured and Waiver of Subrogation are provided as required by written contract.

iii. Professional Liability coverage is excluded. If Delta are performing any professional services, they should consider a Professional Liability policy. A Professional Liability policy would cover Delta for liability (economic damage) associated with its negligence in performing professional services and associated defense costs.

iv. Failure to Supply is excluded. If Delta have any contracts where they could be held liable if they are unable to supply gas to a third party we would recommend exploring the removal of this exclusion. Tariff protection may exist.

v. Policy is subject to audit.

vi. Terrorism is currently excluded. We would suggest revisiting the need for terrorism insurance.

Automobile Liability

Carrier: Liberty Mutual Insurance

Named Insured: Delta Natural Gas Company, Inc.

A. M. Best Rating: A XV

Policy Term: 3/9/16 – 3/9/17

Coverage: Third Party Property Damage and Bodily Injury due to loss involving a covered Automobile. Includes Comprehensive for Owned vehicles.

Limit: $1,000,000 except collision for Owned Autos which is self-insured

Deductible: $Nil except $1,000 Comprehensive

Policy Form: CA 00 01 10 13

Loss History: Delta has had several auto claims since 2011, the largest being a rear-end collision currently reserved at $63,182

Annual Premium: $85,752 including applicable Kentucky surcharge, subject to audit

Key Findings and Recommendations

i. Currently coverage for collision is provided for hired autos only. Consider adding to owned autos.

ii. Policy is auditable, there may be additional premium due if vehicle schedule increased from that declared at inception.

iii. Drive Other Car is provided for specified individuals only. We suggest reviewing the schedule to determine if appropriate to broaden to all individuals of a certain employment level or at a minimum ensure the appropriate names are included.

iv. Additional Insured status currently provided for Lessors only. We suggest broadening to any entity as required by written contract.

Coverage:	**Symbol**	**Covered Autos**
Liability	1	Any "Auto"
Personal Injury Protection	5	Owned "Autos" Subject to no-fault
Medical Payments/Expense	2	Only those autos you own.
Uninsured/Underinsured Motorists	2	Only those autos you own.
Comprehensive	02, 08	Owned autos, Hired Autos
Collision	8	Hired Autos

Workers' Compensation

Carrier:	Liberty Mutual Insurance
Named Insured:	Delta Natural Gas Company, Inc.
A. M. Best Rating:	A XV
Policy Term:	3/9/16 – 3/9/17
Coverage:	Provides Workers' Compensation benefits and coverage for losses when you as the Employer are found legally liable.
Limit:	$1,000,000 EL; Statutory Workers' Compensation
Deductible:	Nil
Policy Form:	WC 00 00 00 C 01/01/15
Loss History:	Delta appear to have good workers' compensation claims experience. Largest claim since 2011 involves a knee sprain currently reserved at $67,898
Annual Premium:	$105,188 including applicable Kentucky surcharge, subject to audit

Key Findings and Recommendations

i. The current experience modifier is 0.92. The experience modifier is a measurement of actual claims experience and the actual expected claim experience for companies of the same class. An employer with an average experience would have a modifier of 1.0. The modifier assigned to Delta indicates above average favorable claims experience.

ii. Policy is auditable and there may be additional premium due upon expiration if payroll increased from that declared at inception.

iii. A new ERM-14 will need to be completed to reflect the change in ownership. A new experience modifier may be issued as a result.

iv. Blanket Waiver of Subrogation not provided. We suggest adding endorsement providing where required by written contract.

Excess Liability

Carrier:	Associated Electric & Gas Insurance Services (AEGIS)
Named Insured:	Delta Natural Gas Company, Inc.
A. M. Best Rating:	A XV
Policy Term:	3/8/16 – 3/8/17
Coverage:	Excess Liability
Limit:	$35,000,000 per Occurrence / $70,000,000 Policy Aggregate
Self-Insured Retention:	$1,000,000
Policy Form:	AEGIS Excess Liability Policy Form 8100 (01/13) – Claims First Made
Loss History:	None
Annual Premium:	$213,792 including applicable surplus lines tax and Kentucky surcharge

Key Findings and Recommendations

i. Does not follow form of the underlying, which means that coverage is only provided as noted within the policy form – exclusions and terms in the underlying policy do not apply unless specifically noted in the AEGIS policy form.

ii. Drop down provisions are not provided in the event of erosion of the underlying policy limits.

iii. Policy term intended to be 3/9/16 – 3/9/17; however, policy Declaration indicate policy term of 3/8/16 – 3/8/17. We recommend requesting an endorsement to amend the policy period to 3/9/16 to 3/9/17 to coincide with the underlying policies and avoid non-currency of terms.

iv. Watercraft in excess of 75 feet are excluded. Ensure Delta have no watercraft in excess of 75 feet.

v. Aircraft, manned or unmanned, which is chartered, operated, hired, loaned, leased or rented for a period of more than 30 consecutive days is excluded. Owned aircraft are also excluded. Ensure no owned or long-term lease aircraft coverage is needed.

vi. Policy is endorsed to specifically state that coverage is excess of any valid and collectible control of well insurance including but not limited to EED, OEE or similar policy forms. In the event of exhaustion of the available underlying control of well limit, the AEGIS policy will be excess of (a) 10% of such limit or (b) $3,000,000 each occurrence – Pollution Liability, whichever is higher.

vii. Pollution coverage is Time Element with 30/60 reporting requirement. This is a mandatory endorsement for AEGIS which they will not amend.

Pollution Liability

Carrier:	XL Insurance
Named Insured:	Delta Natural Gas Company, Inc.
A.M. Best Rating:	A XV
Policy Term:	3/9/16 – 3/9/19
Coverage:	Covers loss and related legal expense resulting from a pollution condition on, at or migrating from any Covered Location for which the Named Insured has become legally obligated to pay. Remediation Expense coverage and Contingent Transportation coverage is included
Limit:	$1,000,000
Deductible:	$100,000
Policy Form:	Pollution and Remediation Legal Liability – Claims Made – PARL6CP1111 (3/18/16)
Loss History:	Loss history not available to review
Annual Premium:	$54,498 three-year prepaid, including applicable Kentucky surcharge. Minimum earned premium 60%

Key Findings and Recommendations

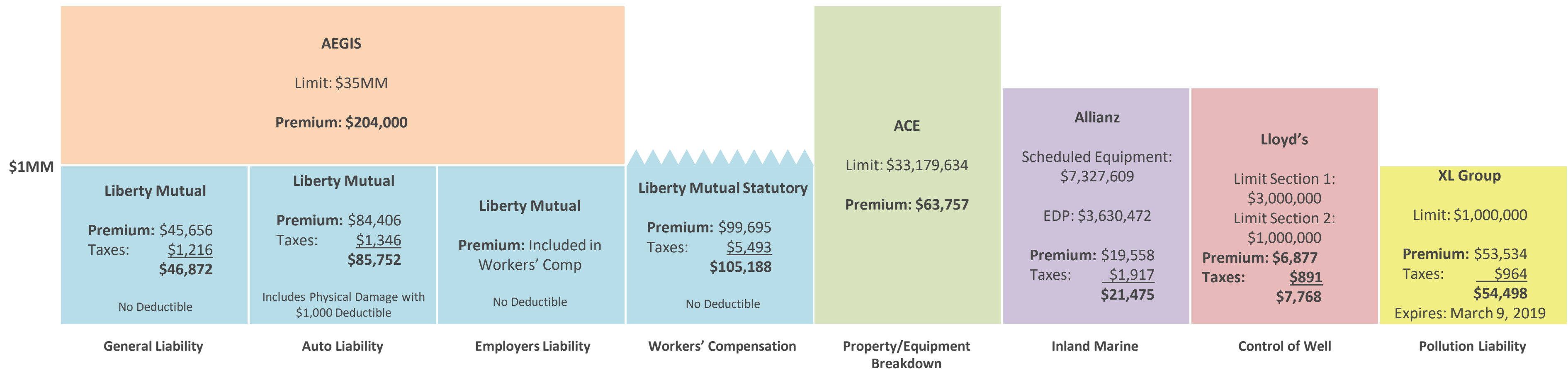
i. Policy includes Mold Exclusion. We suggest requesting this exclusion be removed/

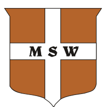
ii. Coverage is provided for locations specifically scheduled only. Ensure all locations are appropriately listed.

iii. Underground storage tank schedule is provided for Canada Mountain only. Ensure no other locations require this endorsement.

CURRENT PROGRAM OVERVIEW 2016-17

Delta Natural Gas Company, Inc.
Expiring Insurance Program
March 9, 2016 - 2017





Casualty Program Analysis – the following tables outline the key coverage items across the casualty and property policies. We recommend achieving consistent coverage for all policies.

	General Liability	Automobile Liability	Workers' Compensation	Excess Liability	Pollution Liability
Ins. Co	Liberty Mutual	Liberty Mutual	Liberty Mutual	AEGIS	XL
Limits	$1M/$10M	$1M	Statutory/$1M EL	$35M/$70M	$1M
Deductible	Nil	Nil except $1,000 Comprehensive	Nil	SIR: $1M	$100,000
1NI	Delta Natural Gas Company, Inc. including Delgasco, Inc Delta Resources, Inc Enpro, Inc and any other organization in which the company owns 50% or more	Delta Natural Gas Company, Inc. including Delgasco, Inc. Delta Resources, Inc. Enpro, Inc. And any other organization in which the company owns 50% or more	Delta Natural Gas Company, Inc. Including Delgasco, Inc. Delta Resources, Inc. Enpro, Inc.	Delta Natural Gas Company, Inc. and any subsidiary company in line of corporate descent including Delgasco, Inc. Delta Resources, Inc. Enpro, Inc.	Delta Natural Gas Company, Inc. including Delgasco, Inc. Delta Resources, Inc. Enpro, Inc.
Additional Insured	Blanket	Provided for Lessors only	Not available	Blanket	

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	General Liability	Automobile Liability	Workers' Compensation	Excess Liability	Pollution Liability
Waiver of Subrogation	Blanket	Blanket		Blanket	
NOC	60 Days/10 Days nonpayment of premium	60 Days/10 days nonpayment of premium	60 Days/10 days nonpayment of premium	90 Days/10 days nonpayment of premium	60 Days/10 days nonpayment of premium
Pollution	Total Pollution Exclusion with Time Element Liability Coverage Extension	Broadened Coverage for Covered Autos		Time Element Reporting/Pollution	

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	General Liability	Automobile Liability	Workers' Compensation	Excess Liability	Pollution Liability
Endorsements, Exclusions and Misc. Conditions	Broad Form Named Insured – Majority Interest Employee Benefits Liability Misdelivery of Liquids Products Contractual Liability – Railroads Non-Cumulation of Limit (Same Occurrence) Unintentional Failure to Disclose Notice of Cancellation to Third Parties (30 Days) Designated Locations Aggregate Subject to General Aggregate Limit ($2,000,000) Professional Health Care Services by Employees Coverage ($1,000,000) Underground Recourses and Equipment Coverage Extension ($2,000,000) Blanket Additional Insured Exclusion of Certified Acts of Terrorism Employment Practices Liability Exclusion Failure to Supply Exclusion Asbestos, Silica, Lead, Fungi, Bacteria Exclusions PCB Exclusion Electromagnetic Fields and Electromagnetic Radiation Exclusion MTBE Exclusion	Broad Named Insured Endorsement Notice of Cancellation to Third Parties (30 Days) Wrong Delivery of Liquid Products Terrorism Exclusion Drive Other Car – Broadened Coverage for Named Individuals Pollution Liability – Broadened Coverage for Covered Autos Hired Autos Specified as Covered Autos you Own Employees As Insureds Unintentional Errors & Omissions Knowledge of Accident – Insurance Manager Blanket Waiver of Subrogation MCS90 Lessor – Additional Insured and Loss Payee Schedule of Additional Insured – Lessor(s) - Blanket Fellow Employee Coverage	Covered State – KY USL&H Compensation Act Schedule Named Insured Endorsement Alternate Employer Endorsement - Blanket Voluntary Compensation and Employers Liability Coverage Endorsement Notification of Change in Ownership Endorsement Terrorism Endorsements Knowledge and Notice of Occurrence Unintentional Errors & Omissions Notice of Cancellation to Third Parties (30 Days)	OFAC Exclusion Named Insured Endorsement Employment Practices Liability Exclusion Revised Exclusion (A) Endorsement Community Service Activity Standard Board Activity MCS90 Other Insurance Time Element Reporting/Pollution MTBE Exclusion Telephone Consumer Protection Act and Similar Exclusion	Location Specific Endorsement Additional Named Insured Fines/Penalties/Assessments Exclusion Amendment Coverage for Civil & Administrative Fines, Penalties and Assessments Mold Matter Exclusion Pollution Condition Amendment – Abandoned Materials Disaster Response Expense Coverage Well Out of Control Exclusion (applies only to Location #2 – Canada Mountain) Certified Acts of Terrorism Exclusion Covered Location Schedule Underground Storage Tank Schedule – Canada Mountain

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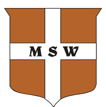

	General Liability	Automobile Liability	Workers' Compensation	Excess Liability	Pollution Liability
Terrorism	Excluded	Excluded	Included	Excluded	Excluded

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SECTION III – SUMMARY OF INSURANCE

Delta Natural Gas
Schedule of Insurance

Type of Coverage	Policy Period	Insurance Company	AM Best Rating	Policy Number	Limits	Coverage	Terrorism	Policy Premium
General Liability	3/9/16 to 3/9/17	Liberty Mutual		TB2-641-443514-056	$1,000,000 $1,000,000 $500,000 $10,000 $10,000,000 $2,000,000 $1,000,000	Each Occurrence Personal & Advertising Injury Damage to Premises Rented to You (any one premise) Medical Expense (any one person) General Aggregate Products Completed Operations Aggregate Employee Benefits Liability (each employee/aggregate)	Rejected	$46,478
Automobile Liability	3/9/16 to 3/9/17	Liberty Mutual		AS2-641-443514-046	$1,000,000 $5,000 $1,000,000	Limit of Liability Medical Payments/Expenses Uninsured/Underinsured Motorists - BI/PD	Excluded	$85,752
Workers' Compensation	3/9/16 to 3/9/17	Liberty Mutual		WC5-641-443514-036	$1,000,000 $1,000,000 $1,000,000	Bodily Injury by Accident Bodily Injury by Disease - Policy Limit Bodily Injury by Disease - Each Employee		$105,188
Excess Liability	3/8/16 to 3/8/17	AEGIS		XL5081505P	$35,000,000 $70,000,000	Each Occurrence General Aggregate	Rejected	$213,792
Pollution Liability	3/9/16 to 3/9/19	XL		PEC003128202	$1,000,000	Each Occurrence	Rejected	$54,498
Control of Well	3/9/2016 to 3/9/17	Lloyds of London		AMW167110	$3,000,000 $1,000,000	Each Occurrence - Control of Well Pollution	Rejected	$8,287
Casualty Total								**$513,995**
Property	3/9/16 to 3/9/17	ACE		EPRN09I77322	$33,179,634	Any One Occurrence	Rejected	$63,757
Inland Marine	3/9/16 to 3/9/17	Allianz		SML-93015533	$3,786,803 $3,630,472	Scheduled Equipment and Miscellaneous Tools EDP	Rejected	$19,910
Property Total								**$83,667**
Total:								**$597,662**

SECTION IV – CARRIER ANALYSIS

All current carriers on the Company's insurance program are A- XI (Excellent) rated or better and are financially solvent.

AM Best's Rating System - The Best's rating system is designed to evaluate a wide range of objective and subjective factors that affect the overall performance of an insurance company (not applicable to associations or intermediaries). These factors deal with the company's financial strength, its operating performance and its ability to meet its financial obligations to policyholders, as follows:

- Profitability
- Quality of reinsurance program
- Quality and diversification of assets
- Adequacy of policy loss reserves
- Capital structure
- Spread of risk
- Leverage/Capitalization
- Liquidity
- Adequacy of policyholder's surplus
- Management experience and objectives

Best's Rating Symbols - A typical Best's rating is composed of two parts. The "Security" portion provides an alphabetical indication of the quality of the security provided by a company to its policyholders. This rating is further defined in three categories, "Secure", "Vulnerable" or "Not Assigned". The "Financial Size" (FSC) portion of the Best's rating uses Roman numerals to rank companies based on the dollar amount of their policyholder's surplus and contingent reserve funds. While comparative rankings for security or financial size by themselves may not adequately portray the complete financial health of a company, the combination of the two has proven to be reliable in predicting the ability of a company to meet its claims obligations in a timely manner, both now and in the near future. The actual rating symbols used by Best and their meanings are:

"Secure" Ratings	A++	or	A+	Superior
	A	or	A-	Excellent
	B++	or	B+	Good
"Vulnerable" Ratings	B	or	B-	Fair
	C++	or	C+	Marginal
	C	or	C-	Weak
	D			Poor
	E			Under Supervision
	F			In Liquidation
	S			Suspended

"Not Rated" Categories – Assigned to companies not rated by A.M. Best.

Financial Size Categories:

I	Under $1,000,000	VIII	100,000,000 - 250,000,000
II	1,000,000 - 2,000,000	IX	250,000,000 - 500,000,000
III	2,000,000 - 5,000,000	X	500,000,000 - 750,000,000
IV	5,000,000 - 10,000,000	XI	750,000,000 - 1,000,000,000
V	10,000,000 - 25,000,000	XII	1,000,000,000 - 1,250,000,000
VI	25,000,000 - 50,000,000	XIII	1,250,000,000 - 1,500,000,000
VII	50,000,000 - 100,000,000	XIV	1,500,000,000 - 2,000,000,000
		XV	Over $2,000,000,000

* Source: Best's Key Rating Guide – 2016 Edition

SECTION V – BENCHMARKING

Property Benchmarking

Company	Values		Limits & Deductible/Retentions			Exposure
	Gas in Storage Value	Total Insurable Values	Limit (MM)	Base PD Deductible / Retention	BI Deductible	NAT CAT
A	$8,000,000	$565,738,172	$105	$100,000	N/A	CA Quake
B	$230,329,896	$10,249,172,974	$350	$1,000,000	15/30 Days / $250k	New Madrid
C	$193,074,563	$992,327,687	$35	$100,000	$100,000	N
D	$463,390,477	$751,779,230	$110	$100,000	14 Days/$25k	N
E	$364,076,760	$1,750,028,747	$200	$2,500,000	$5MM combined PD/BI	High Haz Flood Zone
F	$0	$6,137,310,439	$500	$1,000,000	30 Days	Y - Flood Zone A
G	$0	$6,810,146,000	$300	$2,500,000	30 Days	Flood
H	$0	$10,041,361,421	$500	$1,000,000	N/A	N
I	$0	$20,581,223,715	$750	$2,500,000	N/A	N
J	Included	$41,402,149,379	$600	$10,000,000	45 Days	N
Delta	$7,378,594	$32,735,128	$32.7	$10,000	120 Hours	N

	Gas in Storage Value	Total Insurable Values	Limit (MM)	Base PD Deductible / Retention	BI Deductible
High	$ 463,390,477	$ 41,402,149,379	$ 750	$ 10,000,000	$ 100,000
Low	$ -	$ 32,735,128	$ 33	$ 10,000	$ 100,000
Median	$ 7,689,297	$ 6,137,310,439	$ 300	$ 1,000,000	$ 100,000
Average	$ 126,625,029	$ 9,028,542,990	$ 317	$ 1,891,818	$ 100,000

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AEGIS Excess Liability Benchmarking

Peer Benchmarking Data										
Company	Ops Code	Renewal As Of	Revenues (in 000s)	Total Assets (in 000s)	Total Limits (MMs)	AEGIS GL Attachment	AEGIS Limits (MMs)	10-Yr Loss	AEGIS Price/Mil	Includes EPL
A	LDC	Sep 15	$250,000 to $500,000	$250,000 to $500,000	100	$250,000	$35	35.0%	$42,667	Y
B	LDC	Sep 14	$500,000 to$1,000,000	$2,000,000 to $5,000,000	200	$1,000,000	$35	NA	$57,571	N
C	LDC/Water	Mar 15	$500,000 to$1,000,000	$2,000,000 to $5,000,000	85	$500,000	$35	3.8%	$51,088	N
D	LDC/Elec	Dec 14	$1,000,000 to $2,000,000	$2,000,000 to $5,000,000	185	$2,000,000	$35	0.0%	$54,366	Y
E	LDC/E&P	May 15	$2,000,000 to $5,000,000	$5,000,000 to $10,000,000	385	$1M/$11M	$35	29.0%	$37,875	Y
F	LDC	Mar 15	$1,000,000 to $2,000,000	$2,000,000 to $5,000,000	150	$1,000,000	$35	0.0%	$227,291	Y
G	LDC	Aug 15	$2,000,000 to $5,000,000	$5,000,000 to $10,000,000	450	$1M/$4M Plus	$35	26.7%	$184,950	Y
H	Elec/LDC	Jul 15	$2,000,000 to $5,000,000	$5,000,000 to $10,000,000	135	$1,000,000	$35	60.4%	$132,343	Y
I	Elec/LDC	Oct 14	$2,000,000 to $5,000,000	$15,000,000 to $20,000,000	200	$1,000,000	$35	8.7%	$68,683	Y
J	Gas/Elec	Jul 15	$5,000,000 to $10,000,000	$20,000,000 to $25,000,000	800	$2,000,000	$35	192.0%	$136,429	Y
K	Elec/Gas	Sep 14	$10,000,000 to $15,000,000	$50,000,000 to $60,000,000	600	$5,000,000	$35	31.5%	$100,131	Y
L	Elec/IPP	Jul 15	$15,000,000 to $20,000,000	$40,000,000 to $50,000,000	435	$10,000,000	$35	0.0%	$83,611	Y
M	Elec/IPP	Dec 14	$10,000,000 to $15,000,000	$60,000,000 to $70,000,000	541	$3,000,000	$35	47.0%	$117,263	Y
N	Elec/IPP	May 15	$15,000,000 to $20,000,000	$70,000,000 to $75,000,000	500	$5,000,000	$35	23.0%	$201,581	Y
Delta	LDC	Mar 15	$86,188	$187,794	35	$1,000,000	$35	0.0%	$5,604	N
		High	$ 18,466,704	$ 70,923,000	$ 800	$ 10,000,000	$ 35	192%	$ 227,291	
		Low	$ 86,188	$ 187,794	$ 35	$ 250,000	$ 35	0%	$ 5,604	
		Median	$ 2,121,707	$ 5,795,038	$ 200	$ 1,000,000	$ 35	25%	$ 83,611	
		Average	$ 5,732,581	$ 20,197,798	$ 320	$ 2,519,231	$ 35	33%	$ 100,097	

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OMM DRAFT 1/20/2017

MEMORANDUM

TO:	SteelRiver Infrastructure Fund North America LP PNG Companies LLC
FROM:	O'Melveny & Myers LLP
DATE:	[____________], 2017
SUBJECT:	Project Drake - Legal Due Diligence

have

Stock outstanding.

2.

[1] Capitalized terms used but not defined in this Executive Summary have the meanings provided below.

6. **Employees and Employee Benefits.** Delta employs approximately 150

[2] We have asked Delta to confirm that the Delta A&R By-Laws provided in the VDR are the definitive by-laws adopted by the Board.

[3] We have asked Delta to provide the definitive by-laws of each of the Subsidiaries.

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[4] We have asked Delta to confirm that no shares of Preferred Stock are currently issued and outstanding.

[5] We have asked Delta to provide any certificates evidencing ownership of the Subsidiaries.

under the NPA if it defaults under any other outstanding

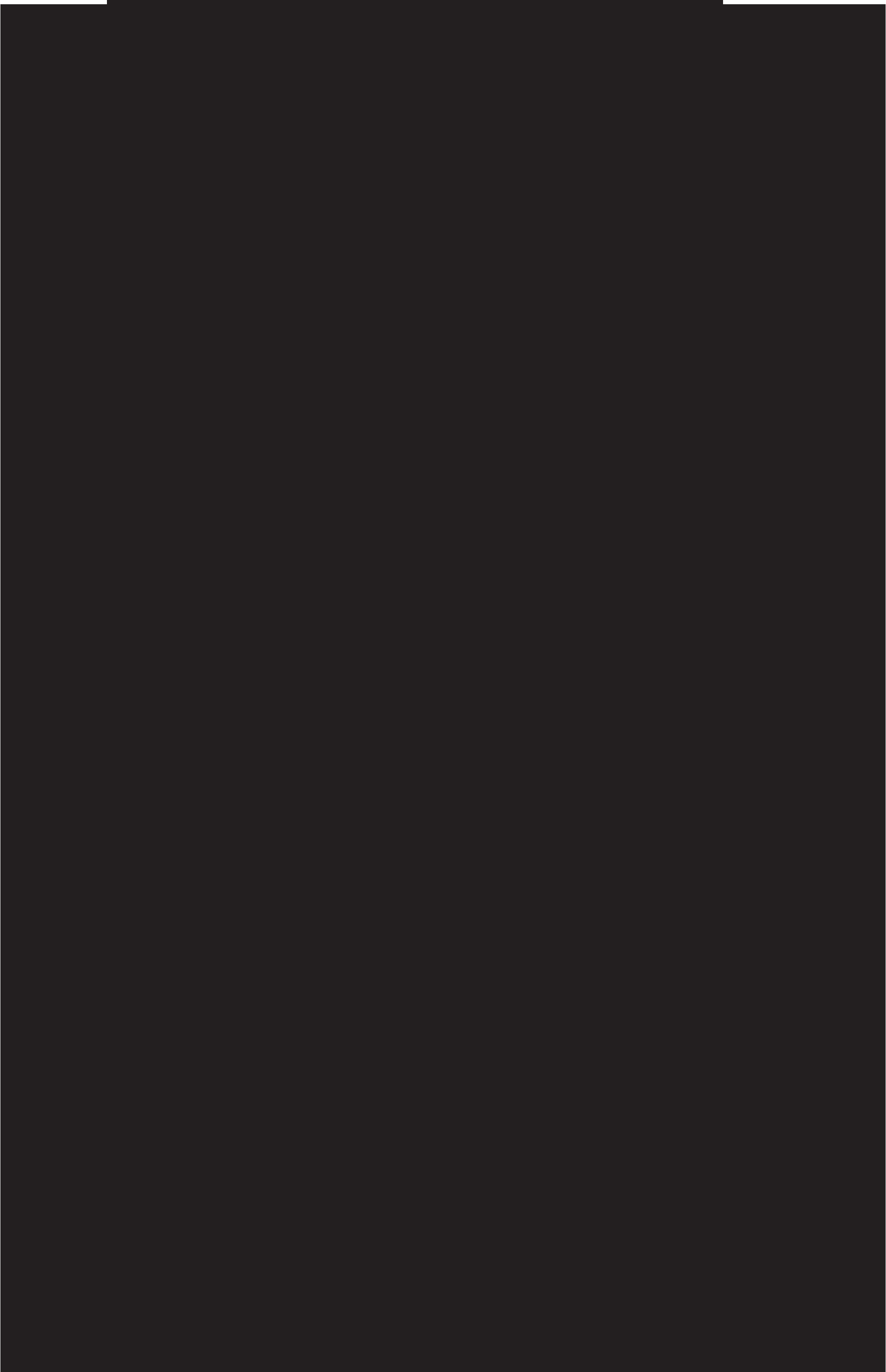
[6] We have asked Delta to provide a copy of the Bank Note, together with all modifications thereto, as well as all amendments to the Loan Agreement.

[7] We have asked Delta to confirm that there are currently no outstanding borrowings under the Loan Agreement.

III.

gas

B.



[8] The law is unsettled as to whether a merger triggers an anti-assignment provision. Our research suggests that, under Kentucky law, a merger does not trigger an anti-assignment provision, unless the agreement specifically provides that the agreement does not survive a merger. As such, we believe that the consummation of the Proposed Transaction does not require the consent of the counterparties to agreements containing anti-assignment clauses.

5. ***On-System Transportation - Small Non-Residential.***

(a) Customer Charge. $31.20

(b) First 200 Mcf. $4.3185

(c) Next 800 Mcf. $2.6696

(d) Next 4,000 Mcf. $1.8735

(e) Next 5,000 Mcf. $1.4735

(f) Over 10,000 Mcf. $1.2735

6. ***On-System Transportation - Large Non-Residential.***

(a) Customer Charge. $131.00

(b) First 200 Mcf. $4.3185

(c) Next 800 Mcf. $2.6696

(d) Next 4,000 Mcf. $1.8735

(e) Next 5,000 Mcf. $1.4735

(f) Over 10,000 Mcf. $1.2735

7. ***On-System Transportation - Residential.***

(a) Customer Charge. $20.70

(b) All Mcf. $4.3185

8. ***Off-System Transportation.***

(a) All Dth. $0.2826

D. Conservation/Efficiency Program Filing. The VDR contains an accepted copy of a Conservation/Efficiency Program filing effective February 1, 2016, applying a Gas Cost Recovery ("**GCR**") rate of $0.40897. Per the most recent gas cost recovery filings, the upcoming Gas Cost Recovery Rate is $0.49461 and will be effective as of January 30, 2017. The VDR also contains the Company's initial application for approval of its Customer Conservation/Efficiency Program received by the KYPSC on February 20, 2008.

[9] We have submitted several requests and questions to Delta related to EHS matters that remain pending.

1.

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C.

D.

[10] We have also asked Delta to provide analysis as to the potential exposure under Section 280G due to any other "disqualified individuals" receiving parachute payments in connection with the Proposed Transaction.

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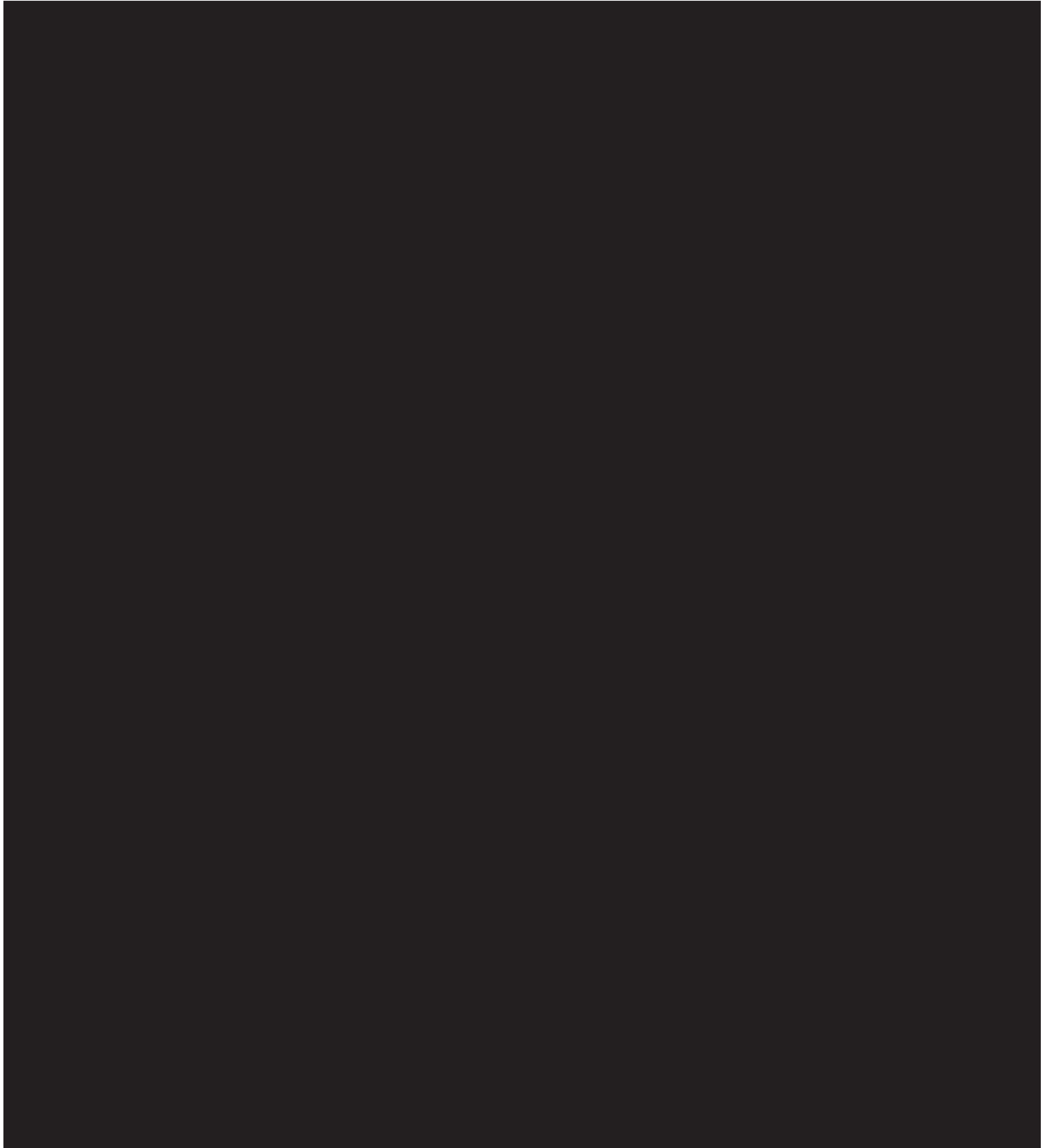

[11] We have asked Delta to provide vesting deeds, title work and surveys for all owned facilities.

[12] We have asked Delta for confirmation as to which offices are leased and which are owned.

[13] We have asked Delta for confirmation as to whether office addresses correspond to leases or deeds, and with respect to any leased property, for copies of each lease.

[14] We have asked Delta for additional information regarding these leases, as well as copies of the leases.

[15] We have asked Delta to describe and provide any documentation in connection with any currently pending or threated (in writing) material litigation against the Company or any of the Subsidiaries.

Exhibit A

Organizational Structure

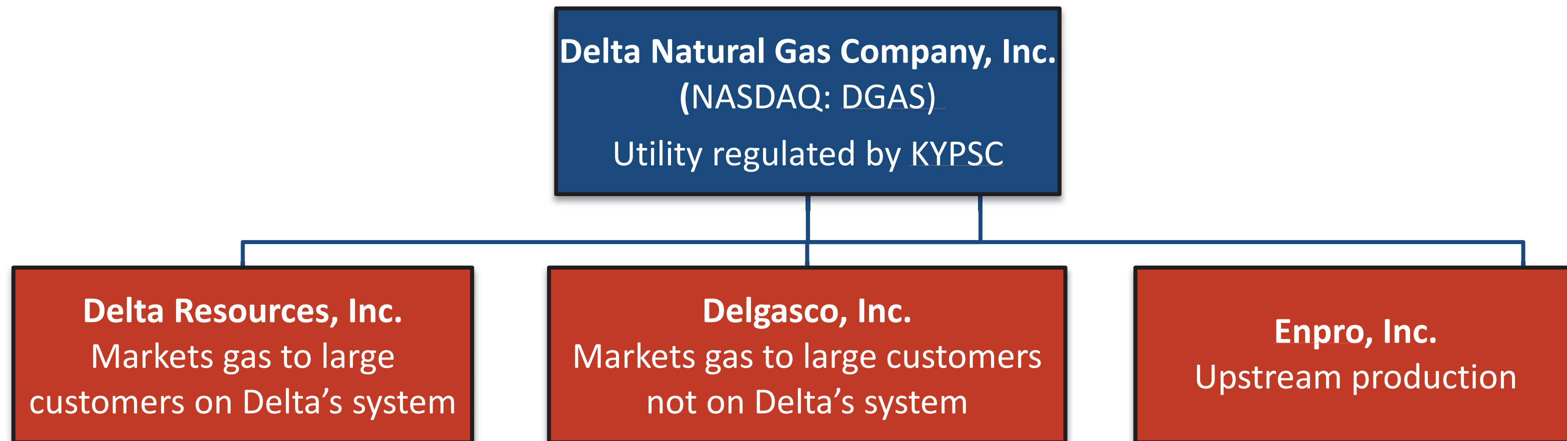

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Exhibit B

IT/Software Licenses[16]

Data Site No.	Name, Parties to and Date of Agreement	Basic Business Purpose	Terms of License IP Ownership Issues	Term / Termination	Assignment / Change of Control	Exclusivity / MFN	Indemnity Obligation by Company/ Limitation of Liability	Non-Compete / Non-Solicit	Governing Law/ Other
4.12.1	**Master Services Agreement between Paymuntus Corporation ("Paymentus") and Delta Natural Gas Company ("Delta"), dated September 8, 2008**	Paymentus provides customers the opportunity to make payments with credit cards and other payment methods.	Inbound License: Paymentus grants Delta a revocable, non-exclusive, royalty-free license to use Paymentus' logo and other service marks to promote the Services. (§7.8)	Term: September 8, 2008 until 3 years after the Launch Date; subject to 2-year automatic renewal periods, provided either party can cancel automatic renewal upon 6 months' notice. (§9.1)	None	None	Indemnity: Delta to indemnify Paymentus for claims arising from the (i) willful misconduct or negligence in performing the Services or (ii) material breaches of covenants. (§§8.1 to 8.2) Limitation of Liability: Paymentus' liability is limited to the Service Fee for the particular transaction that is the subject matter of the claim of damage. (§8.4)	None	Governing Law: Kentucky (§6)
4.12.2	**Purchase Agreement - Cash between Unified Technologies and Delta, dated June 26, 2013**	Unified Technologies to provide telecommunications equipment and 5-year warranty support.	N/A	N/A	N/A	N/A	N/A	N/A	Other: We have requested any related agreements from Delta and will update upon receipt.

[16] Capitalized terms used in this Exhibit B but not defined herein have the definitions set forth in the applicable agreement

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4.12.22 4.12.23	**PowerPlant System Perpetual Licensing Agreement between PowerPlan Consultants, Inc. ("PowerPlan") and Delta, dated June 19, 2006** **Amendment #1, dated July 15, 2006** **Amendment #2, dated March 15, 2007** **Amendment #3, dated January 11, 2010** **Amendment No. 4, dated August 14, 2014**	PowerPlan to provide services and software licenses relating to regulatory, accounting, and tax analysis.	Inbound License: PowerPlan grants Delta a perpetual, non-exclusive license to use the software as limited by License Metrics. (§1.1; 4Amdt §1.2)	Termination: Delta may terminate for any reason upon 30 days' prior written notice, provided Delta may only terminate after all fees are paid. (§24.2)	Assignment: Neither party may assign without the prior written consent of the other party, except each party shall be allowed to assign without the other party's consent in the event of a merger, sale of assets or business, or other transfer of control by operation of law or otherwise; provided that in each case the assignee shall assume all obligations and rights under the Agreement. (4Amdt §5)	None	Indemnity: Delta shall indemnify PowerPlan for alleged infringement arising from (a) the combination or use of the Software with hardware, software, or other materials not provided by PowerPlan, (b) the modification of the Software by anyone other than PowerPlan or at PowerPlan's direction, (c) the use of the Software not in accordance with the Documentation or this Agreement, or (d) the use of other than the then most current Version of the Software if the use of the most current Version of the Software would have eliminated the infringement. (4Amdt §8) Limitation on Liability: PowerPlan's liability, in the aggregate shall not exceed the lesser of: (i) the total amounts paid by Delta pursuant to this Agreement; and (ii) the average monthly charges paid by Delta over the last three years multiplied by 12. (§22)	None	Governing Law: Georgia (§6) Other: We have requested the related Maintenance and Support Policies and will update upon receipt.
4.12.3 4.12.14	**Order Form from PowerPlan to Delta, dated October 17, 2014** **Statement of Work between PowerPlan and Delta, dated October 13, 2014**	Order form and work performed for the PowerPlant software upgrade in 2014 that implemented Mobile Approvals and the Regulatory Management Suite.	Subject to terms and conditions of PowerPlant Perpetual Licensing Agreement above.	Term: Initial Maintenance term October, 17 2014 until August 13, 2017	Subject to terms and conditions of PowerPlant Perpetual Licensing Agreement above.	None	Subject to terms and conditions of PowerPlant Perpetual Licensing Agreement above.	None	

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4.12.9	**Statement of Work between PowerPlan and Delta, dated May 17, 2006**	PowerPlan to provide approximately 30 hours of consulting time for troubleshooting.	Subject to terms and conditions of PowerPlant Perpetual Licensing Agreement above.	Subject to terms and conditions of PowerPlant Perpetual Licensing Agreement above.	Subject to terms and conditions of PowerPlant Perpetual Licensing Agreement above.	None	Subject to terms and conditions of PowerPlant Perpetual Licensing Agreement above.	None	
4.12.4	**Diligent Amendment to Service Agreement between Diligent Corporation and Delta, dated October 5, 2015**	Amendment to Diligent Service Agreement	N/A	N/A	N/A	N/A	N/A	N/A	Other: We have requested the Service Agreement from Delta and will update upon receipt.
4.12.5	**Business Services Agreement between Concur Technologies, Inc. ("Concur"), dated April 18, 2016**	Concur to provide expense software and user support for the software.	Inbound License: Concur grants Delta a non-exclusive, nontransferable, worldwide right during the term of the Agreement to access and use the Service for Delta's internal business purposes as contemplated by the Agreement. (§2.1) Outbound License: Delta grants Concur a non-exclusive, nontransferable, worldwide right to use the electronic data specifically pertaining to Delta and/or its users that is submitted into the Service as necessary for the limited purpose of performing the Service. (§2.1) Ownership: Concur retains ownership of all intellectual property. (§2.2)	Term: Initial three month term began April 18, 2016 ("Initial Term"). After Initial Term, the Agreement shall continue until either party terminates with 30 days' written notice to the other party. (§7.1) Termination for Cause: Either party may terminate if there is a material breach by the other party (with a 30 day cure period). (§7.2)	Assignment: The Agreement may not be assigned or transferred by either party without the prior written consent of the other party, which permission shall not be unreasonably withheld; provided, however, that either party may assign the Agreement in whole in connection with any merger or consolidation, provided that, the assignee (i) provides prompt written notice of such assignment, (ii)is capable of fully performing the obligations of the Assignor under the Agreement, and (iii) agrees to be bound by the terms and conditions of the Agreement. (§8.3)	None	Indemnity: Delta must indemnify for third party claims (i) alleging intellectual property infringement due to Delta's data or Delta's use of the Service in violation of the Agreement; or (ii) resulting from the failure of Delta to comply with its obligations under the Agreement. (§5.2) Limitation on Liability: Liability is limited to general money damages, not to exceed the fees paid or owed by Delta in the first twelve months (but not less than the amount of Base Transaction Fees during the first year after the Effective Date). (§4.4)	None	Governing Law: New York (§6.3) Other Restrictions: Delta prohibited from modifying or reverse engineering software. (§2.2)

4.12.6	**Statement of Work to Master Services Agreement and the Addendum for Data and Hosting Service between Delta and Software Systems, LLC ("SIS"), dated July 25, 2014**	SIS is to provide an on-site server to store backups off-site.	N/A	Term: Approximately July 25, 2014 until July 25, 2017 (36 months); subject to automatic successive one-year renewal terms unless written notice of termination is given at least 90 days prior to the end of the then-current term. (§1.1)	N/A	SIS hosted offerings require SIS to retain exclusive administrative rights to all platforms and services unless expressly agreed upon in the detailed description of services. (§1.1)	N/A	N/A	Other: We have requested the related Master Services Agreement and will update upon receipt.
4.12.19	**IBM Maintenance 2014 between Delta and SIS, dated September 2, 2014**	Maintenance for IBM	N/A	Term: November 29, 2014 to November 28, 2017 (3 years)	N/A	N/A	N/A	N/A	Other: We have requested any related agreements to this document.
4.12.7	**Master Services Agreement between NASDAQ OMX Corporate Solutions, LLC ("Corporate Solutions"), dated June 25, 2015**	Corporate Solutions to provide Delta with a NASDAQ standard website with corporate governance hosting.	Ownership: Delta retains all intellectual property rights with respect to Customer Data. Corporate Solutions retains all intellectual property rights in the Service. (§§2.1 and 2.2)	Term: June 25, 2015 to June 25, 2016 (one year); then automatically renewed for successive one-year terms unless written notice of termination is given at least 90 days prior to the end of the Initial Term or any Renewal Term. (§9.1) Termination for Cause: Either Party may terminate (a) upon a material breach of the other party (with a 30 day cure period); or (b) if the other party liquidates, ceases to do business, or becomes insolvent. (§§9.3 to 9.4)	Assignment: Neither Party may assign or transfer this Agreement (including by operation of law), or any of its rights or obligations to a third party without the prior written consent of the other Party, such consent not to be unreasonably withheld. (§11.9)	None	Indemnity: Delta will indemnify for any third-party claim relating to, or arising out of, the Customer Data, including but not limited to, violations of intellectual property rights. (§§16.1 to 16.2) Limitation on Liability: Except with respect to gross negligence or willful misconduct, aggregate liability is limited to the actual fees paid by Delta for the 12-month period preceding the date of the claim. (§4)	None	Governing Law: New York (§11.1) Other: Arbitration in New York, NY (§11.1)

4.12.8	**Agreement for Consulting Services between Delta and TCG America, LLC ("<u>TCG</u>"), dated April 29, 2015**	TCG to provide IT services.	None	<u>Term</u>: April 29, 2015 to April 29, 2016 (one year). (§8.1) <u>Termination for Convenience</u>: Either party may terminate upon 30 days' prior written notice, provided Delta must pay TCG for all charges and expenses incurred before termination. (§8.1) <u>Termination for Cause</u>: Either party may cancel this Agreement upon a material breach of the other party. (§8.1)	<u>Assignment</u>: Neither party may assign this Agreement without the prior written consent of the other party. A sale of substantially all of the assets of a party or a merger is not an assignment. (§8.2)	None	<u>Indemnity</u>: Delta to indemnify TCG for any claim based on Deltas' products or services. (§5.2)	<u>Non-Solicit</u>: Neither party will hire or solicit the employment of any personnel of the other party for a period of 6 months after termination of this Agreement. (§8.7)	<u>Governing Law</u>: Kentucky (§8.4) <u>Other</u>: §5.2 is cutoff but seemed to intend to provide a limitation of liability for Delta.
4.12.10	**Allegro Scope of Services and Software License and Services Agreement between Delta and Allegro Development Corporation ("<u>Allegro</u>"), dated August 10, 2007** **Purchase Order dated July 25, 2007** **Change Order dated August 10, 2007** **Services Exhibit dated March 2, 2009**	Implementation and licensing of the Allegro software.	<u>Outbound</u>: Allegro grants Delta a nonexclusive, nontransferable right to use the software in the object code format. (§1.1)	<u>Term</u>: Perpetual. <u>Termination</u>: If either party materially defaults in its performance, and such default continues for 180 days after written notice is given to the defaulting party, or the defaulting party does not respond in writing to such notice of default, then the non-defaulting party may terminate by giving the defaulting party written notice of the termination. (§7.1)	<u>Assignment</u>: Either party may assign its rights and obligations under the Agreement to: (i) an entity acquiring, directly or indirectly, control of such party, (ii) an entity with which such party is merged, or (iii) an entity acquiring all or substantially all of such party's assets. (§10.6)	None	<u>Limitation on Liability</u>: Allegro's liability for damages is not to exceed the amount of License Fees paid by Delta. (§9.1)	None	<u>Governing Law</u>: Texas (§10.4) <u>Other</u>: Arbitration in Dallas, Texas (§10.5) <u>Other Restrictions</u>: Delta prohibited from modifying or reverse engineering software. (§1.2)

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4.12.11	**AT&T Business Network (ABN) VPN Value Bundle Express Agreement between Delta and AT&T Corp ("AT&T")**	AT&T to provide ABN VPN Value Bundle Express Service.	Software: Any software provided to Delta by AT&T will be governed by the written terms and conditions applicable to such software. (§6.6)	Term: Initial Term of 3 years starting on first day of full billing cycle; then month-to-month, provided either party may terminate via written notice to the other party at least 90 days prior to the expiration date of the Initial Term or then-current Auto-Renewal Period. (§2) Early Termination: If Delta terminates before the expiration of the Term, in addition to liability for all charges incurred through the disconnection the Service, Delta is liable for the following: (i) reimbursements to AT&T for any unrecoverable time and materials costs incurred prior to the effective date of the termination; *plus* (ii) any unpaid nonrecurring charges; *plus* (iii) a termination fee (approximately 50% of the remaining fees for Term). (§5.8)	Assignment: Delta may not assign without the prior written consent of AT&T (such consent not to be unreasonably withheld). (§6.15)	None	Indemnity: Delta agrees to indemnify for third-party intellectual property claims arising out of: (i) Delta's content; (ii) modification of AT&T's Services; (iii) AT&T's adherence to Delta's written requirements; and (iv) use of the Service in violation of this Agreement. (§6.13) Limitation of Liability: Excluding claims arising out of (i) bodily injury, death, or damage to real or tangible property caused by AT&T's negligence, or (ii) third-party indemnification obligations, AT&T's liability is limited to the applicable credits in the specified service publication, or if no credits are specified, an amount equivalent to the proportionate charge to customer for the period of service in which such mistake, omission, interruption, delay, error, or defect in service occurs or continues. (§6.12)	None	Governing Law: Kentucky (§6.15) Other: Unexecuted copy uploaded to VDR; we will update when executed copy is provided in response to our diligence request.

4.12.12 4.12.13	**Blackline Systems Master Subscription Agreement between Delta and Blackline Systems, Inc. ("Blackline"), dated May 28, 2015**	Purchase order for Blackline's Financial Close Management and associated click-wrap agreement to access Blacklines's OnDemand Service.	Inbound License: Blackline grants Delta a non-exclusive, nontransferable, worldwide right to use the Hosted Service, solely for internal business purposes, subject to the terms of the Agreement. (§1) Ownership: Blackline to retain all IP rights in the Hosted Service and with respect to any feedback from relating to the Hosted Service. (§4)	Term: Initial Term is May 29, 2015 to May 29, 2018 (36 months); subject to an automatic 12 month Renewal Term. Delta may terminate in writing 5 business days prior to the expiration of the then-current Term. BlackLine may terminate effective as of the end of the then-current Term by 180 days' advance notice. (Order; §10) Termination for Cause: BlackLine may terminate for any breach of payment obligations, unauthorized use of the service, or any other material breach of the agreement. There is a 15 day cure period for breaches related to intellectual property rights and a 30 day cure period with respect to all other breaches. (§11)	Assignment: Delta does not need Blackline's consent in the case of assignment to (i) a parent or subsidiary; (ii) an acquirer of assets or equity or (iii) a successor by merger. (§19)	None	Indemnity: Delta to indemnify for third-party claims alleging: (i) that use of the Delta Data infringes the Intellectual Property Rights of a third party; (ii) a claim, which if true, would constitute a violation Delta's representations and warranties; or (iii) a claim arising from the breach by Delta or its Users of this Agreement. (§13) Limitation of Liability: Each parties' liability is limited to the actual fees paid by Delta for the 12 month period preceding the event giving rise to such claim. (§16)	None	Governing Law: California (§19) Other Restrictions: Delta is prohibited from modifying or reverse engineering the Hosted Services or copying any ideas, features, functions or graphics of the Hosted Services. (§1)
4.12.15	**Software License and Support Agreement between Delta and Digital Design, Inc. ("DDI"), dated January 22, 2002**	License of printing software and maintenance of the software and printers.	Inbound License: Digital Designs grants Delta a non-exclusive, nontransferable limited license to use the Licensed Software solely on a single computer processing unit. (§I) Ownership: DDI maintains all rights with respect to its custom-developed software. (§I)	Term: Indefinitely (§VII) Termination: Either party can terminate upon a material breach of the other party. (§VII)	Assignment: The agreement cannot be assigned without the prior written consent of DDI (not to be unreasonably withheld). (§VII)	None	Limitation of Liability: Each parties' liability is limited to the actual fees paid by Delta for the 12 month period preceding the event giving rise to such claim. (§IV)	None	Governing Law: North Carolina (§VII) Other Restrictions: Delta prohibited from reverse engineering software. (§I)

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4.12.16	**Software Support Contract between Delta and InsightAlast, LLC ("<u>InsightAlast</u>"), dated January 1, 2017**	Support for E-CIS software.	None	<u>Term</u>: January 1, 2017 to January 1, 2018 (one year); subject to automatic one year renewals unless either party notifies the other party in writing not less than 30 days prior to the expiration of the term of its intent to terminate the contract. (§4) <u>Termination for cause</u>: Either party may terminate after a 30 day cure period if the other party materially defaults on the Agreement. (§§5 to 6)	None	None	None	None	
4.12.17	**Software License Agreement between Delta and Flow-Cal, Inc.("<u>FCI</u>"), dated June 1, 2006**	The software is used to validate, balance, store, and report gas and liquid measurement data.	<u>Inbound License</u>: FCI grants Delta a non-exclusive, non-transferable limited license to use the Flow-Cal System. (§2)	<u>Term</u>: Begins on Effective Date of June 1, 2006 and lasts for 99 years. (preamble)	<u>Assignment</u>: Delta may not assign the Agreement without the consent of FCI. (§16.2)	None	<u>Limitation on Liability</u>: FCI's liability is limited to the fees actually paid by Delta. (§12)	<u>Non-Solicit</u>: Delta shall not make an offer of employment nor enter into a consulting or employment relationship with any employee of FCI for a period of 2 years after termination or expiration of that employee's employment with FCI. (§15)	<u>Governing Law</u>: Texas (§16.6) <u>Other Restrictions</u>: License includes the Flow-Cal Client/Server with one concurrent user, one occasional user, one view-only user and 2 Test-It! Desktops. (Exhibit C)

4.12.17	**Software Subscription Agreement between Delta and FCI, dated June 1, 2006**	Annual maintenance and support for the Flow-Cal software.	Ownership: Any workarounds, fixes, updates, modifications, and/or enhancements to the Flow-Cal System provided to Delta shall remain the property of FCI and shall be licensed in accordance to the Software License Agreement (described above) (§8)	Term: Initial Term of June 1, 2006 to June 1, 2007 (one year); subject to subsequent renewal periods of one year, provided either party may notify the other party of its intent to terminate 30 days prior to the then-current Term or Renewal Term. (§1.1; preamble)	Assignment: Delta may not assign the Agreement without the consent of FCI. (§12.2)	None	Limitation on Liability: FCI's liability is limited to the fees actually paid by Delta. (§12)	Non-Solicit: Delta shall not make an offer of employment nor enter into a consulting or employment relationship with any employee of FCI for a period of 2 years after termination or expiration of that employee's employment with FCI. (§12)	Governing Law: Texas (§12.6)

4.12.21	**The "OrCom Agreement" includes the following exhibits, all of which are between OrCom Systems, Inc. ("OrCom") and Delta, and dated March 6, 1995:** **Exhibit A- General Terms and Conditions** **Exhibit B - OrCom System's Software and Prices** **Exhibit C- Hardware, IBM Software and Prices** **Exhibit D - OrCom Rate Structure** **Exhibit E - Implementation Services** **Exhibit F- Addendum to OrCom Agreement**	OrCom to provide and install hardware and business and accounting related software. OrCom to also provide Extended Support.	Inbound License: OrCom grants Delta a perpetual, nontransferable, non-exclusive license to use the Software on a single IBM AS/400 computer. (Exhibit A §2.1)	Term: Perpetual software license; annual Extended Support. Termination: Delta may discontinue Extended support by 30 days' advance written notice. (Exhibit F §5.3.5) OrCom shall not discontinue Extended Support during first 2 years; thereafter OrCom may discontinue upon 30 days advance written notice. (Exhibit F §5.3.5)	Assignment: Neither party shall sell, assign or otherwise transfer their rights or obligations under this Agreement without the prior written consent of the other party.(Exhibit A §14)	N/A	Limitation on Liability: OrCom's liability is limited to the License Fee. (Exhibit A §8)	Non-Compete: Neither party shall offer employment in any form or manner to any employee of the party during current employment or for one year after termination of employment without the other party's approval. (Exhibit F §13)	Other: On May 6, 2002, Delta consented to OrCom's assignment of its rights and obligations with to its Classic CIS business to Avenir (see below).

4.12.18	**Vendor Software Maintenance Agreement between Avenir Systems LLC ("<u>Avenir</u>") and Delta, dated August 27,2001**	Maintenance for OrCom software.	Subject to OrCom Agreement (§1.4)	<u>Term</u>: Initial Term of January 1, 2001 to December 31, 2001 (one calendar year); subject to subsequent renewal periods of one calendar year, provided either party may send the other a notice of termination at least 60 days before the end of the preceding term. (§§3.1 & 3.2) <u>Termination</u>: Either party may terminate (i) without a cure right for a failure to pay money owed; or (ii) for the other party's nonmonetary default that remains uncured for 30 days after written notice of default from the innocent party. (§3.4) Events of default include: (i) failure to pay; (ii) breach of confidentiality /non-solicitation provisions; or (iii) material breach of any other provision of the Agreement. (§3.5)	<u>Assignment</u>: Neither party may assign without the prior written consent of the other party (not to be unreasonably withheld). (§6.7)	None	<u>Limitation on Liability</u>: Avenir's liability shall not exceed the goods and services provided under the Agreement; provided the limitation does not apply to claims for: (i) breach of confidentiality or improper advertising or publicity; (ii) intellectual property indemnification responsibilities; or (iii) personal injury or damage to real property. (§5.2)	<u>Non-Solicit:</u> Neither party may solicit any person who has been an employee of the other party within the prior 12-month period. (§1.5)	<u>Governing Law</u>: Oregon <u>Other</u>: On May 30, 2002, Delta consented to the assignment of OrCom's rights and obligations related to its Classic CIS business to Avenir under the Software License Agreement, dated March 6, 1995. According to letters posted to the VDR, Harris Computer Systems acquired the Classic CIS Business as of 2005. We have requested that Delta clarify who is currently providing the software maintenance.
4.12.20	**Software License Agreement Exhibit A between KnowledgeLake Inc. ("<u>Knowledgelake</u>") and Delta**	KnowledgeLake to install and implement the additional KnowledgeLake software	N/A	N/A	N/A	N/A	N/A	N/A	<u>Other</u>: We have requested the related agreements and will update upon receipt.

4.12.24	**Master Subscription & Services Order ("SO") between Delta and WebFilings LLC, ("WebFilings")** **Master Subscription & Services Agreement ("MS") between Delta and Webfilings, dated March 27, 2013**	WebsFilings to provide Securities and Exchange Commission ("SEC") Reporting Solution.	Inbound License: WebFilings grants Delta access rights to its Licensed software to be accessed remotely via the internet. (MS §1.1) Ownership: WebFilings retains all ownership of, and all intellectual property rights, in the Licensed Software and all software, equipment, processes, facilities, and materials utilized by or on behalf of WebFillngs to provide the Subscription or Services. (MS §6.1)	Term: Initial Term April 15, 2013 to July 15, 2013 (three months); subject to automatic three month renewals, provided either party may notify the other party that the Agreement will not renew at least 30 days prior to the expiration of the then-current term. (SO §A.1; MS §4.1) Termination for Cause: Either party may terminate upon (i) the other party's insolvency or bankruptcy; or (ii) a material breach. (MS §4.3, §4.5) Termination for Convenience: Delta may terminate upon 30 days' prior written notice, provided Delta will still be responsible for all fees of the then current term. (MS §4.4) WebFilings may terminate on 90 days' prior written notice, provided that it must refund unearned fees within a commercially reasonable time. (MS §4.4)	Assignment: No prior approval is required for an assignment in connection with (i) the sale of all or substantially all of the party's business related to the subject matter of this Agreement, or (ii) any merger, sale of a controlling Interest or other change of control of such party. However, Delta may not assign this Agreement (whether through sale of assets, merger, or change of control) to any WebFilings Competitor. (MS §10.6)	None	Limitation of Liability: WebFilings' liability is limited to the fees paid by Delta for the 12 month period preceding the date on which the claim first accrued. (MS §9.0)	Non-Solicitation: During term of the Agreement and for 1 year after termination or expiration of the Agreement, neither party may directly solicit any of the other's employees for positions of employment or as consultants or independent contractors. (MS §10.6)	Governing Law: California Other restrictions: License is limited to 5 Professional Level Users and 2 Reader Level Users. (SI §D)

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4.12.25	**Subscription Order between Delta and Workiva LLC ("Workiva"), dated September 29, 2014**	Subscription to Wdesk software.	N/A	Term: September 29, 2014 to September 28, 2017 (3 years); subject to automatic 3 year renewals, provided either party may notify the other party that the Agreement will not renew at least 30 days prior to the expiration of the then current Subscription-Term.	N/A	N/A	N/A	N/A	Other: We have requested the related Terms and Conditions and we will update upon receipt.

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EXHIBIT C

Summary of Owned Real Property

[To Come]

EXHIBIT D

Summary of Leased Real Property

[To Come]

January 31, 2017

SteelRiver Operations LP
500 Fifth Avenue, 55th Floor
New York, New York 10110

Subject: **Due Diligence Report**
Evaluation of Project Drake Assets

Ladies and Gentlemen:

Presented herein is Leidos Engineering, LLC's (the "Consultant") due diligence fact sheet (the "Fact Sheet") of our review and analysis of Delta Natural Gas Company, Inc. (the "Assets"), a local distribution company ("LDC") has been prepared in accordance with a Master Professional Services Agreement dated August 30, 2010 and a Task Authorization dated December 23, 2016 (collectively, the "PSA") between the Consultant and SteelRiver Operations LP (the "Client"). The Report is solely for the information of and assistance to Client and should not be relied upon for any other purpose or by any other party, except for those parties who have agreed to the third party use of work products agreement attached to the PSA. The Report has been developed based on the needs of Client, and the level of information included reflects the knowledge of issues gained by Client through the course of our review. To the extent that any other readers of the Report have not been involved over the course of our review, the information contained herein could be incomplete.

The following is to be used only as an indication of our initial findings in support of a potential equity investment into the Assets.

- The LDC describes their system as Northern and Southern sections divided by Jackson County. The customer base is nearly evenly split between the two sections. The compressor and metering stations are located in both sections. The Northern section has the majority of the natural gas connections to the interstate pipelines crossing the area. The Southern section is unique in that it includes:
  - Natural gas production which includes wells owed by the LDC (35) and natural gas provided by outside producers.
  - The Canada Mountain Storage facility which is drawn down during the peak natural gas demand winter season. The storage facility has a working volume of approximately 5.1 billion standard cubic feet.
  - A gas processing plant which removes heavy hydrocarbons from the natural gas (the "Processing Plant"). The Processing Plant is located at the Canada Mountain Storage facility.
- We visited the Canada Mountain Storage and Processing Plant facilities and the Gabbards Fork compressor station on January 19, 2017. The maintenance facilities and equipment appeared neat and well-kept and the sites only had minor housekeeping items for cleanup.
- Table 1 shows the distribution and transmission pipelines and services within the Assets. The miles of main piping shown totals approximately 2,062 miles. The LDC reports that the total piping is approximately 2,600 miles which includes services lines not shown in the table. Table 1 lists the number of potential services available in the system as approximately 41,500. However, the actual number of customers as of mid-2016 was approximately 35,000. The majority of the steel piping is coated and cathodically protected. The LDC has an active program to replace the unprotected bare steel and older plastic piping sections.

Table 1
Distribution and Transmission Mains Gathering Pipelines and Services
End of 2015

	Miles of Mains			
	Distribution	**Transmission**	**Gathering**	**Number of Services**
Unprotected				
Bare Steel	43.76	-	-	1,214
Coated Steel	-	-	-	-
Cathodically-Protected				
Bare Steel	-	-	-	-
Coated Steel	467.56	148.35	7.41	1,676
Plastic, PE	1,382.16		12.98	38,639
Total	**1,893.48**	**148.35**	**20.38**	**41,529**
% of Steel Pipe Protected	91.4%	100%	100%	97.1%

- Table 2 delineates the compressor stations within the assets. The LDC owns a compressor station referred to as "Kettle Island" but this compressor is disconnected from service and is no longer used. Table 2 also lists the compressor operating hours and the percentage the compressors ran for the year 2015. With the exception of the smaller Veach and Woodbine compressor stations, all the stations ran for significantly less time than their maximum capability which allows for scheduled maintenance without impacting the operations of the system.

Table 2
Compressor Station Summary

							Operating Time	
Station	**County**	**No. of Units**	**Make**	**Horse-power**	**Capacity (1) (MMCFD)**	**In-Service Year**	**Hours**	**% of Max**
Canada Mtn	Bell	5	Ajax	2,065	26 to 43	1986-2013	29,852	68
East/West	Bell	1	Ajax	400	3.9-6.2	2006	4,120	47
Flat Lick	Knox	2	Ajax, Ariel	392	2.4 to 4.1	1986	5,108	29
Gabbard Fork	Clay	3	Ajax	1,600	16-34	2008-2012	9,019	34
Johnson	Whitley	3	Ajax, Waukesha	940	7.4-13.1	1986	483	2
Liford	Whitley	1	Ajax	80	0.25-0.45	1986	4,971	57
Rader Creek	Clay	1	Ajax	200	2.1-3.4	2003	0	0
Red Lick	Estill	3	Ajax	1,200	14-24	2006-2007	9,287	35
Veach	Whitley	1	Quincy (2)	10	0.02-0.05	2008	8,284	95
Woodbine	Whitley	1	Ajax	80	0.25-0.45	1986	8,715	99
Total		**22**		**7,316**			**79,839**	**41**

(1) Compressor capacities vary depending on the pressure requirements.
(2) Veach Station compressor is electric driven. All other compressors are gas driven.

- The assets also include 505 metering stations. The LDC reports that the metering stations are inspected annually as required per state federal regulations.

- Based on our conversations with the LDC, the system Assets are not currently reaching their equipment or pipeline capacity limits. If, in the future, the LDC were to expand production in the Southern system to provide additional natural gas to the Northern system the Gabbards Fork compressor station would be the first bottleneck followed by the 8-inch transmission pipeline from Gabbards Fork to the Red Lick compressor station.

- The Processing Plant has a maximum capacity of approximately 15 million standard cubic feet per day ("MMCFD") of raw gas while producing 8,000 to 10,000 gallons of liquid recovered per day depending on the gas composition. The Processing Plant removes water from the natural gas and uses propane refrigeration to reduce the gas temperature to approximately 12 degrees Fahrenheit to condense the heavy hydrocarbons. The maximum

Processing Plant capacity recorded in the period July 2013 through September 2016 was approximately 241 MMCF per month (7.8 MMCFD). The most recent time this maximum rate was achieved was in May 2015. The Processing Plant removed heavy hydrocarbons which reduced the gas flow rate to approximately 215 MMCF that month (7.2 MMCFD).

- The LDC gas tariff reports the LDC will typically supply natural gas with a heating value of approximately 1,070 British thermal units per standard cubic foot ("Btu/CF") having a specific gravity of approximately 0.62. The LDC has reported average historic system natural gas heating values and specific gravities that generally correspond with the typical tariff values. The LDC limits the amount of hydrogen sulfide ("H2S") in their system to less than 4 parts per million. The H2S enters the system from contact with the water in the storage field and is present in the gas produced from the wells and from gas provided by third parties. The third party natural gas producers are responsible for reducing the H2S content of the gas they sell into the system. The LDC monitors the H2S level in the gas from their production wells and from the storage field. Wells that are found to be producing high levels of H2S are injected with a scavenger chemical that reacts with the H2S and removes it from the natural gas.
- The Canada Mountain storage field has seven withdrawal wells. The total withdrawal rate becomes limited as the storage field pressure is reduced and gas from three of the wells is blocked or "watered over" by the rising water level. The LDC has a current program in place to drill a new well with an extended horizontal reach that is to be above the upper water levels in the field. The new well would increase the withdrawal capacity and overall working volume of the field.
- Provided (1) all equipment comprising the Assets is operated in accordance with manufacturer recommendations and company policies; (2) all such equipment continues to be maintained consistent with generally-accepted engineering practices, including the provisions for recommended major maintenance; and (3) all required renewals and replacements are made on a timely basis, the equipment and technology utilized by the Assets represent a sound, proven method of natural gas distribution and is consistent with our expectations based on our experience with local distribution companies.
- Historical and projected performance of the Assets is as summarized in Table 3 below.

Table 3
Gas Volumes and Unaccounted-For
(MMCF, Unless Otherwise Noted)

Regulated	**2013 (1)**	**2014**	**2015**	**2016 (2)**	**Average (3)**	**Projection**
Distribution	888	3,566	3,536	2,566	3,248	2,989
On System Transportation	2,526	4,798	5,181	3,774	5,009	5,181
Off-System Transportation	5,692	11,402	11,868	9,300	11,773	11,868
Non-Regulated						
Delgasco	N/A	N/A	N/A	6,698	N/A	6,361
Delta Resources	N/A	N/A	N/A	738	N/A	740
Processing Plant						
Gas Received	1,323	2,496	2,229	1,834	2,425	N/A
Residue Gas	N/A	N/A	1,787 (4)	1,644	2,167	N/A
Liquids Recovered (Thousand gallons)	1,371	2,240	1,986	1,454	2,227	2,071
Total System						
LUG (5)	1,320	957	511	517 (6)	775	
LUG as % of Receipts	3.69	4.43	2.47	2.66 (6)	3.24	

(1) Data provided from July 2013 through December 2013.
(2) Data provided from January 2016 through September 2016.
(3) Average based on historical monthly average multiplied by 12 months.
(4) Data provided from February 2015 through December 2015.
(5) Lost and Unaccounted for Gas ("LUG").
(6) Twelve months ended September 2016.

- LUG typically averages between approximately 2.5 and 4.5 percent. According to the Owner, the Kentucky Public Service Commission ("PSC") does not have a mandate for maximum LUG level, however, historical precedence is for the PSC to limited LUG to less than 5 percent.

- Table 4 lists the system leaks over the past three years.

Table 4
System Leaks

2014	Distribution Main	Gathering Line	Meter Installation	Regulator Station	Service Line	Transmission Line	Total
Leak Class 1							
Reported	85	-	15	-	118	-	218
Repaired	85	-	15	-	118	-	218
Unrepaired	-	-	-	-	-	-	-
Leak Class 2							
Reported	47	-	10	-	24	2	83
Repaired	50	-	10	-	26	2	88
Unrepaired	19	-	-	-	3	-	22
Leak Class 3							
Reported	24	-	46	5	28	2	105
Repaired	36	-	44	3	25	1	109
Unrepaired	44	-	4	2	9	5	64
2015							
Leak Class 1							
Reported	77	2	22	-	137	5	243
Repaired	77	2	22	-	137	5	243
Unrepaired	-	-	-	-	-	-	-
Leak Class 2							
Reported	55	5	7	-	27	1	95
Repaired	60	1	7	-	25	1	94
Unrepaired	14	4	-	-	5	-	23
Leak Class 3							
Reported	15	-	40	3	12	2	72
Repaired	22	-	44	4	19	4	93
Unrepaired	37	-	-	1	2	3	43
2016							
Leak Class 1							
Reported	73	-	16	1	127	1	218
Repaired	73	-	16	1	127	1	218
Unrepaired	-	-	-	-	-	-	-
Leak Class 2							
Reported	45	6	12	-	33	3	99
Repaired	45	10	12	-	30	4	101
Unrepaired	17	-	-	-	7	-	24
Leak Class 3							
Reported	11	-	19	-	14	-	44
Repaired	15	-	16	-	12	2	45
Unrepaired	32	-	3	1	3	-	39

- As is typical for LDCs, the majority of the Class 1 leaks were found in the services lines. All Class 1 leaks were repaired the same year they were discovered.

- The sections of Owner's pipelines that are catholically protected use a combination of impressed current and sacrificial anodes – need to confirm they use both, which is typical of LDC's with which we are familiar. Cathodic protection is typically included in the PSC inspections. The PSC inspection reports provided for the past three years state that no deficiencies were identified.

- The Processing Plant averaged 99.3 percent availability in 2016, including scheduled and unscheduled maintenance. While 2015 availability data was not provided for our review, the Owner did state that the Processing Plant was shutdown for approximately 6 weeks from August 2015 to September 2015 as a result of a damaged mist eliminator. The extended outage was due to a delay in receiving the replacement part. During that time, the Owner took

advantage of the fact that the plant was down and performed some routine maintenance on the plant. The Owner has stated that it has not experienced any other extended unplanned outages on the Processing Plant.

- Table 5 below shows the historical average compressor station availability for 2016, including scheduled and unscheduled maintenance. Compressor station availability has averaged over 99 percent for all compressor stations in 2016.

Table 5
Compressor Station 2016 Availability

Station	Average Availability (%)
Canada Mountain	99.8
East/West	99.9
Flat Lick	99.9
Gabbard Fork	99.8
Johnson	100.0
Liford	99.9
Rader Creek	99.7
Red Lick	99.7
Veach	99.9
Woodbine	99.8

- Table 6 lists the historical O&M expenses for the Assets as shown in the provided file "*7.12.1 O&M History – July 2013 – Nov 2016.xlsx*" and the projected expenses as provided in the file "*7.12.2 O&M Projection by Month.xlsx*". The historical O&M expenses shown in Table 6 for the FY 2014 is greater by approximately $2 million than the value given in the LDC provided ("Financial Model") "*7.4.6 Drake Model_vF.xlsx" tab "Assumptions Back-up*" due to the Financial Model not correctly accounting for the property and payroll taxes (decimal place error).

Table 6
Historical O&M Expenses
($000)

	FY 2014 [1]	FY 2015 [2]	FY 2016 [3]	YTD Nov 2016 [4]	Historical Average [5]	Projected
Fixed, $000						
Labor	6,957	7,071	7,331	3,009	7,130	7,523
Employee Benefits	2,779	2,573	2,860	1,295	2,806	2,740
Outside Services	3,897	2,836	2,089	1,226	2,937	1,423
Property Taxes	1,733	2,169	2,319	919	2,080	2,353
Transportation	1,121	987	852	328	969	896
General Administration	747	925	938	551	905	1,044
Insurance	756	799	828	347	799	857
Other	723	695	703	243	689	756
Payroll Taxes	591	627	646	248	624	630
Administrative	519	473	445	163	472	515
General Operations	394	395	409	178	399	425
Customer Billing	355	348	348	135	352	348
Uncollectible Accounts	107	161	238	(26)	169	142
Mains	56	61	65	36	62	60
Meter & Regulators	49	47	39	21	45	48
Expenses Transferred	(5,497)	(4,546)	(3,879)	(1,655)	(4,555)	(3,904)
Subtotal	**15,287**	**15,620**	**16,231**	**7,017**	**15,882**	**15,854**
Incentive Compensation	2,045	1,238	291	32	1,092	45
Subtotal Fixed	**17,333**	**16,858**	**16,522**	**7,050**	**16,974**	**15,898**
Variable, $000						
General Operations	186	207	169	73	193	219
Labor	168	188	149	50	168	0
Other	133	151	115	49	131	174
Subtotal Variable	**487**	**546**	**433**	**172**	**492**	**393**
Total	**17,820**	**17,404**	**16,955**	**7,221**	**17,466**	**16,291**
Variable, $/mcf						
General Operations	0.008	0.009	0.007		0.008	0.010
Labor	0.007	0.008	0.007		0.007	0.000
Other	0.006	0.007	0.005		0.006	0.008
Total Variable	**0.022**	**0.024**	**0.019**		**0.022**	**0.019**

(1) Data provided for fiscal year 2014 from July 2013 through June 2014.
(2) Data provided for fiscal year 2015 from July 2014 through June 2015.
(3) Data provided for fiscal year 2016 from July 2015 through June 2016.
(4) Data provided for July 2016 through November 2016.
(5) Calculated using the historical monthly average and multiplying by 12.

- The LDC Financial Model Projected O&M expenses are based on the 2017 budget. However, when compared to the previous three (3) years of operations we note that the historical average is approximately 7 percent more than the projected expenses for total O&M costs. The lower projected O&M expenses are mainly due to a decreased budget for Incentive Compensation, which, according to the Owner, is an optional expense based on exceeding projected financial performance. If we remove this expense, the total projection is consistent with the historical average total. Based on our review and adjusting for the Incentive Compensation expense, the projected O&M expenses should be sufficient to operate the LDC.
- Table 7 lists the historical capital expenditures for the Assets.

Table 7
Historical Capital Expenditures
($)

	FY 2015 (1)	FY 2016 (2)	Projected
Gathering	N/A	63,707	N/A
Storage	N/A	188,305	N/A
Transmission	N/A	536,783	N/A
Distribution	N/A	3,971,618	N/A
Other	N/A	1,343,520	N/A
Total Capital Expenditures	**7,929,271**	**6,103,932**	**8,518,000**

(1) Data provided for fiscal year 2015 from July 2014 through June 2015
(2) Data provided for fiscal year 2016 from July 2015 through June 2016.

- Based on our review of the limited capital expenditure data provided, the magnitude of, and trends evident in, historical capital expenditures are consistent with the operation of the systems and the projected capital expenditures are consistent with historical.
- The Owner's rate case approved by the PSC includes a pipeline replacement ("PRP") rider, which allows the Owner to receive a fixed rate of return on capital spent for pipeline replacement. Historically, the Owner has averaged PRP costs of approximately $2,418,000 per year since 2010. The Owner is using the historical average as the basis for PRP projected yearly costs, which is consistent with our expectations and the Owner's current pipeline replacement plan of approximately 8 miles per year of both bare steel and plastic (specifically Aldyl-A plastic, which has been determined in the industry to have a higher risk of leaks and ruptures). Although the PRP costs are required to be approved by the PSC the year following pipeline installation, according to the Owner, there is theoretically no maximum for the PRP yearly costs. Therefore, the Owner could potentially accelerate the pipeline replacement program while still earning a fixed return on the capital incurred.
- Following our review of the Integrity Management Programs ("IMP") of the Assets the (1) Owner's Distribution IMP ("DIMP") appears to cover the requirements of 49 CFR 192 for natural gas distribution systems, including the Simple Handy Risk-based IMP ("SHRIMP"), which is a recent addition for distribution systems; (2) the Owner's transmission IMP ("TIMP") appears to also cover the requirements of 49 CFR 192 for natural gas transmission systems and identifies two high consequence areas ("HCA") for a total of 2,403 feet throughout the transmission system; (3) audits performed by the PSC completed since 2013 show no identified deficiencies, and (4) direct assessments of the transmission pipeline completed in 2016 showed no measureable indication of internal or external corrosion of the transmission pipelines.
- As part of our review with respect to Environmental, Health, and Safety ("EH&S"), Leidos personnel reviewed documents provided in the data room established by the company and visited the Canada Mountain Storage and Processing Plant and the Gabbard's Fork Compressor Station on January 19, 2017. From this review, it appears that the environmental functions are handled within the engineering group and operations personnel are made aware of various requirements. The specific structure of the safety organization was not presented or reviewed. There is a noticeable absence of information on the company website, and within materials reviewed, to indicate that EH&S is a significant focus and an important part of corporate culture. However, it does appear that the company is generally aware of EH&S requirements and has the staff to stay abreast of applicable requirements and maintain compliance. Items to note with respect to EH&S follow.
  - The sites visited were somewhat remote with no observed neighbors or sensitive receptors nearby. The sites were fenced and appeared secure.
  - A Standard Practices document for Spill Prevention Control and Countermeasure ("SPCC") Plans from 2010 was included in the data room. Regulations and applicability have changed since this date and an examination of the specific requirements pertaining to the company facilities should be conducted to determine whether any of the recent changes affect company facilities. Leidos did not evaluate the requirement for SPCC Plans at individual facilities.
  - Company personnel reported that Occupational Safety and Health Administration ("OSHA") programs were in place as required. It was also reported that there are currently some significant changes and modifications being made to these programs. The reason for these changes was not determined, but no issues of significance were reported during the site visit or observed in the data room.

- Vents to discharge natural gas during emergencies at the Gabbard's Fork Compressor Station were only about six feet above ground level. Company personnel indicated it was not possible for the vents to discharge with personnel in the vicinity. Further investigation into the purpose and operation of these vents should be conducted and it would likely be prudent for the height of the discharge to be raised.
- Overall, the two sites visited appeared generally as expected for facilities associated with hydrocarbon production, treating, and compression. There were some noticeable stains and a few housekeeping areas that may need some attention, but nothing appeared significantly out of order.
- Based on information provided during the site visit and information included the data room, it appears that the current owners are generally aware of the regulations and the requirements for obtaining permits and authorizations required for operation of the facilities, and that the required permits and authorizations have either been obtained or are in the process of being obtained. We note that the data room contained permits for five compressor stations, and we were informed that authorizations for four additional sites are in process, with some being only registrations. It appears that some of these authorizations may now be finalized and included in the data room.
- No significant compliance issues were made known during the site visit, and a high level review of the data room did not reveal any such issues.
- The company reports that all facilities are currently in compliance with applicable environmental requirements, including submittal of compliance reports and annual fees. It was reported during the site visit that the last few inspections from the Kentucky Division of Air Quality ("DAQ") indicted there were no identified issues. We note that an air quality environmental audit conducted by Kenvirons, Inc. at the Woodbine, Rader Creek, and East/West Compressor Stations and summarized in letters dated August 8, 2016, indicates that DAQ registrations were required under 401 KAR 52:070 in order to comply with the requirements of 40 CFR 63, Subpart ZZZZ. It is believed that the required authorizations for those, and possibly other, facilities were subsequently submitted to DAQ. There was no indication during the site visit that, since some facilities were apparently constructed and in operation without the required permits or registrations in place, that there would be compliance action taken by DAQ.
- During the site visit at Canada Mountain, it was observed that glycol dehydrator reboiler vents discharged to the atmosphere. Company personnel stated that, other than compressor exhaust, there were no other regulated emission points at the facilities. This may be the case. However, it may be wise to look into whether there are any requirements for these vents to be controlled and/or whether there are sufficient hydrocarbon losses to warrant recovery for product or fuel gas. It is also noted there are some atmospheric tanks receiving water and possibly hydrocarbons from system pressure (approx. 600 psi) that may need vapor recovery or at least further investigation.

Respectfully submitted,

LEIDOS ENGINEERING, LLC