COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN INVESTIGATION OF THE IMPACT OF THE TAX	**)**	
CUTS AND JOB ACT ON THE RATES OF ATMOS	**)**	
ENERGY CORPORATION, DELTA NATURAL GAS	**)**	
COMPANY, INC., COLUMBIA GAS OF KENTUCKY,	**)**	**CASE NO. 2017-00481**
INC., KENTUCKY-AMERICAN WATER COMPANY,	**)**	
AND WASTE SERVICE CORPORATION OF	**)**	
OF KENTUCKY	**)**	

DIRECT TESTIMONY OF

MATTHEW D. WESOLOSKY

January 25, 2018

Q. Please state your name and business address.

A. My name is Matthew D. Wesolosky. My business address is 3617 Lexington Road, Winchester, Kentucky, 40391.

Q. By whom and in what capacity are you employed?

A. I am employed by Delta Natural Gas Company, Inc. as its Vice President - Controller.

Q. Please describe your professional and educational background.

A. I received a Bachelor's of Science in Accounting from the University of Kentucky in 1999. I am a Certified Public Accountant in the State of Kentucky. From 1998 through 2001, I worked at Delta as the Accounting Systems Analyst/Coordinator. From 2001 through 2005 I worked in public accounting including two years at PricewaterhouseCoopers specializing in the utilities industry. From 2005 through 2007 I worked at Delta as the Manager – Internal Controls. From 2007 through 2010 I worked as the Manager – Accounting & IT. Beginning in 2010 I became Delta's Vice President-Controller.

Q. Generally, what are your duties at Delta?

A. As Vice President – Controller, I am responsible for Delta's accounting and IT functions, which include income tax accounting and compliance.

Q. Please describe your previous professional experience with Delta.

A. Prior to leading the accounting and IT functions, I was primarily responsible for the monitoring and evaluation of Delta's internal controls. I reported to and acted on behalf of

Delta's Audit Committee to assist in the Committee's oversight of Delta's corporate governance. I also assisted in directing the Company's programs for compliance under Section 404 of the Sarbanes-Oxley Act of 2002 and assisted in coordination of the audit performed by our independent certified public accountants, Deloitte. As the Accounting Systems Analyst/Coordinator, my primary responsibility was to assist in the integration of the accounting and information technology departments.

Q. Please describe your public accounting experience related to the utilities industry.

A. I was a senior associate with PricewaterhouseCoopers from 2003-2005. During this time, I primarily worked on the financial audits for E.ON U.S. and its subsidiaries (Louisville Gas and Electric Company, and Kentucky Utilities Company), Western Kentucky Energy Corp. and the internal control audit for Southwest Power Pool. I was in charge of planning and managing the audit fieldwork as well as focusing on industry specific issues dealing with regulatory accounting, energy trading and ISO transactions.

Q. Have you been a witness in matters previously before the Commission?

A. Yes, I have been a witness on behalf of Delta in the following proceedings:

- Case No. 2007-00089, *Application of Delta Natural Gas Company, Inc. for an Adjustment of Rates,*
- Case No. 2008-00062, *Application of Delta Natural Gas Company, Inc. for Approval of a Customer Conservation/Efficiency Program and Demand Side Management Cost Recovery Mechanism,*

- Case No. 2010-00116, *Application of Delta Natural Gas Company, Inc. for an Adjustment of Rates,*
- Case No. 2012-00136, *Application for Adjustment of the Pipe Replacement Program Rider of Delta Natural Gas Company, Inc.*,
- Case No. 2013-00101, *Application for Adjustment of the Pipe Replacement Program Rider of Delta Natural Gas Company, Inc.*,
- Case No. 2013-00365, *Application of Delta Natural Gas Company, Inc. For an Order Declaring That it is Authorized to Construct, Own and Operate a Compressed Natural Gas Station in Berea, Kentucky,*
- Case No. 2014-00072, *Application for Adjustment of the Pipe Replacement Program Rider of Delta Natural Gas Company, Inc.*,
- Case No. 2015-00066, *Application for Adjustment of the Pipe Replacement Program Rider of Delta Natural Gas Company, Inc.*,
- Case No. 2016-00110, *Application for Adjustment of the Pipe Replacement Program Rider of Delta Natural Gas Company, Inc.*,
- Case No. 2017-00111, *Application for Adjustment of the Pipe Replacement Program Rider of Delta Natural Gas Company, Inc.*,
- Case No. 2017-00125, *Electronic Joint Application of PNG Companies LLC, Drake Merger Sub Inc. And Delta Natural Gas Company, Inc. for Approval of an Acquisition of Ownership and Control of Delta Natural Gas Company, Inc.*

Q. Are you generally familiar with the business affairs of Delta?

A. Yes, I am.

Q. Please summarize the scope of your testimony.

A. My testimony provides the estimated impact the federal income tax legislation enacted on December 22, 2017, commonly referred to as the Tax Cuts and Jobs Act ("TCJA"), will have on Delta's financial operations and customer rates.

Q. Are you familiar with Delta's tax and accounting records?

A. Yes.

Q. How will the TCJA impact Delta?

A. With the TCJA being signed into law on December 22, 2017, Delta is still evaluating the provisions of the law and its impact on Delta. However, the most significant provision of the tax law is the reduction of the corporate income tax rate to 21%.

Q. How will the corporate income tax rate reduction impact customer rates?

A. Delta's rates are cost-of-service rates that allow Delta the opportunity to recover reasonable operating costs, as well as the opportunity for its investors to earn a fair rate of return on invested capital. Income tax expense is included in the calculation of Delta's cost of service. Delta's current rates are designed to recover income tax expense assuming a 34% federal rate. Therefore, pursuant to the Commission's order in this case, Delta's rates should be reduced on a prospective basis to reflect the impact of the TCJA.

Q. Is the tax savings to be realized the 13% difference between the prior 34% rate and the new 21% rate, multiplied by the historical test period's net income before taxes?

A. No. Although the rate federal corporate income tax rate decreased 13%, the reduction was partially offset by the benefit received from deducting state income taxes on Delta's federal income tax return.

The benefit from deducting state income taxes is reduced as a result of the decreased federal income tax rate, as described later in this testimony. Additionally, the TCJA's elimination of bonus depreciation and other changes to deferred income taxes including the amortization of excess deferred taxes negatively impact cash flow and thus will increase Delta's cost of capital.

Q. How did Delta calculate the impact the TCJA will have on customer rates?

A. Please refer to Schedule MDW – 1 which summarizes the estimated impact the TCJA will have on customer rates. The federal corporate income tax rate change impacts the tax expense included in Delta's revenue requirement. Reductions in tax expense are expected due to the application of a lower tax rate to current period operations, as well as due to the amortization of existing excess deferred tax liabilities, resulting in a reduction in deferred tax expense.

Q. How did Delta calculate the revenue requirement impact?

A. Delta utilized a historic test period, where the actual net income before taxes for the twelve months ended September 30, 2017 was adjusted to create a regulatory net income before taxes.

Income tax expense is calculated at the statutory rate, which is the combined federal and state income tax rates adjusted for the federal benefit of the state tax deduction. Schedule MDW- 2 shows the calculation of the statutory rate with the prior 34% federal corporate tax rate, as well as the new 21% corporate tax rate. With the TCJA, Delta's statutory rate has decreased 12.22% from 37.96% to 25.74%.

The income tax expense adjustment calculates income tax expense by multiplying regulatory net income before taxes by both the pre and post-TCJA statutory rates of 37.96% and 25.74%, respectively. The difference between the two results in a decrease to income tax expense.

To determine the adjustment to the revenue requirement, the decrease in income tax expense is grossed-up at the 25.74% statutory rate. The result is an adjustment of approximately $1.5 million to Delta's revenue requirement on an annual basis.

Q. Does the adjustment to the revenue requirement impact Delta's earnings?

A. No. The decrease to the revenue requirement is offset by the income tax benefit it generates making the adjustment earnings neutral, as shown in the mathematical proof on Schedule MDW- 2.

Q. Are expenses related to the merger with PNG Companies LLC and Drake Merger Sub included in the determination of regulatory net income before taxes?

No. Consistent with prior practice in rate cases, Delta has removed the impact of non-operating income and expense from determining the impact on the revenue requirement. Included in this category of expenses are the merger-related costs incurred during the test period. Pursuant to the regulatory commitments in Case No. 2017-00125, Delta will not seek to recover costs associated with the transaction in rates. Therefore, these expenses have been excluded so the tax benefit of the merger expenses does not impact the income tax expense adjustment to cost of service.

Q. Other than the merger costs, were adjustments made to income or expense items on a prospective basis?

A. No. Pursuant to the Commission's order, the issues in this case are limited to the savings resulting from the TCJA. All adjustments made to arrive at regulatory net income before taxes represent recurring adjustments utilized in Delta's general rate cases. The adjustments normalize the financial results to the extent actual weather in the test period deviated from the thirty-year average and excludes specific classes of income and expense which Delta has not historically included in the determination of its revenue requirement.

Q. How does the corporate income tax rate reduction impact Delta's deferred income taxes?

A. Under the Accounting Standards Codification *Topic 740 – Income Taxes*, deferred tax assets and liabilities are measured at the currently enacted tax rate expected to apply to taxable income in the period in which the deferred tax liability or asset is expected to be settled or realized. When there is a change in the tax rate, deferred tax assets and liabilities are adjusted in the period in which the change in the applicable tax rate is enacted into law. Prior to enactment of the TCJA, Delta's deferred tax assets and liabilities were measured at a statutory rate assuming a 34% corporate income tax rate. As it closes its books for December 2017, Delta intends to remeasure its deferred taxes using the 25.74% statutory rate which assumes the new 21% corporate federal income tax rate.

Q. What impact does remeasurement of deferred income taxes have on customer rates?

A. For non-regulated entities, the remeasurement of deferred income taxes results in deferred tax expense or benefit in the period of enactment that is allocated to income from continuing operations. However, regulated entities can be required by their regulator to refund through future rates the portion of deferred taxes recovered from customers based on the higher pre-TCJA tax rates. These deferred taxes to be refunded to customers are defined as excess deferred income taxes and recorded as a regulatory liability in the period of enactment.

Q. How did Delta calculate its excess deferred taxes resulting from the TCJA?

A. For estimation purposes, Delta utilized its deferred taxes as of September 30, 2017. As of September 30, 2017, Delta's estimated cumulative timing differences between financial reporting and income tax purposes were multiplied by the 37.96% statutory rate to calculate the deferred taxes as of September 30, 2017. Schedule MDW – 3 calculates excess deferred taxes as the difference between measuring the September 30, 2017 cumulative timing differences at the prior 37.96% statutory rate versus the new 25.74% statutory rate. This difference of approximately $14.2 million represents an estimation of the excess deferred taxes to be refunded to Delta's customers.

Q. Does Delta have any other excess deferred taxes? If so, how are those impacted by the corporate income tax rate change?

A. Delta has excess deferred taxes resulting from the Kentucky corporate income tax rate change where rates decreased from 8% to 6% for Delta's 2005 to 2007 tax years. The remaining unamortized excess deferred income taxes resulting from the change in the Kentucky corporate tax rate remain unchanged as they remeasured Delta's deferred income taxes down to the 37.96% statutory rate. However, as the excess deferred income taxes are amortized under the new federal corporate income tax rate, less of a gross-up is required on the excess deferred income taxes. Therefore, the deferred tax gross-up on the 2005 regulatory liability has been remeasured at the new 25.74% statutory rate as shown on Schedule MDW-3.1.

Q. Do the excess deferred taxes represent the liability Delta owes its customers for the deferred taxes recovered at higher corporate income tax rates?

A. The excess deferred taxes represent a portion of the liability owed to customers. However, similar to the adjustment of income tax expense, excess deferred taxes require gross-up at the new statutory rate of 25.74%. Please refer to Schedule MDW - 4 for a calculation of the liability.

Q. Is $19.2 million the actual amount to be refunded to customers?

A. No. It is an estimate based on September 30, 2017 amounts. December 31, 2017 cumulative timing differences must be known for the calculation to reflect the actual amounts due to customers.

Q. When will Delta know the exact amount of its cumulative timing differences for the tax year ended December 31, 2017?

A. In closing the books for December, cumulative timing differences between calculating income for financial reporting and income tax purposes will be estimated. However, the exact amounts will not be known until Delta files its corporate tax return in October of 2018.

Q. What is the journal entry to record excess deferred taxes?

A. Under Accounting Standards Codification *Topic 980 - Regulated Operations*, when it is probable that the future decrease in taxes payable will be returned to customers through future rates, a regulatory liability shall be recognized for that probable reduction in future revenue. That asset or liability also shall be a temporary difference for which a deferred tax liability or asset shall be recognized. Please refer to Schedule MDW - 5 for the estimated journal entry to record the excess deferred taxes.

Q. Does Delta agree it should return the excess deferred income taxes to customers over a twenty year period?

A. No. the TCJA specifically addresses the return of excess deferred income taxes in a manner similar to the Tax Reform Act of 1986. Section 13001 (d) of the TCJA discusses normalization requirements where the reserve for excess deferred income taxes cannot be reduced more rapidly or to a greater extent than such reserve would be reduced under the average rate assumption method ("ARAM").

Q. What is the impact if Delta does not conform to the normalization requirements?

A. Failure to comply with the normalization requirements results in a utility's tax liability for a given year to increase by the amount which it reduced its excess tax reserve in excess of the amount permitted under the normalization rules. In addition, the utility becomes ineligible to deduct accelerated depreciation for federal income tax purposes and instead may only deduct the amount of depreciation expensed for regulatory reporting purposes.

Q. Can Delta amortize the excess deferred taxes over a twenty year period?

A. No. Section 13001 (d) of the TCJA precludes a taxpayer from reducing its excess deferred income taxes more rapidly or to a greater extent than such would be reduced under ARAM. Under ARAM, as described in Section 13001(d)(3)(B) of the TCJA, "the excess reserve for deferred taxes is reduced over the remaining lives of the property as used in its regulated books of account which gave rise to the reserve for deferred taxes." Twenty years would be more rapid than allowed.

Q. How did Delta calculate the amortization of excess deferred?

A. Delta engaged tax consultants to study Delta's book and tax depreciation records and develop an amortization schedule under ARAM. However, it was determined that Delta's property records for income tax purposes do not contain a sufficient level of detail to calculate the amortization under ARAM.

The normalization rules, however, permit an entity without sufficient records to calculate amortization of excess deferred income taxes under ARAM to utilize the Reverse South Georgia Method, referred to as the Alternative Method in the TCJA, which amortizes the excess deferred taxes ratably over the remaining life of the utility's assets. Delta estimates the remaining life of its utility assets to be 21 years. Schedule MDW - 4 shows the amortization of excess deferred income taxes over this period. This manner of amortization is consistent with the method of amortization of excess deferred taxes approved in Case No. 9785, *The Effects of the Federal Tax Reform Act of 1986 on the Rate of Delta Natural Gas Company, Inc.* and the amortization of 2005 excess deferred income taxes included in Case No. 2007-00089, *Application of Delta Natural Gas Company Inc. for an Adjustment of Rates*.

Q. Why is Delta proposing an adjustment for increased cost of capital?

A. Tax return deductions related to capital expenditures provide a utility with a zero cost of capital source of financing. To the extent the corporate income tax rate decreases or deductions related to capital expenditures are limited or disallowed, the decrease in tax benefit decreases the zero cost of capital financing available to a utility. Under the TCJA, both the loss of bonus depreciation and the decrease in the tax rate mean that Delta's tax benefit from these deductions will decrease; therefore, increasing Delta's annual cost of capital. Schedule MDW – 6 compares the tax effect of the capital expenditure related deductions as calculated on Delta's 2017 fiscal year-end income tax return with what that same deduction would be under the TCJA. The difference between the two, plus the amortization of excess deferred income taxes, results in reduced cash flow which increases Delta's capital requirements. The incremental capital requirement is then multiplied by the actual test year weighted average cost of capital for Delta and grossed-up for income taxes to calculate the test year impact the TCJA has on cost of capital.

Q. How much does Delta estimate its customers rates would be reduced on an annual basis for both changes in the revenue requirement and amortization of excess deferred income taxes?

A. Schedule MDW - 1 shows the combined estimated impact of all the adjustments to be $2.2 million. Delta proposes to refund retail and on-system transportation customers a portion of the monthly customer charge in the following amounts:

Residential $3.29

Small Non-Residential $6.26

Large Non-Residential $46.92

Interruptible $318.48

However, Delta proposes that the rate would be adjusted to actual amounts once actual amount of excess deferred income taxes are known and the 2017 tax return is filed.

Q. How did Delta determine the amount to refund to each customer class?

A. Delta allocated the amount to be refunded to each customer class in the same manner in which it allocates rates under its annual Pipe Replacement Program ("PRP") filing. The allocation, as shown on Schedule MDW -1, is based on the class allocations used in the cost of service study from Delta's last general rate case.

Q. How would Delta reflect such charge on a customer's bill?

A. Delta proposes to have a separate line item on the monthly bills for Residential, Small Non-Residential, Large Non-Residential, Interruptible and On-System Transportation. Such refund would be included on the bills until the earlier of Delta's next general rate case when the impact of the new tax rate will be included in the base rate calculations or further change in federal or Kentucky corporate tax rates.

Q. Does the change in federal corporate tax rate impact any periodic filings Delta makes with the Commission?

A. Yes. Delta's annual PRP filing includes a return grossed up for income taxes which assumes a 34% federal corporate income tax rate and the 37.96% statutory rate used to compute the deferred tax liability impact on PRP rate base.

Q. Does the revenue requirement adjustment discussed earlier in this testimony include amounts billed under the PRP?

A. Yes. The adjustment to tax expense includes all regulated pre-tax income during the test period, so earnings generated under the current PRP rates are being adjusted through the proposed rates. Additionally, the calculation of excess deferred taxes discussed previously in this testimony included all PRP property. Thus, no adjustment to current PRP rates is needed. However, the PRP filing for 2018 would include a revised tax gross-up factor and statutory rate to calculate deferred income taxes for post 2017-PRP vintages. All prior PRP vintages would remain unchanged as they have been considered in the calculation described in this testimony.

Q. Does this conclude your testimony at this time?

A. Yes. However, Delta respectfully requests the Commission to allow Delta the opportunity to supplement the record if additional factors or information that might affect customer rates but were not previously considered in this testimony, come to light as Delta continues to review the TCJA. Examples include, but are not limited to, the issuance of clarifying guidance by the Internal Revenue Service and adjustments to deferred tax balances identified during the preparation of the 2017 tax return.

VERIFICATION

COMMONWEALTH OF KENTUCKY)
) SS:
COUNTY OF CLARK)

The undersigned, Matthew D. Wesolosky, being duly sworn, deposes and says that he is Vice President - Controller of Delta Natural Gas Company, Inc. and that he has personal knowledge of the matters set forth in the foregoing testimony, and the answers contained therein are true and correct to the best of his information, knowledge and belief.

Matthew D. Wesolosky

Subscribed and sworn to before me, a Notary Public, in said County and State this 26th day of January 2018.

Donna K. Fuller (SEAL)
Notary Public

My Commission Expires:

July 11, 2020

Donna K. Fuller
Notary Public, ID No. 558932
State at Large, Kentucky
My Commission Expires on July 11, 2020

Delta Natural Gas Company, Inc.
Case No. 2017-00481
Schedule MDW-1
Calculation of Customer Rate Reduction
Test Period: September 30, 2017

Annual impact of rate change on:		
Adjustment to income tax expense	(1,450,715)	Schedule 2
Amortization of regulatory liability - 2005 rate change	11,412	Schedule 3.1
Amortization of regulatory liability - 2018 rate change	(915,171)	Schedule 4
Adjustment to cost of capital	202,137	Schedule 6
	(2,152,337)	

		Calculated Net Revenue @ Approved Rates per Case No. 2010-00116	Class Allocation		Allocated Tax Adjustment	# of Customers for the 12 months ended September 30, 2017		Monthly per Customer Tax Reduction Rate
Residential	$	14,846,218	54.3%	$	(1,169,205)	355,300	$	(3.29)
Small Non-Residential		3,991,286	14.6%	$	(314,331)	50,181		(6.26)
Large Non-Residential		7,008,122	25.6%	$	(551,920)	11,763		(46.92)
Interruptible		1,484,119	5.4%	$	(116,881)	367		(318.48)
	$	27,329,745	100.0%	$	(2,152,337)	417,611		

Delta Natural Gas Company, Inc.
Case No. 2017-00481
Schedule MDW-2
Tax Expense Impact

Cost of Service

	9/30/2017	
Net income before taxes	4,651,289	
Recurring historic rate case test year adjustments		
Adjust net revenue to normal weather	1,330,610	Schedule 2.1
Exclude impact of unbilled revenue, net of unbilled gas cost	(115,169)	
Lobbying (1.930.12)	8,810	
Advertising (1.913.00)	250	
Public and community relations (1.930.10)	13,133	
Marketing (1.930.04)	4,060	
Non-operating (income) expense, incl merger-related costs	2,922,903	
Regulatory net income before taxes	8,815,886	
Statutory rate	37.96%	
Income tax expense, at statutory rate	(3,346,510)	
Regulatory net income	5,469,376	

Calculation of Statutory Rate

Federal	34.0%	21.0%
State	6.0%	6.0%
Federal benefit of state tax (Federal Rate * 6%)	-2.0%	-1.3%
Statutory rate	37.96%	25.74%

Calculation of Gross-Up Factor

	34.0%	**21.0%**
$\frac{1}{1 - (\text{Statutory Rate})}$	1.6118633	1.3466200

Income Tax Expense Adjustment and Proof

Income tax expense at 37.96%	(3,346,510)
Income tax expense at 25.74%	(2,269,209)
Difference	(1,077,301)
Gross-up factor, at new rates	1.3466200
Income tax expense impact to revenue requirement	(1,450,715)

Mathematical Proof

9/30/17 Net Income Before Taxes	8,815,886	
Income tax expense adjustment to revenue requirement	(1,450,715)	Schedule 1
Net Income before taxes, adjusted	7,365,171	
January 1, 2018 statutory rate	25.74%	
Income tax expense, adjusted	(1,895,795)	
Net income, after rate change	5,469,376	
Net income, before rate change	5,469,376	
Difference	(0)	

Delta Natural Gas Company, Inc.
Case No. 2017-00481
Schedule MDW-2.1
Natural Gas Temperature Normalization Adjustment
For the 12 months Ended September 30, 2017

	Cycle Billing Basis	Calendar Basis
Normal Heating Degree Days	4,527	4,528
Actual Heating Degree Days	3,476	3,494
Normal over (under) Actual	1,051	1,034

	Cycle Billing Basis
Normal Heating Degree Days **(7 Non-WNA Months)**	769
Actual Heating Degree Days **(7 Non-WNA Months)**	381
Normal over (under) Actual	388

	Meter Reading Basis	(A) Total Mcf	(B) Non-Temp Mcf	(C) Non-Temp Mcf Full Year	(D) Temperature Sensitive Mcf (Column (A) - (C))	(E) Actual Degree Days	(F) Mcf per Degree Days (Column (D) / (E))	(G) Normal Degree Days	(H) Departure From Normal (Column (G) - (E))	(I) Normal Temperature Adjustment (Column (F) x (H))	(J) Net Revenue Per Mcf Sold	(K) Net Revenue Adjustment (Column (I) x (J))
General Service												
Residential	Cycle Billing	225,417 {1}	45,453 {3}	159,086 {4}	66,332	381	174	769	388	67,512	$ 4.3185	$ 291,551
Small Non-Residential	Cycle Billing	88,525 {1}	21,536 {3}	75,376 {4}	13,149	381	35	769	388	13,580	$ 4.3185	$ 58,645
Large Non-Residential	Cycle Billing	770,971 {2}	56,174 {3}	337,044 {5}	433,927	3,476	125	4,527	1,051	131,375	$ 4.3185	$ 567,343
Interruptible Service	Cycle Billing	20,951 {2}	1,226 {3}	7,356 {5}	13,595	3,476	4	4,527	1,051	4,204	$ 1.6000	$ 6,726
Transportation												
Small Non Residential	Calendar	16,206 {2}	139 {3}	834 {5}	15,372	3,494	4	4,528	1,034	4,136	$ 4.3185	$ 17,861
Large Non Residential	Calendar	1,522,662 {2}	203,294 {3}	1,219,764 {5}	302,898	3,494	87	4,528	1,034	89,958	$ 4.3185	$ 388,484
Residential	Calendar	1,279 {2}	2 {3}	12 {5}	1,267	3,494	-	4,528	1,034	-	$ 4.3185	$ -
		2,646,011	327,824	1,799,472	846,540					310,765		$ 1,330,610

Schedule 2

{1} Seven months May to November, as December through April is billed through Delta's Weather Normalization Adjustment

{2} Twelve months ended September 30, 2017

{3} Non-temperature sensitive MCF is the MCF billed during the months of July and August

{4} (Column (B) x 6) * 7/12

{5} Column (B) x 6

Delta Natural Gas Company, Inc.
Case No. 2017-00481
Schedule MDW-3
Remeasurement of Deferred Taxes

	9/30/2017 Cumulative Timing Difference	**Deferred Rate**	**Deferred 9/30/2017 Balance**	**New Statutory Rate**	**Remeasured Deferred at New Rate**	**Estimated Excess Deferred Taxes {1}**
Cost of Service Items						
1.242.13 DEF INC TAX DEFERRED GAS COST	(2,778,483)	37.96%	(1,054,712)	25.74%	(715,182)	(339,530)
1.242.14 DEF INC TAX BAD DEBT RESERVE	156,133	37.96%	59,268	25.74%	40,189	19,079
1.242.18 DEF INC TAX MEDICAL RESERVE	70,857	37.96%	26,897	25.74%	18,239	8,658
1.242.19 DEF INC TAX PROFESSIONAL FEES	188,400	37.96%	71,517	25.74%	48,494	23,023
1.242.22 DEF INC TAX ACCRUED VACATION	29,943	37.96%	11,366	25.74%	7,707	3,659
1.282.02 DEF INC TAX PENSION PLAN	(3,334,906)	37.96%	(1,265,930)	25.74%	(858,405)	(407,525)
1.282.06 DEF INC TAX ANNUAL LEAVE PLAN	668,961	37.96%	253,938	25.74%	172,191	81,747
1.283.03 DEF INC TAX SUPPLEMENTAL RETIREMENT PLAN	1,257,584	37.96%	477,379	25.74%	323,702	153,677
			(1,420,277)		(963,065)	(457,212)
Rate Base Items						
1.242.16 DEF INC TAX PREPAID INS	(974,787)	37.96%	(370,029)	25.74%	(250,910)	(119,119)
1.282.01 DEF INC TAX ACCEL DEPR - FEDERAL	(106,326,946)	34.00%	(36,151,162)	21.00%	(22,328,659)	(13,822,503)
1.282.01 DEF INC TAX ACCEL DEPR - STATE	(89,585,696)	3.96%	(3,547,594)	4.74%	(4,246,362)	698,768
1.282.07 DEF INC TAX CONSTRUCTION CONTRIBUTIONS	44,364	37.96%	16,841	25.74%	11,419	5,422
1.282.10 DEF INC TAX DEBT EXPENSE	(2,414,057)	37.96%	(916,376)	25.74%	(621,378)	(294,998)
1.282.12 DEF INC TAX STORAGE GAS	102,814	37.96%	39,028	25.74%	26,464	12,564
1.282.14 DEF INC TAX ASSET RETIREMENT OBLIGATION	3,493,275	37.96%	1,326,047	25.74%	899,169	426,878
1.282.18 DEF INC TAX COST OF REMOVAL	(2,334,280)	37.96%	(886,093)	25.74%	(600,844)	(285,249)
1.283.06 DEF INC TAX ARO REG ASSET	(2,973,010)	37.96%	(1,128,555)	25.74%	(765,253)	(363,302)
1.283.07 DEF INC TAX ARC DEPRECIATION	(597,211)	37.96%	(226,701)	25.74%	(153,722)	(72,979)
1.283.10 DEF INC TAX - 2005 KY RATE CHANGE		{2}	122,738	25.74%	122,738	-
			(41,721,856)		(27,907,338)	(13,814,518)
Total Deferred Taxes			**(43,142,133)**		**(28,870,403)**	**(14,271,730)**

{1} Actual excess deferred taxes will be updated upon filing 12/31/17 tax return

Schedule 4 & 5

{2} see schedule 3.1 for calculation of deferred tax balance

Delta Natural Gas Company, Inc.
Case No. 2017-00481
Schedule MDW-3.1
Remeasurement of Existing Excess Deferred Income Taxes
2005 Kentucky Income Tax Rate Change

Remeasurement of Regulatory Liability for 2005 Rate Change

Gross excess deferred taxes on 2005 KY rate change	837,300
Less: amortization to date	(483,200)
Excess deferred taxes, net of amortization	354,100
Regulatory liability	
(excess deferred taxes, net / (1 - 37.96%)	(570,761)
(excess deferred taxes, net / (1 - 25.74%)	(476,838)
Deferred income taxes on	
2005 KY reg liability, at new rates	122,738

Adjustment to 2005 Regulatory Liability

Kentucky 2005 Income Tax Rate Change	**Balance September 30, 2017**	**Remeasured**	**Adjustment Required**
Excess deferred income taxes	354,100	354,100	-
Deferred tax asset on reg liability	216,661	122,738	(93,923)
Regulatory liability	(570,761)	(476,838)	93,923

Tax Expense Impact from Remeasuring 2005 Regulatory Liability

Remeasured regulatory liability	(476,838)	
Remaining amortization, months	203	
Monthly amortization (credit to income tax expense)	2,349	
Remeasured annual amortization	28,188	
Annual pre-TCJA amortization	39,600	
Difference	(11,412)	Schedule 1

Delta Natural Gas Company, Inc.
Case No. 2017-00481
Schedule MDW-4
Measurement of Excess Deferred Income Taxes - 2018 Income Tax Rate Change

2018 Federal Income Tax Rate Change		
Gross excess deferred taxes	14,271,730	Schedule 3
Regulatory liability		
(excess deferred taxes/ (1 - 25.74%)	(19,218,597)	
Deferred income tax gross-up on regulatory liability	4,946,867	
Weighted average remaining life of assets	21	years
Annual amortization of excess deferred taxes into tax expense	679,606	
Annual adjustment of excess deferred taxes to revenue requirement	(915,171)	Schedule 1

Delta Natural Gas Company, Inc.
Case No. 2017-00481
Schedule MDW-4.1
Proposed Amortization Schedule

	Regulatory Liability				Deferred Taxes on Reg Liability				
	Beginning Balance	Amortization into Tax Expense	Ending Balance		Beginning Balance	Amortization into Tax Expense	Ending Balance	% of Reg Liability	Tax Expense
12/31/2017			(19,218,597)	{1}			4,946,867	-25.74%	
2018	(19,218,597)	915,171	(18,303,426)	{2}	4,946,867	(235,565)	4,711,302	-25.74%	(679,606)
2019	(18,303,426)	915,171	(17,388,255)		4,711,302	(235,565)	4,475,737	-25.74%	(679,606)
2020	(17,388,255)	915,171	(16,473,084)		4,475,737	(235,565)	4,240,172	-25.74%	(679,606)
2021	(16,473,084)	915,171	(15,557,913)		4,240,172	(235,565)	4,004,607	-25.74%	(679,606)
2022	(15,557,913)	915,171	(14,642,742)		4,004,607	(235,565)	3,769,042	-25.74%	(679,606)
2023	(14,642,742)	915,171	(13,727,571)		3,769,042	(235,565)	3,533,477	-25.74%	(679,606)
2024	(13,727,571)	915,171	(12,812,400)		3,533,477	(235,565)	3,297,912	-25.74%	(679,606)
2025	(12,812,400)	915,171	(11,897,229)		3,297,912	(235,565)	3,062,347	-25.74%	(679,606)
2026	(11,897,229)	915,171	(10,982,058)		3,062,347	(235,565)	2,826,782	-25.74%	(679,606)
2027	(10,982,058)	915,171	(10,066,887)		2,826,782	(235,565)	2,591,217	-25.74%	(679,606)
2028	(10,066,887)	915,171	(9,151,716)		2,591,217	(235,565)	2,355,652	-25.74%	(679,606)
2029	(9,151,716)	915,171	(8,236,545)		2,355,652	(235,565)	2,120,087	-25.74%	(679,606)
2030	(8,236,545)	915,171	(7,321,374)		2,120,087	(235,565)	1,884,522	-25.74%	(679,606)
2031	(7,321,374)	915,171	(6,406,203)		1,884,522	(235,565)	1,648,957	-25.74%	(679,606)
2032	(6,406,203)	915,171	(5,491,032)		1,648,957	(235,565)	1,413,392	-25.74%	(679,606)
2033	(5,491,032)	915,171	(4,575,861)		1,413,392	(235,565)	1,177,827	-25.74%	(679,606)
2034	(4,575,861)	915,171	(3,660,690)		1,177,827	(235,565)	942,262	-25.74%	(679,606)
2035	(3,660,690)	915,171	(2,745,519)		942,262	(235,565)	706,697	-25.74%	(679,606)
2036	(2,745,519)	915,171	(1,830,348)		706,697	(235,565)	471,132	-25.74%	(679,606)
2037	(1,830,348)	915,171	(915,177)		471,132	(235,565)	235,567	-25.74%	(679,606)
2038	(915,177)	915,177	-		235,567	(235,565)	2	0.00%	(679,612)

{1} Will be adjusted to actual once 12/31/17 tax return is completed and filed

{2} Will begin amortization in the month rates become effective and amortize for 252 months (21 years)

Delta Natural Gas Company, Inc.
Case No. 2017-00481
Schedule MDW-5
Estimated Journal Entries

2017 Federal Income Tax Rate Change

Deferred income tax assets and liabilities	14,271,730
Deferred income tax asset on reg liability	4,946,867
Regulatory liability	(19,218,597)

estimated remeasurement of deferred income taxes resulting from change in tax law

2005 Kentucky Income Tax Rate Change

Deferred income tax asset on reg liability	(93,923)
Regulatory liability	93,923

estimated remeasurement of existing excess deferred income taxes resulting from change in tax law

Delta Natural Gas Company, Inc.
Case No. 2017-00481
Schedule MDW-6
Cost of Capital Impact

Tax return deduction related to capital expenditures including depreciation

	2017 Fiscal Tax Return		Under TCJA	
Deduction	(8,751,150)		(6,645,248)	{1}
	37.96%		25.74%	
Tax benefit of plant-related deductions	(3,321,937)		(1,710,487)	
Decreased deduction	(1,611,450)			
Annual refund of excess deferred taxes, under TCJA	(915,171)	Schedule 4		
Annual incremental capital requirements due to change in tax law	(2,526,621)			
Actual test year cost of capital	6.6804%			
Increased cost of capital	(168,789)			
Allocated Cost of Capital:				
Equity (57%)	(96,210)			
Debt (43%)	(72,579)			
Tax gross-up factor	1.346620			
Equity component of cost of capital (grossed-up)	(129,558)			
Debt component of cost of capital	(72,579)			
Adjustment for cost of capital	(202,137)	Schedule 1		

{1} Difference between the two amounts represents the loss of bonus depreciation