Business Valuation of
Southern Water and Sewer District
As of June 28, 2018

Prepared for:

Dean Hall
President
Southern Water and Sewer
245 Kentucky Rt 680
McDowell, WV 41647
United States

Report Date:

10/31/2018

Prepared by:

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President
The Fyffe Jones Group
2155 Carter Avenue
Ashland, Kentucky 41105-2245
United States

10/31/2018

Dean Hall
President
Southern Water and Sewer
245 Kentucky Rt 680
McDowell, WV 41647
United States

RE: Southern Water and Sewer District

Dear Dean Hall:

At your request, we have performed a valuation engagement, as defined in the Statement on Standards for Valuation Services (SSVS) of the American Institute of Certified Public Accountants. The valuation is for lost revenues of Southern Water and Sewer District's as of June 28, 2018. This valuation was performed solely to assist in the matter of Support Existing Sale and Transfer and the resulting estimate of value should not be used for any other purpose or by any other party for any purpose. This valuation engagement was conducted in accordance with the SSVS. The estimate of value that results from a valuation engagement is expressed as a conclusion of value.

We have estimated the Fair Market Value on a controlling interest, marketable basis for lost revenues of Southern Water and Sewer District's as of June 28, 2018 as described within the valuation report.

Our conclusion is $4,020,000 as summarized below. This conclusion is subject to the Statement of Assumptions and Limiting Conditions and the Representations presented in the following report. We have no obligation to update this report or our conclusion of value for information that comes to our attention after the date of this report.

In arriving at this opinion of value, we relied on a “value in use” or going-concern premise. This premise assumes that the Company is an ongoing business enterprise with management operating in a rational way with a goal of maximizing entity value.

As part of this report, we were also asked to opine on the viability of both Southern Water and Sewer District and Prestonsburg City’s Utilities Commission after the transfer. See opinion at the end of this report.

Respectfully,

____
(Signature)

____
(Date)

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Valuation Objective and Summary

Assignment Objective

We were engaged by Dean Hall, President, Southern Water and Sewer, to issue a detailed report. Our objective was to estimate the Fair Market Value of lost revenues due to a transfer of customer accounts and related assets of Southern Water and Sewer District's system as of June 28, 2018.

Company Description

Southern Water and Sewer District is a Non-Profit and is organized under the laws of Kentucky. It is primarily engaged in the business of Water Distribution and is doing business as Southern Water District.

Qualifications of Appraiser

This report was prepared by Terry R. Fyffe President of The Fyffe Jones Group. Terry R. Fyffe holds the following professional designations and certifications: CPA, ABV.

Purpose of Valuation

The purpose of this valuation is Support Existing Sale and Transfer of customer accounts and related assets. This report is prepared for Dean Hall President Southern Water and Sewer and should not be used by others without his consent. This report is dated 10/31/2018.

Standard of Value

The standard of value used in our valuation of Southern Water and Sewer District is *Fair Market Value*. Fair Market Value is defined in IRS Revenue Ruling 59-60 as: "The price at which the property would change hands between a willing buyer and a willing seller when the former is not under any compulsion to buy and the latter is not under any compulsion to sell, both parties having reasonable knowledge of relevant facts. Court decisions frequently state in addition that the hypothetical buyer and seller are assumed to be able, as well as willing, to trade and to be well informed about the property and concerning the market for such property."

Premise of Value

Our opinion of value relied on a "value in use" or going-concern premise. This premise assumes that the Company is an ongoing business enterprise with management operating in a rational way with a goal of maximizing shareholder value.

Scope of Work

Our analysis considers those facts and circumstances present at the Company at the Valuation Date. Our opinion would most likely be different if another Valuation Date was used. There were no restrictions or limitations in the scope of our work or in the data available for analysis, and no hypothetical assumptions were used.

The factors we considered include the history of the business, economic outlook, financial condition of the business, earnings and dividend paying capacity, book value of the stock and the size of the block being valued, prior sales of the Company's stock, goodwill and intangible value, and the market prices for publicly traded and privately held companies in the same or similar line of business.

Valuation Procedures

To arrive at our conclusion of value, we performed the following procedures:

* Identified the nature of the business and reviewed the history of the Company since its inception.
* Researched the general economic outlook and the outlook for the specific industry at the date of the valuation.
* Collected the Company's relevant historic financial statements.
* Assisted management in preparing a 5 year projection of the lost revenue based on management's assumptions as to the Company's future outlook.
* Developed risk-adjusted Capitalization and Discount Rates to apply to the Company's historic and projected earnings, respectively.
* In reaching the conclusion of value, we considered the Asset, Income, and Market valuation approaches and the following methods under each approach.

    1. Asset Approach

       Net Asset Value.

    2. Income Approach

       Discounted Future Earnings/Discounted Cash Flow.

    3. Market Approach

       No comparable data was available.

* Selected the most reasonable enterprise-level equity value from the range of values established in the valuation methods
* Applied any appropriate enterprise-level discounts and/or premiums to arrive at an enterprise-level equity value.

External Sources of Information

To aid us in our analysis of the Company, we consulted a number of publicly available sources of information. Numerous financial publications and databases were consulted including *Business Statistics*, Standard & Poor's *Industry Surveys*, Ibbotson Associates' *Stocks, Bonds, Bills and Inflation 200X Yearbook*, *Mergerstat Review*, *U.S. Financial Data*, Standard & Poor's *Register of Corporations, Directors, and Executives*, Disclosure, Inc. on-line database, and *Value Line Investment Survey*.

Internal Sources of Information

To aid us in our analysis of the Company, we interviewed and obtained the following:

1. Site Visit with Eddie Campbell.
2. Kentucky Public Service Commission report on the rate increase filing by Southern.
3. Various Return on Equity including Kentucky American Water Company summary.
4. Telephone conversation with Floyd County Judge Executive Ben Hale.
5. Telephone conversation with Southern Water President Dean Hall.
6. Financial Statements from Prestonsburg City Utilities.
7. Lost revenues and related costs from the PSC report..
8. Lost revenues and related costs estimates from Prestonsburg City Utilities.

Assumptions and Limiting Conditions

This valuation is subject to the following assumptions and limiting conditions:

1. Public, industry, statistical, and other information furnished by others, upon which all or portions of this analysis is based, is believed to be reliable. However, we make no representation as to the accuracy or completeness of such information and have performed no procedures to corroborate the information.

2. The Company and its representatives warranted to us that the information they supplied was complete and accurate to the best of their knowledge and that the financial statement information reflects the Company's results of operations and financial and business condition in accordance with generally accepted accounting principles, unless otherwise noted. The financial statements and other related information supplied by management has been accepted as correct without further verification. We have not audited, reviewed, or compiled the financial information provided to us and, accordingly, we express no audit opinion or any other form of assurance on this information.

3. This report and conclusion of value is restricted to the internal use of the management of the Company for the sole and specific purpose as noted herein, and shall not be used to obtain credit or for any other purpose or by any other party for any purpose. Neither our work product nor any portions thereof, including any conclusions or the identity of our firm, any individuals signing or associated with this report, or the professional associations or organizations with which they are affiliated, shall be disseminated to third parties other than the Company, its financial accounting firm and attorneys, and governmental agencies by any means without our prior written consent and approval.

4. We or any individual associated with this assignment are not required to provide future services regarding the subject matter of this report, including but not limited to providing further consultation, providing testimony, or appearing in court or other legal proceedings unless specific arrangements have been made.

5. The conclusion of value is valid only for the stated purpose as of the valuation date indicated. We take no responsibility for changes in market conditions and assume no obligation to revise our conclusion of value to reflect events or conditions which occur subsequent to the valuation date.

6. Full compliance by the Company with all applicable federal, state, and local zoning and use, occupancy, environmental, and similar laws and regulations is assumed, unless otherwise stated. Furthermore, no effort has been made to determine the possible effect, if any, on the Company due to future Federal, state, or local legislation including any environmental or ecological matters or interpretations thereof, unless otherwise stated.

7. This report and the conclusion of value arrived at herein are not intended by the author and should not be construed by the reader to be investment advice in any manner whatsoever. The conclusion of value represents the considered opinion of The Fyffe Jones Group based on information furnished to them by the Company and other sources.

8. We do not provide assurance on the achievability of the results forecasted by the Company because events and circumstances frequently do not occur as expected; differences between actual and expected results may be material; and achievement of the forecasted results is dependent on actions, plans, and assumptions of management.

9. For the prospective financial information approved by management that was used in our engagement, we have not examined or compiled the prospective financial information and therefore, do not express an

audit opinion or any other form of assurance on the prospective financial information or the related assumptions. Events and circumstances frequently do not occur as expected and there will usually be differences between prospective financial information and actual results, and those differences may be material.

10. We are not environmental consultants or auditors, and we take no responsibility for any actual or potential environmental liabilities. Any person entitled to rely on this report, wishing to know whether such liabilities exist, or the scope and their effect on the value of the property, is encouraged to obtain a professional environmental assessment. We do not conduct or provide environmental assessments and have not performed one for the subject property.

11. We have not determined independently whether the Company is subject to any present or future liability relating to environmental matters, including but not limited to CERCLA/Superfund liability, nor the scope of any such liabilities. Our valuation takes no such liabilities into account, except as they have been reported to us by the Company or by an environmental consultant working for the Company, and then only to the extent that the liability was reported to us in an actual or estimated dollar amount. Such matters, if any, are noted in the report. To the extent such information has been reported to us, we relied on it without verification and offer no warranty or representation as to its accuracy or completeness.

12. Except as noted, we have relied on the representations of the owners, management, and other third parties concerning the value and useful condition of all equipment, real estate, and any other assets or liabilities, except as specifically stated to the contrary in this report. We have not attempted to confirm whether all assets of the business are free and clear of liens and encumbrances or that the Company has good title to all assets.

13. Neither all nor any part of the contents of this report (including the conclusion of value, the identity of any valuation specialist(s), the firm with which such valuation specialists are connected, or any reference to any of their professional designations) should be disseminated to the public through advertising media, public relations, news media, sales media, mail, direct transmittal, or any other means of communication without our prior written consent and approval.

14. We have not made a specific compliance survey or analysis of the subject property to determine whether it is subject to, or in compliance with, the American Disabilities Act of 1990, and this valuation does not consider the effect, if any, of noncompliance.

15. No change of any item in this valuation report shall be made by anyone other than , and we shall have no responsibility for any such unauthorized change.

16. We have not conducted interviews with the current management of the Company concerning the past, present, and future operating results of the Company.

17. This conclusion of value assumes that the Company will continue to operate as a going concern, and that the character and integrity of the Company through any sale, reorganization, exchange, or diminution of the owners' participation would not be materially or significantly changed. It also assumes that the current level of management expertise and effectiveness would continue to be maintained.

Company Background

Company Identification

Southern Water and Sewer District is a Non-Profit organized under the laws of Kentucky and located at 245 Kentucky Rt 680, McDowell, KY, 41647.

Nature and History of the Company

Southern Water and Sewer District was established in 1999 and operates under the trade name of Southern District.

The following table describes the business activities in which Southern Water and Sewer District is engaged:

Business Activity	Description
Primary Business Activity	Water Distribution
Secondary Business Activity	Sewer Treatment

Governmental or Regulatory Environment

The District is subject to the Kentucky Public Service Commission. A rate increase was requested to replace the lost revenue from the transfer of certain customers and associated assets to Prestonsburg City Utilities by contract effective June 28, 2018. The PSC approved the rate increase for more than what Southern Water had applied for. The PSC performed a two tier approach in arriving at their decision, and our valuation utilized the detailed info prepared by them.

Business Risks

The District has additional risks associated with aged lines and sewer treatment plant. Regulatory pressures have been assessed to improve both. Therefore, additional risk assessments have been made in building the Cost of Capital and Discount Rate.

Current Operations

This valuation only includes specific loss of revenues identified by the transfer of customers and associated assets outlined in the June 28, 2018 agreement. However, the PSC report was relied upon in determining the viability of Southern Water District

Company Expectations

The Southern Water District expects to continue to be viable after the transfer given the PSC rate increase and the reduction of debts afforded by proceeds from the contract dated June 28, 2018.

National Economic and Industry Conditions

General Economic Conditions and Outlook

The U.S. economic outlook is healthy according to experts. That's because the GDP growth rate will be between the 2 percent to 3 percent ideal range. Unemployment will continue at the natural rate. There isn't too much inflation or deflation. That's a Goldilocks economy.

Donald Trump promised to increase economic growth to 4 percent. That could create the irrational exuberance that creates damaging booms and busts.

U.S. GDP growth will rise to 2.1 percent in 2017. That's better than the 1.9 percent estimated for 2016 and the same as 2015's growth rate of 2.1 percent. The increase in gross domestic product will remain at 2.1 percent in 2018 and drop to 1.9 percent in 2019. That's according to the most recent forecast released at the Federal Open Market Committee meeting on March 15, 2017. That begins to take into account the impact of Trump's policies.

The unemployment rate will drop to 4.5 percent in 2017 and beyond. That's better than the 4.7 percent rate in 2016, and the Fed's 6.7 percent target. Most job growth is in low-paying retail and food service industries. Many people have been out of work for so long that they'll never be able to return to the high-paying jobs they used to have. That means structural unemployment increased. Federal Reserve Chair Janet Yellen admits a lot of workers are part-time and would prefer full-time work. That makes the unemployment rate seem artificially low. She considers the real unemployment rate to be more accurate. That rate is usually double the official rate.

Inflation will be 1.9 percent in 2017 and 2.0 percent in 2018 and beyond. These rates are higher the 1.5 percent rate in 2016, and the 0.7 percent inflation experienced in 2015. Both were caused by low oil prices. The core inflation rate (without gas or food prices) will be 1.9 percent in 2017 and 2.0 percent in 2018 and beyond. That's close to the Fed's 2.0 percent target inflation rate.

U.S. manufacturing is forecast to increase faster than the general economy. Production will grow 3 percent in 2017, and 2.8 percent in 2018. Growth will slow to 2.6 percent in 2019 and 2 percent in 2020.

Interest Rates

The FOMC first raised the Fed funds rate to 0.5 percent in December 2015 and raised interest rates again in December 2016 to 0.75 percent. It expects the rate to rise to 1.5 percent in 2017, 2 percent in 2018 and 3 percent in 2019. The fed funds rate controls short-term interest rates. These include banks' prime rate, the LIBOR, most adjustable-rate and interest-only loans, and credit card rates.

The Fed said it would start selling $4 trillion in Treasuries after the Fed funds rate has normalized to about 2.0 percent. The Fed acquired these securities during quantitative easing, which ended in 2014. When it does start selling them, there will be more supply. That should raise the yield on the 10-year Treasury note. That drives up long-term interest rates, such as fixed-rate mortgages and corporate bonds. But Treasury yields also depend on demand for the dollar. If demand is high, yields will drop, and vice-versa. As the global economy improves, demand for this ultra-safe investment is falling. As a result, long-term and fixed interest rates will rise in 2017 and beyond.

Oil and Gas Prices

The U.S. Energy Information Administration outlook is from 2017-2040. It predicts crude oil prices will average $55/barrel in 2017. That's for Brent global. West Texas Crude will average around $1/barrel or less.

The EIA warned that commodities traders believe prices will range between $45/b and $65/b for April 2017 delivery. Prices will rise to $57/b in 2018. (Source: "Short-Term Energy Outlook," EIA, November 8, 2016)

A strong dollar continues to depress oil prices. That's because oil contracts are priced in dollars. Oil companies are laying off workers, and some may default on their debt. High-yield bonds funds are doing poorly as a result.

The oil market is still responding to the impact of U.S. shale oil production. That reduced oil prices 25 percent in 2014 and 2015. The good news for the economy is that it also lowered the cost of transportation, food, and raw materials for business. That raised profit margins. It also gave consumers more disposable income to spend. The slight slowdown is because both businesses and families are saving instead of spending.

By 2020, the average oil price will rise to $76.57/b (in 2015 dollars, which removes the effect of $136.21/b in 2040. By then, the cheap sources of oil will have been exhausted, making crude oil production more expensive. (Source: "Annual Energy Outlook," EIA, July 7, 2016.)

Jobs

The Bureau of Labor Statistics publishes an outlook for U.S. employment each decade. It goes into great detail about each industry and occupation. Overall, the BLS expects total employment to increase by 20.5 million jobs from 2010-2020. While 88 percent of all occupations will experience growth, the fastest growth will occur in healthcare, personal care and social assistance, and construction. Furthermore, jobs requiring a master’s degree will grow the fastest while those that only need a high school diploma will grow the slowest. (Source: BLS Occupational Outlook Summary)

The BLS assumes that the economy will fully recover from the recession by 2020 and that the labor force will return to full employment or an unemployment rate between 4-5 percent. The biggest growth (5.7 million jobs) will occur in healthcare and other forms of social assistance as the American population ages.

The next largest increase (2.1 million jobs) will occur in professional and technical occupations. Most of this is in computer systems design, especially mobile technologies, and management, scientific, and technical consulting. Businesses will need advice on planning and logistics, implementing new technologies, and complying with workplace safety, environmental, and employment regulations.

Other substantial increases will occur in education (1.8 million jobs), retail (1.7 million jobs) and hotel/restaurants (1 million jobs). Another area is miscellaneous services (1.6 million jobs). That includes human resources, seasonal and temporary workers, and waste collection.

As housing recovers, construction will add 1.8 million jobs while other areas of manufacturing will lose jobs due to technology and outsourcing.

Summary:
The economy appears to be good at the national, regional, and local level that should allow Southern Water District to succeed under the current economic conditions resulting from the rate increase and debt reduction.

Historical and Normalized Financial Statements

The lost revenues were arrived from the PSC report which was filed by the Southern Water District. The below represents what the District determined were their lost revenues. Prestonsburg City Utilities provided their estimate and was more detailed, and resulted in less lost revenues. However, we determined the PSC performed extensive work on the District's records and therefore were more reliable.

Summary Historical Income Statements

The following tables provide a summary of Southern Water and Sewer District's lost revenues..

	2013	2014	2015	2016	2017
Total Sales Revenue	**656,122**	**656,122**	**656,122**	**656,122**	**656,122**
Total Cost of Goods Sold	173,277	173,277	173,277	173,277	173,277
Gross Profit	**482,845**	**482,845**	**482,845**	**482,845**	**482,845**
Income From Operations	**482,845**	**482,845**	**482,845**	**482,845**	**482,845**
Net Income	**482,845**	**482,845**	**482,845**	**482,845**	**482,845**

Normalized Earnings and Net Cash Flow Summary

The following tables present various measures of normalized earnings and net cash flows that are available to apply in the valuation methods that follow later in this report.

Normalized Earnings

The table below summarizes the income and expense normalization adjustments and constructs the indicated measures of earnings on an adjusted basis. The District does not pay income taxes like normal companies.

	2013	2014	2015	2016	2017
Total Income & Expense Adjustments Before Tax	0	0	0	0	0
Less: Tax Effect	0	0	0	0	0
Less: Adjustment to Historic Tax	0	0	0	0	0
Plus: Adjustments to Net-of-Tax Items	0	0	0	0	0
Net Adjustments	**0**	**0**	**0**	**0**	**0**
Plus: Historic Net Income	482,845	482,845	482,845	482,845	482,845
Net Income	**482,845**	**482,845**	**482,845**	**482,845**	**482,845**
Plus: Normalized Income Taxes	0	0	0	0	0
EBT	**482,845**	**482,845**	**482,845**	**482,845**	**482,845**
Plus: Normalized Interest Expense	0	0	0	0	0
EBIT	**482,845**	**482,845**	**482,845**	**482,845**	**482,845**
Plus: Normalized Depreciation & Amortization	0	0	0	0	0
EBITDA	**482,845**	**482,845**	**482,845**	**482,845**	**482,845**

Valuation of Southern Water and Sewer District

We were engaged by Dean Hall President Southern Water and Sewer to issue a detailed report. Our objective was to estimate the Fair Market Value of lost revenue and associated assets of Southern Water and Sewer District's per contract as of June 28, 2018.

The standard of value used in our valuation of Southern Water and Sewer District is *Fair Market Value*. Fair Market Value is defined in IRS Revenue Ruling 59-60 as: "The price at which the property would change hands between a willing buyer and a willing seller when the former is not under any compulsion to buy and the latter is not under any compulsion to sell, both parties having reasonable knowledge of relevant facts. Court decisions frequently state in addition that the hypothetical buyer and seller are assumed to be able, as well as willing, to trade and to be well informed about the property and concerning the market for such property."

The purpose of this valuation is Support Existing Sale and Transfer of customers and associated assets. This report is prepared for Dean Hall President Southern Water and Sewer and should not be used by others. This report is dated 10/31/2018.

There are a large number of factors to consider when estimating the common stock value of any business entity. These factors vary for each valuation depending on the unique circumstances of the business enterprise and general economic conditions that exist at the effective date of the valuation. However, fundamental guidelines of the factors to consider in any valuation have been established. The most commonly used valuation guidelines are derived from the Internal Revenue Service's Revenue Ruling 59-60. Revenue Ruling 59-60 states that in the valuation of the stock of closely held businesses, the following factors, although not all inclusive, are fundamental and require careful consideration in each case:

a) The nature of the business and the history of the enterprise from its inception.
b) The economic outlook in general and the condition and outlook of the specific industry in particular.
c) The book value of the stock and the financial condition of the business.
d) The earning capacity of the company.
e) The dividend-paying capacity.
f) Whether or not the enterprise has goodwill or other intangible value.
g) Sales of the stock and the size of the block of stock to be valued.
h) The market price of stocks of corporations engaged in the same or a similar line of business having their stocks actively traded in a free and open market, either on an exchange or over-the-counter.

Based on circumstances unique to Southern Water and Sewer District as of June 28, 2018, additional factors have been considered. Since we were charged with valuating specific customer revenues and associated assets, many of these factors were not applicable.

In addition to providing general valuation guidelines, Revenue Ruling 59-60 outlines other considerations and techniques for valuing businesses. The techniques are commonly divided into general approaches, i.e., the Asset, Income and Market approaches. Specific methods are then used to estimate the value of the total business entity under each approach. Our conclusion of Fair Market Value is determined based on the results of these methods and the specific circumstances surrounding the interest being valued.

Overview of Valuation Approaches and Methods

As previously specified, various approaches have been used to value Southern Water and Sewer District. These approaches, described below, are the: 1) Asset Approach, 2) Income Approach, and 3) Market Approach.

Asset Approach

The Asset Approach is generally considered to yield the minimum benchmark of value for an operating enterprise. The most common methods within this approach are Net Asset Value and Liquidation Value. Net Asset Value represents net equity of the business after assets and liabilities have been adjusted to their fair market values. The Liquidation Value of the business represents the present value of the estimated net proceeds from liquidating the Company's assets and paying off its liabilities.

Income Approach

The Income Approach serves to estimate value by considering the income (benefits) generated by the asset over a period of time. This approach is based on the fundamental valuation principle that the value of a business is equal to the present worth of the future benefits of ownership. The term income does not necessarily refer to income in the accounting sense but to future benefits accruing to the owner.

The most common methods under this approach are Capitalization of Earnings and Discounted Future Earnings. Under the Capitalization of Earnings method, normalized historic earnings are capitalized at a rate that reflects the risk inherent in the expected future growth in those earnings. The Discounted Future Earnings method discounts projected future earnings back to present value at a rate that reflects the risk inherent in the projected earnings.

Additional methods under the Income Approach are Capitalization of Excess Earnings and Multiple of Discretionary Earnings. Commonly referred to as the “formula method,” the Capitalization of Excess Earnings method determines the value of tangible and intangible assets separately and combines these component values for an indication of total entity value. Under the Multiple of Discretionary Earnings method, the entity is valued based on a multiple of “discretionary earnings,” i.e., earnings available to the owner who is also a manager. Both of these methods are normally used to value small businesses and professional practices.

Market Approach

The Market Approach compares the subject company to the prices of similar companies operating in the same industry. Comparable companies can be privately owned or publicly traded where the valuation multiples are determined from the purchase/sale price for the company. A common problem for privately owned businesses is a lack of publicly available comparable data. Comparable companies can also be publicly traded where the valuation multiples are derived from the trading price for the public companies stock as of the date of the valuation.

The methods utilized under each approach are presented and discussed in the following sections.

Less: Value of Total Liabilities	0

Equity Value Conclusions

We have estimated the Fair Market Value on a controlling interest, marketable basis for lost revenues and associated assets of Southern Water and Sewer District's transfer contract as of June 28, 2018 as described within this report.

Our conclusion is $4,020,000 as summarized below. This conclusion is subject to the Statement of Assumptions and Limiting Conditions and the Representations presented in the following report. We have no obligation to update this report or our conclusion of value for information that comes to our attention after the date of this report.

In arriving at this opinion of value, we relied on a "value in use" or going-concern premise. This premise assumes that the Company is an ongoing business enterprise with management operating in a rational way with a goal of maximizing shareholder value.

Enterprise-Level Equity Value

When there is more than one indication of value produced by the different valuation approaches and methods, the analyst must reconcile these values. Therefore, in arriving at our conclusion of the enterprise equity value for Southern Water and Sewer District, we assigned relative weights to the individual indications of enterprise-level equity value and calculated a weighted average of these values. The weighted-average enterprise-level equity value is $4,020,000 as presented in the following table.

Southern Water and Sewer District **Discounted Equity Net Cash Flows**	**Projected** **Equity Net Cash Flows**	**Discount** **Factor**	**Present Value** **Factor**	**Present** **Value** **2017**
FY 2018	482,906	1.000000	0.892777	431,127
FY 2019	482,906	2.000000	0.797052	384,901
FY 2020	482,906	3.000000	0.711590	343,631
FY 2021	482,906	4.000000	0.635291	306,786
FY 2022	482,906	5.000000	0.567174	273,892
Terminal Value of Equity Net Cash Flows **	4,020,864	5.000000	0.567174	2,280,530
Operating Value				4,020,866
Calculated Equity Value				4,020,866
Indicated Equity Value				4,020,000
End-of-Year Discount Factors are Based on the Discount Rate of:		12.01%		
Terminal Value is Based on the Capitalization Rate of:		12.01%		

*** Calculated as Terminal Equity Net Cash Flows x (1 + LT Growth Rate) / Capitalization Rate*

Present Value Factor = 1 / (1 + Discount Rate)^Discount Factor

Discount Factor (end-of-year convention): Year 1 = 1, Year 2 = 2, etc.

The calculation of the Cap Rate of 12.01% is on the next page.

Southern Water and Sewer District Cap Rate Build Up

Discount Rate and Capitalization Rate Calculations and DCF Assumptions

Discount Rate and Capitalization Rate Calculations

Discount Rate Method	Build-Up Method		
Risk-Free Rate		2.91%	
Market Equity Risk Premium from CAPM / Beta			
Total Return on Asset Class	0.00%		
- Risk-Free Rate	2.91%		
= Subtotal	2.91%		
x Selected Beta	0.00		
= Market Equity Risk Premium		0.00%	
Other Risk Factors / Premiums:			
Equity Risk		15.10%	
Utility Factor		-8.00%	
Specific Company Size Premium		2.00%	
Discount Rate		12.01%	
Earnings Base Conversion Adjustment		0.00%	
Adjusted Discount Rate		12.01%	*(Applied to future benefit stream.)*
Less: Long-Term Growth in Benefit Stream		0.00%	
Capitalization Rate		12.01%	
Divided by: (1 + Long Term Growth Rate)		100.00%	
Historic Earnings Capitalization Rate		12.01%	*(Applied to historic benefit stream.)*
Excess Earnings Capitalization Rate		25.00%	*(Applied to historic excess earnings benefit stream.)*

Discounted Cash Flow and Earnings Calculation Based On

Discounting Convention:	**Terminal / Residual Basis:**
End of Year	Terminal Earnings
Years for Discounting:	**Terminal Growth Rate:**
5	0.00%

Terminal / Residual Value Calculation Method:
Gordon Method (level growth)

The utility industry has a lower Cap Rate than normal industries. The large utilities enjoy an average cap rate of 10%. I was able to support this rate with empirical data including specific to water and Ky companies. I added a Specific Company and Size premium of 2% due to the smaller size of District compared to the NYSE companies and other challenges the District faces in updating their assets.

Appendix — Representations

The following factors guided our work during this engagement:

- The analyses, opinions, and conclusions of value included in this report are subject to the assumptions and limiting conditions specified previously in this report, and they are our personal analyses, opinions, and conclusion of value.

- The economic and industry data included in this report were obtained from sources that we believed to be reliable. We have not performed any corroborating procedures to substantiate that data.

- This engagement was performed in accordance with the American Institute of Certified Public Accountants Statement on Standards for Valuation Services.

- We have previously identified the parties for whom this information and report have been prepared. This valuation report is not intended to be, and should not be, used by anyone other than those parties.

- Our compensation for this engagement is not contingent on the outcome of this valuation.

- We have no obligation to update this report or our opinion of value for information that comes to our attention after the report date.

(Signature)	(Date)
(Signature)	(Date)

Appendix — Qualifications

This report was prepared by Terry R. Fyffe President of The Fyffe Jones Group. Terry R. Fyffe holds the following professional designations and certifications: CPA, ABV.

CURRICULUM VITAE

TERRY R. FYFFE, CPA, ABV

Academic and Professional Credentials
Bachelor of Science, Business Administration – Accounting Option, Morehead State University, 1977

Certified Public Accountant (CPA) issued by the AICPA, 1980-present

Accredited in Business Valuation (ABV) issued by the AICPA, 1998-present

Certified Financial Forensics (CFF) issued by the AICPA, 2008-present

Position and Experience
Managing Shareholder, The Fyffe Jones Group, 1984-present with offices in Huntington, West Virginia, Ashland, Kentucky and Portsmouth, Ohio

Manager, Kelley, Galloway & Company, 1977-1983

Performed valuations and testified as an expert witness on business valuation and other issues, 1980-present

Completed 64 hours and received the Certificate of Educational Achievement (CEA) in business valuations issued by the AICPA which included litigation support, 1995-1997

Completed 24 hours of the advanced Certificate of Educational Achievement, 1998-present including classes in litigation support

Attended AICPA Conference on Business Valuations annually for over 500 hours CPE, 1995-present and AICPA Conference on Litigation Support for 40 hours CPE along with numerous other Conferences including Healthcare/Physician, Divorce, etc.

Professional Affiliations

American Institute of Certified Public Accountants
Kentucky Society of Certified Public Accountants
West Virginia Society of Certified Public Accountants
Kentucky, West Virginia and Ohio Licensed
AICPA Consulting Section
Institute of Business Appraisers
Huntington Estate Planning Council Past President and Current Member
Board Member and Treasurer of Community College of Ashland Foundation Board
Board Member and Treasurer of Heritage, Arts, Science & Tourism Center
Board Member and President of Waipani Homeowners Association
KY Society of CPAs Key Contact for Tanya Pullin, Kentucky State Representative

Appendix — Projections & Assumptions

Projection Summary

	2017	2018	2019	2020	2021	2022
Net Sales Revenue		656,122	656,122	656,122	656,122	656,122
Gross Profit		482,906	482,906	482,906	482,906	482,906
EBITDA		482,906	482,906	482,906	482,906	482,906
EBIT		482,906	482,906	482,906	482,906	482,906
EBT		482,906	482,906	482,906	482,906	482,906
Net Income		482,906	482,906	482,906	482,906	482,906
Equity Net Cash Flows		482,906	482,906	482,906	482,906	482,906
Invested Capital Net Cash Flows		482,906	482,906	482,906	482,906	482,906
Net Change in Cash		482,906	482,906	482,906	482,906	482,906
Total Current Assets		482,906	965,812	1,448,717	1,931,623	2,414,529
Total Equity		482,906	965,812	1,448,717	1,931,623	2,414,529
Federal Income Tax Before NOL Adjustment		0	0	0	0	0
Plus: NOL Tax Adjustment		0	0	0	0	0
Federal Income Tax Expense		0	0	0	0	0
Equity Net Cash Flows (FCF-Equity)						
Net Income		482,906	482,906	482,906	482,906	482,906

Summary Income Statement Projections

	2018	**2019**	**2020**	**2021**	**2022**
Total Sales Revenue	**656,122**	**656,122**	**656,122**	**656,122**	**656,122**
Total Cost of Goods Sold	173,216	173,216	173,216	173,216	173,216
Gross Profit	**482,906**	**482,906**	**482,906**	**482,906**	**482,906**
Income From Operations	**482,906**	**482,906**	**482,906**	**482,906**	**482,906**
Net Income	**482,906**	**482,906**	**482,906**	**482,906**	**482,906**

Summary Cash Flow Projections

	2018	**2019**	**2020**	**2021**	**2022**
Net Cash Flow From Operations	482,906	482,906	482,906	482,906	482,906
Net Cash Flow From Investments	0	0	0	0	0
Net Cash Flow From Financing	0	0	0	0	0
Net Cash Flow	**482,906**	**482,906**	**482,906**	**482,906**	**482,906**
Cash at Beginning of Period	0	482,906	965,812	1,448,717	1,931,623
Cash at End of Period	**482,906**	**965,812**	**1,448,717**	**1,931,623**	**2,414,529**

Overview of Projection Assumptions

In preparing the preceding financial statement projections, management made various assumptions about expected future revenues, expenses, assets, liabilities and equity. These assumptions were made after gathering and analyzing data that affects the future economic outlook of the Company. This data was derived from sources such as the normalized financial statements, publicly available information and other economic materials.

This section of the report provides a broad overview of the Projection Assumptions and has been prepared to emphasize items considered significant to the overall understanding of the projections.

Revenue & Expense Assumptions

Net Sales Revenues over the past 5 historic years have grown at a compound average annual rate of 0.00%. Future Net Sales Revenues are projected to grow at an estimated, compound average annual rate of 0.00%, starting from a base amount of $656,122 and growing to $656,122 in the first projected year and $656,122 in projected year 5.

Total Cost of Goods Sold over the past 5 historic years has averaged 26.41% of Net Sales Revenues for each respective year and was 26.41% of Net Sales Revenues in the most recent historic fiscal year, 2017. Total Cost of Goods Sold has been projected to be $173,216, or 26.40% of Net Sales Revenues in the first projected year and $173,216, or 26.40% of Net Sales Revenues in projected year 5. On average, Total Cost of Goods Sold has been projected to be 26.40% of each year's respective Net Sales Revenues.

Viability of Southern Water and Sewer District

As part of my engagement, I was asked to provide an opinion as to the viability of Southern Water and Sewer District after the Agreement effective June 28, 2018 between the District and Prestonsburg City Utility Commission. In my opinion, the District is viable after the agreement based on the following:

The Kentucky Public Service Commission issued a report on the determination of the rate increase filed by the District. In addition to reviewing information provided by the filing, the Commission assigned staff members to do a thorough examination of the District's finances. Their conclusion was to approve a rate increase for both the basic and second tier rates than what the District had requested, which is very unusual by the Commission. The combination of these rate increases and the reduction of debt/working capital provided by the $2,140,000 contract dated June 28, 2018 and the additional agreement of $2,000,000, should make the viability of the District positive for many years based on my understanding. I place a great deal of reliance on the Commission's detailed work and confidence that the rate increase was sufficient to assure their success.

Viability of Prestonsburg City Utilities Commission

As part of my engagement, I was asked to provide an opinion as to the viability of Prestonsburg City Utilities Commission after the Agreement effective June 28, 2018 between the Southern Water and Sewer District and Prestonsburg City Utility Commission. In my opinion, the District is viable after the agreement based on the following:

I reviewed the most current financial statement of Prestonsburg City Utilities Commission as of June 30, 2018. The City has been operating under a Management agreement to service these customers and perform services and maintenance/repairs on the associated assets for about two years. The financial statements reflected the actions taken by the City to update and improve the assets, including financing required to make substantial extensive improvements to the existing systems. In addition to the water revenues, the City was in the favorable position to provide sewer services for additional revenues. Many if not most of the subject customers were along the US 23 corridor and are commercial business accounts. Upon my site visit, we traveled US 23 to tour the customers affected by the transfer. After these improvements and additions, the City still showed Fund Balance Equity of over $4M. Interview with Turner E. Campbell, Superintendent/CEO of Prestonsburg City Utilities Commission also confirmed my understanding of the financials and viability of the City Commission.