Kern Energy

Financial Statements

November 30, 2023 and 2022

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BARBICH HOOPER KING
DILL HOFFMAN, LLP

Independent Auditors' Report

Board of Directors
Kern Energy
Bakersfield, California

Opinion

We have audited the accompanying financial statements of Kern Energy (a California corporation), which comprise the balance sheets as of November 30, 2023 and 2022, and the related statements of income and retained earnings, and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Kern Energy as of November 30, 2023 and 2022, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of Kern Energy and to meet our other ethical responsibilities in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about Kern Energy's ability to continue as a going concern within one year after the date that the financial statements are available to be issued.

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Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with generally accepted auditing standards, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Kern Energy's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Kern Energy's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

BARBICH HOOPER KING
DILL HOFFMAN
Accountancy Corporation

Barbich Hooper King

Bakersfield, California
February 22, 2024

Kern Energy

Balance Sheets
November 30, 2023 and 2022
(in thousands)

	2023	2022
ASSETS		
Current Assets		
Cash and cash equivalents	$ 72,127	$ 76,010
Marketable securities	17,153	14,818
Trade accounts receivable	58,538	63,959
Taxes and other receivables	12,833	18,850
Inventories	25,730	25,115
Prepaid expenses and other assets	5,541	11,943
	191,922	210,695
Property, Plant and Equipment, at cost	167,419	158,303
Less accumulated depreciation	(116,042)	(110,839)
	51,377	47,464
	$ 243,299	$ 258,159
LIABILITIES AND STOCKHOLDER'S EQUITY		
Current Liabilities		
Accounts payable	$ 74,182	$ 98,395
Accrued liabilities and taxes	20,546	22,518
	94,728	120,913
Stockholder's Equity		
Common stock, no par value, authorized, issued and outstanding 2,000 shares	21	21
Additional paid in capital	10,578	10,578
Retained earnings	137,972	126,647
	148,571	137,246
	$ 243,299	$ 258,159

See Notes to Financial Statements.

Kern Energy

Statements of Income and Retained Earnings
Years Ended November 30, 2023 and 2022
(in thousands)

	2023	2022
Sales	$ 1,067,015	$ 1,286,825
Operating expenses		
Cost of products sold	951,190	1,146,992
Refinery operating costs	83,378	76,818
Selling, general and administrative	7,548	6,486
Depreciation	6,881	6,678
	1,048,997	1,236,974
Operating income	18,018	49,851
Dividends, interest, other income and (expenses), net	5,307	(545)
Net income	23,325	49,306
Retained earnings at beginning of year	126,647	97,341
Dividends paid to stockholder	(12,000)	(20,000)
Retained earnings at end of year	$ 137,972	$ 126,647

See Notes to Financial Statements.

Kern Energy

Statements of Cash Flows
Years Ended November 30, 2023 and 2022
(in thousands)

	2023	2022
Cash flows from operating activities:		
Net income	$ 23,325	$ 49,306
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	6,881	6,678
Net realized and unrealized (gain) loss on marketable securities	(1,229)	2,351
Changes in operating assets and liabilities:		
(Increase) decrease in trade and other receivables	11,438	(17,655)
(Increase) decrease in inventories	(615)	3,779
(Increase) decrease in prepaid expenses and other assets	6,402	(2,284)
Increase (decrease) in accounts payable, accrued liabilities and taxes	(26,185)	35,253
Net cash provided by operating activities	20,017	77,428
Cash flows from investing activities:		
Net proceeds (purchase) of marketable securities	(1,106)	17,947
Purchase of property, plant and equipment	(10,794)	(9,229)
Net cash provided by (used in) investing activities	(11,900)	8,718
Cash flows from financing activities:		
Dividends paid to stockholder	(12,000)	(20,000)
Net cash used in financing activities	(12,000)	(20,000)
Net increase (decrease) in cash and cash equivalents	(3,883)	66,146
Cash and cash equivalents at beginning of year	76,010	9,864
Cash and cash equivalents at end of year	$ 72,127	$ 76,010

See Notes to Financial Statements.

Note 1. Nature of Business and Summary of Significant Accounting Policies

Nature of business:

Kern Oil and Refining Co., a California "S" Corporation, doing business as Kern Energy (the Company) is a petroleum refiner and renewable fuels producer with operations located near Bakersfield, California. The Company is the successor to other entities that originally began operations at the location in the 1930's.

The Company is a wholly owned subsidiary of Casey Co., a privately held company headquartered in Long Beach, California. The Company refines crude oil and other petroleum feedstocks into various petroleum products, processes biomass into renewable diesel and produces biodiesel blends. The Company markets and sells those products primarily to retailers, wholesalers, distributors and major oil companies located in California. Credit is extended to customers in the form of accounts receivable in the normal course of business.

Basis of accounting:

Assets, liabilities, income and expenses are recognized on the accrual basis of accounting.

Use of estimates:

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

Cash and cash equivalents:

For purposes of reporting cash balances and cash flows, the Company considers all highly liquid debt instruments purchased with a maturity or effective maturity of three months or less to be cash equivalents.

Cash and cash equivalents are concentrated in high quality financial institutions, and are placed in money market funds, United States government securities, municipal bonds, and commercial paper. Although these balances exceed government insurance levels, the Company does not believe it has any significant risk associated with these investments.

Marketable securities:

Investments in marketable securities are accounted for as trading securities and stated at market value, using quoted market prices. Unrealized gains and losses are included in earnings on the statements of income.

The unrealized gain (loss) recognized for the years ended November 30, 2023 and 2022 for equity securities held as of year-end were $1,200,537 and $(1,817,468), respectively.

Accounts receivable:

Accounts receivable are stated at the amount management expects to collect from outstanding balances. Management believes that all accounts receivable are fully collectible as of November 30, 2023 and 2022. Accordingly, no reserve for bad debts exists at November 30, 2023 and 2022.

Inventories:

Crude oil and refined product inventories are stated at lower of cost or market, with cost being determined by the last-in, first-out (LIFO) method. Refinery supply inventories are stated at lower of cost or market determined by the average cost method.

Property, plant and equipment:

Property, plant and equipment are recorded at cost. Depreciation is computed using the straight line method over estimated useful lives of 10 to 20 years.

Expenditures which materially increase values, expand capacities, or extend useful lives are capitalized. Maintenance and repairs of property and equipment are charged to operations as incurred. Upon retirement, sale, or other disposition of property, plant and equipment, the cost and accumulated depreciation are eliminated from the accounts and gains or losses are included in net income or loss.

Long-lived assets:

The Company evaluates its long-lived assets for indicators of possible impairment when events or changes in circumstances indicate the carrying value of an asset may not be recoverable. To date, management has determined that no impairment of long-lived assets exists and therefore no impairment losses have been recognized as of November 30, 2023 and 2022.

Asset retirement obligations:

The Financial Accounting Standards Board (FASB) requires that the fair value of a liability associated with the retirement of long-lived assets be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. Retirement dates for the Company's assets generally cannot be determined, and estimates of the fair value of asset retirement liabilities cannot be made, therefore no liabilities have been recorded as of November 30, 2023 and 2022.

Revenue recognition:

The Company records revenues for products sold when it has completed its performance obligation, typically upon delivery to customers, which is the point at which title is transferred and when payment has either been received or collection is reasonably assured. Revenue is measured at the amount the Company expects to receive in exchange for transferring commodities to the customer. All revenues are reported on a net basis, exclusive of shipping and handling costs. Excise and other taxes collected from customers and remitted to governmental authorities are not included in revenues and costs.

The Company enters into certain purchases and sales of inventory with the same counterparty that are deemed to be made in contemplation of one another. These buy/sell transactions are combined and, as a result, revenues and cost of sales are not recognized in connection with these arrangements, with no effect on net income or loss.

Income taxes:

The Company and its parent company have elected to be taxed as "S" Corporations under Internal Revenue Code Section 1371 and file consolidated income tax returns. Under this election, the corporation does not pay Federal income taxes. Although California has conformed to "S" Corporation provisions, it still imposes a minimum tax of 1.5% on taxable income, which is paid by the parent company. The income and other distributable items of the consolidated tax returns flow through to the stockholder and will be reported by them on their individual income tax returns.

Futures contracts:

The Company periodically enters into futures contracts to manage its exposure to crude oil and refined products price fluctuations. Futures contracts are carried at fair value. Generally, because of the short-term nature of the contracts or their limited use, the Company does not apply hedge accounting principles, and changes in the fair value of these contracts are reflected in current operating income.

Margin deposits and futures contract balances were $2,082,000 and $3,233,000 at November 30, 2023 and 2022, respectively, and are included in prepaid expenses and other assets on the balance sheets. For the years ended November 30, 2023 and 2022, the gains (losses) recognized from futures contracts in the statements of income in cost of products sold were $1,371,000 and ($10,148,000), respectively.

At November 30, 2023, the Company held futures contracts obligating the Company to sell crude oil at a fair value of approximately $29,250,000. The crude oil futures contracts have maturity dates of January 2024 and February 2024. The Company also held futures contracts obligating the Company to purchase crude oil at a fair value of approximately $6,420,000. These crude oil futures contracts had a maturity date of January 2024.

At November 30, 2022, the Company held futures contracts obligating the Company to sell crude oil at a fair value of approximately $30,715,000. The crude oil futures contracts had maturity dates of January 2023 and February 2023. The Company also held futures contracts obligating the Company to purchase crude oil at a fair value of approximately $6,265,000. These crude oil futures contracts had a maturity date of January 2023.

Environmental costs:

Environmental expenditures that relate to current operations are expensed or capitalized as appropriate. Expenditures that relate to existing conditions caused by past operations and that do not contribute to future revenue generation are expensed. Reserves for estimated expenses are recorded when environmental remediation efforts are considered probable and the costs can be reasonably estimated. Expenditures that will ultimately be capitalized are not accrued in advance.

Retirement plans:

The Company maintains a 401(k) plan covering qualified full time employees. Employees may contribute up to 100% of their wages subject to the statutory limitations. Company contributions are made at the discretion of the Board of Directors.

The Company also maintains a defined contribution plan covering substantially all full time employees. The Company contributes 5.1% of eligible compensation to the plan.

All contributions are funded currently. Company contributions to these plans for the years ended November 30, 2023 and 2022 were $1,200,000 and $1,103,000, respectively.

Change in accounting principle:

ASU 2016-02, "Leases" (Topic 842), and subsequent amendments is effective December 1, 2022 and requires lessees to recognize on the balance sheet right-of-use assets and lease liabilities for leases previously classified as operating leases under the previous authoritative standards and provides enhanced disclosures surrounding the leasing arrangements.

The Company adopted the new lease standards using the modified retrospective transition approach which did not have any effect on the Company's financial statements.

Note 2. Fair Value Measurements

In accordance with generally accepted accounting principles (GAAP), fair value is determined as the price that would be received in exchange for an asset or paid to transfer a liability in an orderly transaction between market participants on the measurement date. The standard establishes three levels of inputs that may be used to measure fair value:

Level 1 – Values are based on quoted prices in active markets for identical assets or liabilities.

Level 2 – Values are based on quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data of substantially the full term of the assets or liabilities.

Level 3 – Values are determined using pricing models, discounted cash flow methodologies or similar techniques, and at least one significant model assumption or input is unobservable. Determination of the fair value requires significant management judgment or estimation.

Assets measured at fair value on a recurring basis, excluding accrued interest components, consisted of the following:

	2023 (in thousands)	**2022** (in thousands)
Cash and cash equivalents:		
Cash	$ 372	$ 2,341
Cash and money market funds	71,755	73,669
	$ 72,127	$ 76,010
Marketable securities:		
Certificates of deposit	$ 50	$ 50
Common stocks, exchange-traded funds	16,104	14,747
Mutual funds	21	21
US Treasury bills	978	-
	$ 17,153	$ 14,818
Margin deposits:		
Futures contracts	$ 2,082	$ 3,233

Cash and cash equivalents and marketable securities are considered Level 1 assets. Margin deposits are considered Level 2 assets and are included in prepaid expenses and other assets on the balance sheets.

Note 3. Inventories

Inventories at November 30, 2023 and 2022 consisted of the following:

	2023 (in thousands)	2022 (in thousands)
Crude oil	$ 21,111	$ 22,425
Refined products	26,363	28,214
Exchanges	10,035	13,760
Refinery supplies	4,359	3,444
LIFO reserve	(36,138)	(42,728)
	$ 25,730	$ 25,115

If the first-in, first-out (FIFO) method had been used to determine the cost of inventories, inventories would have been approximately $36,138,000 and $42,728,000 higher than reported at November 30, 2023 and 2022, respectively. If the FIFO method had been used, the income statement would have reported operating income of $11,428,000 and net income of $16,735,000 for the year ended November 30, 2023, and operating income of $56,869,000 and net income of $56,324,000 for the year ended November 30, 2022, respectively.

Note 4. Property, Plant and Equipment

Property, plant and equipment consisted of the following at November 30, 2023 and 2022:

	2023 (in thousands)	2022 (in thousands)
Land	$ 1,208	$ 1,208
Buildings and leasehold improvements	4,336	3,465
Refinery machinery and equipment	161,228	152,748
Office equipment	647	882
	167,419	158,303
Accumulated depreciation	(116,042)	(110,839)
	$ 51,377	$ 47,464

Refinery machinery and equipment included construction in progress of $13,473,000 and $7,418,000 as of November 30, 2023 and 2022, respectively.

During the years ended November 30, 2023 and 2022, the Company disposed of fully depreciated assets with a cost and accumulated depreciation of $1,679,000 and $-0-, respectively.

Note 5. Bank Line of Credit

The Company has a line of credit with a bank for available credit of $35,000,000 and $40,000,000 at November 30, 2023 and 2022, respectively, to finance general working capital needs and to provide letters of credit to facilitate the purchases of crude oil and petroleum products. Borrowings on this line of credit are collateralized by all assets of the Company. The interest rate on borrowings is the secured overnight financing rate (SOFR) plus one and three-quarters percent at November 30, 2023 and 2022. The line of credit expires March 31, 2025.

The line of credit agreement with the bank has financial covenants which, among other things, require the Company to maintain minimum liquidity, tangible net worth and profitability levels. At November 30, 2023, the Company was in compliance with these covenants.

At November 30, 2023 and 2022, the Company had outstanding letters of credit of $25,277,000 and $21,000,000, respectively and no outstanding borrowings under the line of credit.

Note 6. Concentrations

Refinery sales to two major oil companies approximated 11% and 11% of total sales for the year ended November 30, 2023 and sales to two major oil companies approximated 13% and 12% of total sales for the year ended November 30, 2022.

At November 30, 2023, two customers' accounts receivable balances were in excess of 10% of the Company's total trade accounts receivable. The balances were $16,837,000 and $14,378,000 or 29% and 25%, respectively, of the total.

At November 30, 2022, two customers' accounts receivable balances were in excess of 10% of the Company's total trade accounts receivable. The balances were $18,745,000 and $12,725,000, or 29% and 20%, respectively, of the total.

Purchases of raw materials from two suppliers approximated 18% and 11% of cost of products sold for the year ended November 30, 2023. Purchases of raw materials from one supplier approximated 17% of cost of products sold for the year ended November 30, 2022.

Note 7. Related Party Transactions

The Company has entered into various related party transactions, including product sales and terminal services, for the years ended November 30, 2023 and 2022, with its parent company, Casey Co. and with Kern Fuels Research, LLC (KFR), an operating subsidiary of Casey Co. Transactions between all entities within common control of Casey Co. are conducted in the same manner as transactions with unrelated entities.

The Company's sales to KFR for the years ended November 30, 2023 and 2022, were $3,229,000 and $5,303,000, respectively. As of November 30, 2023 and 2022, accounts receivable from KFR were $188,000 and $424,000, respectively.

The Company's purchases from KFR for the years ended November 30, 2023 and 2022 were $354,000 and $330,000, respectively.

Related party transactions with Casey Co. relate primarily to expense allocation and reimbursements between the parties. The Company paid $1,027,000 and $1,041,000 to Casey Co. during the years ended November 30, 2023 and 2022, respectively, for management fees.

Note 8. Commitments and Contingencies

Capital expenditures:

The Company had commitments for capital expenditures of approximately $6,400,000 and $5,100,000 at November 30, 2023 and 2022, respectively.

Environmental:

The Company is subject to various Federal, state and local environmental laws and regulations relating to its operations and facilities. Consistent with its accounting policy for environmental costs, the Company had reserves for environmental expenses of $199,000 at November 30, 2023 and 2022. Such amounts reflect the Company's most likely estimates of the costs that will be incurred over an extended period to remediate identified environmental conditions for which costs are reasonably estimable.

Litigation:

The Company is subject to various claims and lawsuits, some of which may be for substantial amounts. The Company will record a loss contingency for these matters if it is probable that an asset has been impaired or a liability has been incurred and the amount of the loss can be reasonably estimated. In addition, the Company will disclose, in aggregate, its exposure to loss in excess of the amount recorded on the balance sheet for these matters if it is reasonably possible that an additional material loss may be incurred. The determination of loss contingencies are based on judgments made by management with respect to the likely outcome of these matters and are adjusted as appropriate. Management's judgments could change based on new information, change in, or interpretations of, laws and regulations, changes in management's plans, intentions, or opinions regarding the outcome of legal proceedings, or other factors. Based on management's assessment, there is no litigation ongoing that would require disclosure in the financial statements.

Note 9. Subsequent Events

The Company has evaluated events and transactions subsequent to November 30, 2023 through February 22, 2024, the date of the independent auditors' report, noting no significant items requiring further discussion.