

STATE OF ALASKA

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BEFORE THE REGULATORY COMMISSION OF ALASKA

Before Commissioners:

T. W. Patch, Chairman
Kate Giard
Paul F. Lisankie
Robert M. Pickett
Janis W. Wilson

In the Matter of the Application by AltaGas Ltd.,)
AltaGas Utility Holdings (U.S.) LLC and Continental)
Energy Systems LLC for Approval of Acquisition of) Docket No. U-12-006
Control of Cook Inlet Natural Gas Storage Alaska,)
Holder of Certificate of Public Convenience and)
Necessity No. 733, by AltaGas Ltd. and AltaGas)
Utility Holdings (U.S.) LLC)
)
)
)
)
)

DIRECT TESTIMONY OF DEBORAH S. STEIN

Q1 PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A1 My name is Deborah S. Stein. My business address is 1700, 355 4th Ave. S.W., Calgary,
AB, T2P 0J1.

Q2 BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

Direct Testimony of Deborah S. Stein
Docket No. U-12-006
Page 1 of 10

Date: 5-30-12 Exh # T2
Regulatory Commission of Alaska
Stein By: CPT 412-006
Northern Lights Realtime & Reporting, Inc.
(907) 337-2221

1 A2 I am Senior Vice President, Finance and Chief Financial Officer ("CFO") of AltaGas
2 Ltd., and Treasurer of AltaGas Utility Holdings (US) LLC ("AltaGas U.S."), two of the
3 applicants in this docket.

4 **Q3 PLEASE SUMMARIZE YOUR EDUCATIONAL AND PROFESSIONAL**
5 **BACKGROUND.**

6
7 A3 My education includes a Bachelor of Arts in Economics from York University in North
8 York, Ontario, Canada. I qualified as a Chartered Accountant in 1990. Prior to joining
9 AltaGas Ltd. in January 2005, I held the following positions: Manager, Investor
10 Relations, and Senior Internal Auditor, TransCanada Corporation; Controller, Paramount
11 Canada's Wonderland; and Director, Finance, Wendy's Restaurants of Canada. I am a
12 member of the Institute of Chartered Accountants of Ontario and Alberta and a member
13 of the Institute of Corporate Directors of Canada. I am a certified Financial Risk
14 Manager and hold my certification from the Institute of Corporate Directors of Canada. I
15 joined AltaGas Ltd. in January 2005 as Vice President, Corporate Risk and Investor
16 Relations. In August 2005, I was appointed CFO of AltaGas Utility Group Inc.
17 ("AUGI"), a publicly-traded entity that resulted from the spin-out of the utility business,
18 which was subsequently reacquired in November 2009. I retained the position of CFO of
19 AUGI until December 2006. During that time, I also held the role of Vice President,
20 Corporate Controller of AltaGas Ltd. I was appointed Vice President Finance in January
21 2007, Vice President Finance, CFO in January 2008 and Senior Vice President Finance
22 and CFO in January 2011. My responsibilities include leading the finance, tax, corporate
23 reporting, information systems, investor relations and planning functions of AltaGas Ltd.

1 I have testified before the Alberta Utilities Commission as part of AltaGas Utilities Inc.
2 General Rate Application, in 2007.

3 **Q4 WHAT IS THE PURPOSE OF YOUR TESTIMONY I N THIS PROCEEDING?**

4 A4 In conjunction with John E. Lowe's testimony, my testimony is provided on behalf of
5 AltaGas Ltd. and AltaGas Utility Holdings (U.S.) LLC ("AltaGas U.S.") in support of
6 the applications jointly submitted by AltaGas Ltd., AltaGas U.S.(to which I occasionally
7 refer together as "AltaGas") and Continental Energy Systems LLC ("Continental")
8 (collectively, the "Applications") for approval of the acquisition of control of ENTAR
9 Natural Gas Company ("ENSTAR"), Alaska Pipeline Company ("APC") and Cook
10 Inlet Natural Gas Storage Alaska, LLC ("CINGSA") by way of the transaction
11 embodied in the February 1, 2012 Stock Purchase Agreement, attached to the
12 Application as Exhibit A (the "Proposed Transaction").
13
14
15

16 I will address and provide exhibits concerning the following topics:

- 17 (1) the capital structure of AltaGas Ltd. and AltaGas U.S. prior to the closing of the
18 Proposed Transaction;
19 (2) the expected capital structure of AltaGas Ltd. and AltaGas U.S. after the closing of
20 the transaction;
21 (3) why AltaGas Ltd. and AltaGas U.S. are financially capable of acquiring and owning
22 ENSTAR, APC and CINGSA;
23 (4) the expected capital structure of ENSTAR, APC and CINGSA after closing of the
24 Proposed Transaction; and
25

1 (5) the effect of the Proposed Transaction on the ability of ENSTAR, APC and CINGSA
2 to obtain access to capital.

3 Exhibit DSS-1 to my testimony includes the Financing Commitment letter from the
4 Toronto Dominion Bank, Bank of Montreal and the Royal Bank of Canada, for a US\$300
5 million credit facility that AltaGas Ltd. obtained on February 1, 2012. Closing of the
6 credit facility occurred on March 2, 2012.
7

8
9 Exhibit DSS-2 to my testimony is the final short form prospectus ("Prospectus") dated
10 February 14, 2012, with respect to a subscription receipt offering which was completed
11 on February 22, 2012 with gross proceeds of approximately C\$403 million
12 (approximately US\$396 million).
13

14
15 Exhibit DSS-3 to my testimony is a press release dated April 13, 2012 regarding the
16 completion of the issuance of C\$200 million (approximately US\$ 200 million) senior
17 unsecured medium term notes ("MTNs") by AltaGas Ltd.

18 **Q5 WHAT IS THE DIFFERENCE BETWEEN THE CANADIAN AND U.S.**
19 **ACCOUNTING POLICY, AND HOW WILL THE TRANSACTION AFFECT**
20 **THE FINANCIAL STATEMENTS OF SEMCO HOLDING CORPORATION**
21 **AND ITS SUBSIDIARIES?**
22

23 **A5** With respect to accounting for rate regulated activities, Canadian GAAP and US GAAP
24 are not significantly different. Semco Holding Corporation ("Semco Holding") and its
25 subsidiaries, including SEMCO Energy Inc., will continue to prepare their financial
26

1 statements in accordance with U.S. GAAP. The Proposed Transaction is not expected to
2 have any impact on the financial statements for the subsidiaries of Semco Holding.
3 Furthermore, effective January 1, 2012, AltaGas Ltd, adopts U.S. GAAP for financial
4 reporting purpose.

5 **Q6 PLEASE DESCRIBE THE CAPITAL STRUCTURE OF ALTAGAS LTD. AND**
6 **ALTAGAS U.S. PRIOR TO THE CLOSING OF THE PROPOSED**
7 **TRANSACTION**

8
9 A6 Table 1 below shows the capital structure of AltaGas Ltd. as at December 31, 2011:

10 Table 1

AltaGas Ltd. capital structure prior to closing of the Proposed Transaction		
As at December 31, 2011	C\$ Million	%
Shareholder equity	1,357	50%
Long term debt (including current portion)	1,307	49%
Short term debt	17	1%
	2,681	

16
17 As at December 31, 2011¹:

18 i. AltaGasLtd.'s shareholder equity of approximately C\$1.4 billion included the
19 following:

20 (a) Approximately 89 million common shares outstanding. AltaGas Ltd.'s
21 common shares are listed and traded on the Toronto Stock Exchange
22 ("TSX").
23

24
25 ¹ Exchange rate of US to Canadian dollar as at December 31, 2011 was approximately 1.017.

(b) Eight million cumulative redeemable five-year rate-reset preferred shares, Series A (the "Series A Preferred Shares) outstanding. The Series A Preferred Share are listed on the TSX.

ii. Table 2 below shows AltaGas Ltd.'s total debt outstanding of \$1.3 billion:

Table 2

ALtaGas Ltd. outstanding debt	
As at December 31, 2011	<u>C\$ Million</u>
Senior unsecured medium term notes (MTNs) issued:	
5.07% MTN maturing January 19, 2012	100
7.42% MTN maturing April 29, 2014	200
6.94% MTN maturing June 29, 2016	100
5.49% MTN maturing March 27, 2017	200
4.6% MTN maturing January 15, 2018	175
4.1% MTN maturing March 24, 2016	200
4.55% MTN maturing January 17, 2019	<u>200</u>
	1,175
Credit facilities maturing 2015 and 2016	38
Debtenture notes issued by subsidiary	87
Other long term indebtedness	7
Short term indebtedness	<u>17</u>
	1,324

iii. As at December 31, 2011, AltaGas Ltd. had approximately C\$1.1 billion of available liquidity through credit facilities, of which over C\$0.85 billion remained undrawn, and cash in hand available, including:

(a) C\$600 million unsecured extendible revolving credit facility with a C\$200 million accordion feature which allows the facility to be increased to C\$800 million, with a maturity date of May 30, 2016;

- (b) Approximately C\$170 million under the C\$200 million unsecured extendible revolving credit facility maturing on November 17, 2015;
- (c) C\$79 million under C\$96 million demand operating facilities; and
- (d) \$7 million under a C\$75 million unsecured extendible revolving letter of credit facility².

AltaGas U.S. was formed on January 27, 2012, as a Delaware limited liability corporation. As at January 27, 2012, it had shareholder capital of US\$100 and nil debt. The Proposed Transaction will be funded through AltaGas U.S. as described below.

Q7 PLEASE DESCRIBE THE CAPITAL STRUCTURE OF ALTAGAS LTD. AND ALTAGAS U.S. AFTER THE CLOSING OF THE TRANSACTION.

A7 Table 3 below shows the pro forma AltaGas Ltd. capital structure post transaction close, based on audited financial results as at December 31, 2011:

Table 3

Forecast AltaGas Ltd. capital structure after closing of the Proposed Transaction		
Forecast, post transaction close	C\$ Million	%
Shareholder equity	1,729	45%
Long term debt (including current portion)	2,115	55%
Short term debt	17	0%
	3,861	

- i. The increase in shareholder equity reflects, among other things, the net proceeds to AltaGas Ltd. resulting from the subscription receipt offering announced on

²Amounts drawn under the C\$75 million extendible revolving letter of credit facility were in the form of Letters of Credit and not recorded as indebtedness for accounting purposes.

February 1, 2012 in conjunction with the announcement of the Proposed Transaction. The subscription receipt offering was completed on February 22, 2012 with gross proceeds of approximately C\$403 million held in trust.

- ii. The increase in AltaGas Ltd.'s indebtedness post transaction close includes the assumption of Semco Holding's indebtedness of approximately US\$355 million (approximately C\$360 million), as well as incremental debt expected to be incurred by AltaGas Ltd. and AltaGas U.S. to finance the Proposed Transaction.

- (a) After closing of the Proposed Transaction, AltaGas Ltd. is expected to maintain its investment grade credit ratings with both DBRS and S&P.

Post-closing capital structure of AltaGas U.S.:

AltaGas U.S. has been created as a Delaware limited liability corporation to hold AltaGas Ltd.'s utilities investments in the U.S.. Post-closing, it is expected that AltaGas U.S.'s capital structure will approximate 50percent debt to total capitalization. The actual amounts of debt and equity will depend on the final consideration paid subject to the adjustments as set forth in the Stock Purchase Agreement. The debt of AltaGas U.S. will be intercompany debt loaned from AltaGas Ltd. or an affiliate. The terms and conditions of the intercompany debt have not yet been determined by AltaGas Ltd. The terms and conditions of the intercompany debt of AltaGas U.S. owed to the parent will not affect the rates paid by customers.

Q8 PLEASE EXPLAIN WHY ALTAGAS LTD. AND ALTAGAS U.S. ARE FINANCIALLY FIT AND CAPABLE OF OWNING ENSTAR, APC AND CINGSA

1 A8 AltaGas Ltd. is financially capable of closing the Proposed Transaction. The Proposed
2 Transaction was valued at US\$1.135 billion, including assumption of approximately
3 US\$355 million of debt at Semco Holding. Cash to close the Proposed Transaction is
4 expected to be approximately US\$780 million, subject to adjustment as set forth in the
5 Stock Purchase Agreement. As I have previously described in A6 and A7, as at
6 December 31, 2011, AltaGas Ltd. had access to approximately C\$1.1 billion credit
7 facilities of which over C\$0.85 billion remained available. In addition, since January 1,
8 2012, AltaGas Ltd. has completed over C\$0.9 billion of debt and equity financing,
9 including (a) the subscription offering that was completed in February 2012 with
10 proceeds of C\$403 million held in trust; (b) closing of the US\$300 million unsecured
11 credit facility on March 2, 2012; and (c) issuance of C\$200 million MTNs in April 13,
12 2012.
13

14
15
16 Financial discipline is a fundamental cornerstone of AltaGas Ltd.'s strategy. AltaGas
17 Ltd. has the financial strength to finance the continued growth of ENSTAR, APC and
18 CINGSA after completion of the Proposed Transaction. AltaGas Ltd. is well-positioned
19 to fund its capital program through its growing internally-generated cash flow, its
20 dividend reinvestment plan, its available credit on bank lines and its continued strong
21 access to capital markets. It has a BBB investment grade rating from both S&P and
22 DBRS. Both of these credit rating agencies confirmed AltaGas Ltd.'s investment grade
23 credit rating with a stable trend after the announcement of the Proposed Transaction.
24

25 Furthermore, S&P views the Proposed Transaction to be positive for both AltaGas Ltd.

1 and SEMCO, as is evident from its February 9, 2012 Research Update entitled "*Ratings*
2 *on SEMCO Energy Inc. are Placed on Credit Watch Positive After Announced Sale to*
3 *AltaGas*" attached to Mr. Schreiber's testimony.

4 **Q9 PLEASE DESCRIBE THE EFFECT OF THE PROPOSED TRANSACTION ON**
5 **THE CAPITAL STRUCTURE OF ENSTAR, APC AND CINGSA.**

6
7 A9 The Proposed Transaction will not affect the capital structures of ENSTAR, APC or
8 CINGSA. AltaGas Ltd. has the financial strength to capitalize ENSTAR, APC and
9 CINGSA and they will be adequately funded in accordance with sound utility
10 management practices.

11 **Q10 PLEASE DESCRIBE THE EFFECT OF THE PROPOSED TRANSACTION ON**
12 **THE ABILITY OF ENSTAR, APC AND CINGSA TO ACCESS CAPITAL.**

13 A10 The Proposed Transaction will not impact the ability of ENSTAR, APC and CINGSA to
14 access capital. There are no covenants, agreements or legislative restrictions on AltaGas
15 Ltd. or AltaGas U.S. that would reduce or impair the ability of ENSTAR, APC or
16 CINGSA to access capital. As I have stated in A8, AltaGas Ltd. has the financial
17 strength to finance the continued growth of ENSTAR, APC and CINGSA after
18 completion of the Proposed Transaction through its growing internally-generated cash
19 flow, its dividend reinvestment plan, its available credit on bank lines and its continued
20 strong access to capital markets.

21 **Q11 DOES THIS CONCLUDE YOUR TESTIMONY?**

22
23 A11 Yes, it does.
24
25

Financing Commitment Letter

Exhibit DSS - 1

TD SECURITIES
THE TORONTO-DOMINION BANK
100 Wellington Street West
CP Tower, 27th Floor
Toronto, Ontario M5K 1A2

BMO CAPITAL MARKETS
BANK OF MONTREAL
2200, 333-7th Ave S.W.
Calgary, Alberta T2P 2Z1

RBC CAPITAL MARKETS
ROYAL BANK OF CANADA
Royal Bank Plaza, South Tower
200 Bay Street, P.O. Box 50
Toronto, Ontario M5J 2W7

CONFIDENTIAL

February 1, 2012

AltaGas Ltd
1700, 355 4th Avenue S.W.
Calgary, Alberta T2P 0J1

Attention: Shaun Toivanen, Treasurer

Ladies and Gentlemen:

Commitment Letter (US\$300,000,000 Facility)

We are pleased to advise AltaGas Ltd (the Borrower, AltaGas or you) that each of The Toronto-Dominion Bank (TD), Bank of Montreal (BMO) and Royal Bank of Canada (RBC) (collectively, the Lenders, we and us) has agreed to severally commit to provide US\$100,000,000 of the credit facility, in the aggregate maximum amount of US\$300,000,000 (the Facility) as more particularly described in the attached Summary of Terms and Conditions (the Term Sheet) and that each of TD Securities (TDS), BMO Capital Markets (BMOCM) and RBC Capital Markets (RBCCM) has agreed to arrange the Facility. TDS, BMO's and RBC's commitments to provide the above portions of the Facility and TDS, BMOCM's and RBCCM's agreement to arrange the Facility (collectively, the Undertaking) are subject to the terms and conditions set forth in this letter and the Term Sheet (collectively, the Commitment Letter) and the fee letter from TD, BMO and RBC dated the date hereof and delivered concurrently herewith (the Fee Letter) (collectively, the Commitment Papers) including the payment of the fees referred to in the Fee Letter.

TD will act as Administrative Agent for the Facility. TDS, BMOCM and RBCCM will act as Co-Lead Arrangers and Co-Bookrunners (in such capacities, the Lead Arrangers) and BMOCM and RBCCM will act as Co-Syndication Agents. You agree that no additional agents, co-agents, arrangers or bookrunners will be appointed, or other titles conferred, without the consent of the Lead Arrangers.

CONDITIONS TO COMMITMENT

The commitments of TD, BMO and RBC hereunder are subject to: (i) the preparation, execution and delivery of mutually acceptable loan documentation (the Credit Documentation) incorporating substantially the terms and conditions outlined in the Commitment Papers; (ii) the accuracy and completeness of all representations that you make to us and all information that you furnish to us and your compliance in all material respects with the terms of the Commitment Papers; (iii) the payment of all fees, expenses and other amounts payable under the Commitment Papers; and (iv) the other conditions set forth or referred to in the Term Sheet.

UNDERTAKING TERMINATION

The Undertaking set forth in the Commitment Papers will terminate on March 15, 2012 if the Credit Documentation has not been executed or the Facility has not closed on or prior to such date. Prior to such date, this Commitment Letter may be terminated (i) by you at any time at your option upon payment of all arranger fees, expenses and other amounts theretofore payable under this Commitment Letter or

(ii) by TD, BMO or RBC if any condition set forth in the immediately preceding paragraph captioned **Conditions to Commitment** becomes incapable of being satisfied.

NO SYNDICATION

Although the Lead Arrangers do not intend to syndicate the Facility to other financial institutions, each of TD, BMO and RBC reserves the right to assign any or all of its commitment under the Facility in accordance with the customary assignment provisions to be set forth in the Credit Documentation.

FEES

You agree to pay on the closing of the Facility the fees contemplated in the Fee Letter. Each of such fees will be non-refundable once paid.

INDEMNIFICATION

You agree to indemnify and hold harmless each of TD, BMO and RBC, their respective affiliates and their respective shareholders, officers, directors, employees, advisors and agents (each an indemnified person) from and against any and all losses, claims, damages, liabilities and expenses to which any such indemnified person may become subject or may incur arising out of or in connection with this Commitment Letter, the Facility, the use of the proceeds thereof (including the Acquisition (as that term is defined in the Term Sheet)), or any claim, litigation, investigation or proceeding relating to any of the foregoing, regardless of whether any indemnified person is a party thereto, and to reimburse each indemnified person upon demand for any reasonable legal or other expenses incurred in connection with investigating or defending any of the foregoing, provided that the foregoing indemnity will not, as to an indemnified person, apply to losses, claims, damages, liabilities or related expenses to the extent they are found by a final, non-appealable judgment of a court to arise directly from the willful misconduct or gross negligence of such indemnified person. You agree not to assert any claim against any indemnified person for special, indirect, consequential, punitive, or exemplary damages in connection in any way with the transactions described in or contemplated by this Commitment Letter. In the absence of fraud or willful misconduct by the applicable indemnified person, no indemnified person shall be liable for any damages arising from the use by unauthorized persons of information or other materials sent through electronic, telecommunications or other information transmission systems that are intercepted by such unauthorized persons.

You also agree to reimburse and indemnify each of TD, BMO and RBC and their respective affiliates in respect of all their reasonable costs and expenses (including the fees and disbursements of legal counsel) in connection with (i) the implementation of the Facility, the preparation, negotiation and administration of the Commitment Papers and the Credit Documentation (regardless of whether the Credit Documentation is executed or the closing occurs) and any amendment or waiver with respect thereto; and (ii) all reasonable costs and expenses of Administrative Agent, the Lead Arrangers and the Lenders in connection with the enforcement of the Credit Documentation.

CONFIDENTIALITY

By accepting delivery of the Commitment Papers, you agree that the Commitment Papers are for your confidential use only and that neither their existence nor the terms thereof will be disclosed by you to any person other than your officers, directors, employees, accountants, attorneys and other advisors, and then only on a "need to know" basis in connection with the transactions contemplated hereby and on a confidential basis. Notwithstanding the foregoing, following your acceptance of the provisions hereof: (i) you may make public disclosure of the existence and amount of the Undertaking and the identity of each of the Administrative Agent and the Lead Arrangers; and (ii) you may make such other public disclosures of the terms and conditions hereof as you are required by law, in the opinion of your counsel, to make. The Borrower agrees to permit the Lead Arrangers to review and approve any reference to the Lead Arrangers contained in any press release or similar public disclosure prior to public release.

Upon the execution of this Commitment Letter by the Borrower, and subject to closing of the Facility, the Lead Arrangers may, without the consent of the Borrower, disclose the relevant deal characteristics relating to this commitment (including the name of the borrower and any guarantors under the Facility) to the Loan Pricing Corporation (or successors thereof), and similar recognized bank loan information services so long as all information that is so disclosed is true and accurate. Further the Lead Arrangers shall be permitted to use information related to the arrangement of the Facility in connection with marketing, press releases or other transactional announcements or updates subject to confidentiality obligations or disclosure restrictions reasonably requested by you.

NO THIRD PARTY RELIANCE

The agreements of TD, BMO, BMOCM, RBC and RBCCM hereunder and of any Lender that issues a commitment to provide financing under the Facility are made solely for your benefit and may not be relied upon or enforced by any other person.

OTHER MATTERS

Please note that those matters that are not covered or made clear herein or in the Commitment Papers are subject to mutual agreement of the parties. The terms and conditions of the Commitment Papers may be modified only in writing.

The obligations of each of TD, BMO and RBC under this Commitment Letter are several (and not joint or joint and several) and apply only to itself and its actions (and not to any other Lead Arranger or Lender or the actions of any other Lead Arranger or Lender).

The indemnification and confidentiality provisions contained in this letter will remain in full force and effect regardless of whether or not the Credit Documentation is executed and notwithstanding any termination of the Undertaking, provided, however, that if definitive Credit Documentation is executed, the terms of such documentation will supersede the applicable terms of this Commitment Letter.

You acknowledge that TD, BMO, RBC and their respective affiliates may be providing debt financing, equity capital or other services (including, without limitation, financial advisory services) to other persons in respect of which the Borrower may have conflicting interests regarding the Facility and otherwise. Each of TD, BMO and RBC agrees not to use confidential information obtained from the Borrower by virtue of the Facility or their respective other relationships with the Borrower in connection with the performance by TD, BMO and RBC of services for other persons, and to not furnish any such information to other persons. The Borrower also acknowledges that TD, BMO and RBC have no obligation to use in connection with the Facility, or to furnish to the Borrower, confidential information obtained from other persons.

The Commitment Papers shall not be assignable by the Borrower without the prior written consent of the Lead Arrangers (and any purported assignment without such consent shall be null and void), are intended to be solely for the benefit of the Borrower and are not intended to confer any benefits upon or create any rights in favour of any person other than the parties hereto and the indemnified persons.

The Commitment Papers will be governed by, and construed in accordance with, the laws of the Province of Alberta and the federal laws of Canada applicable therein.

The Commitment Papers set forth the entire agreement between the parties with respect to the matters addressed therein and supersede all prior communications, written or oral, with respect thereto. This letter may be executed in any number of counterparts, each of which, when so executed, will be deemed to be an original and all of which, taken together, will constitute one and the same letter. Delivery of an executed signature page of this Commitment Letter by facsimile transmission or by e-mail in pdf format shall be effective as delivery of a manually executed counterpart hereof.

Please indicate your acceptance of the provisions hereof by signing the enclosed duplicate copy of this letter and returning same to the undersigned at or before 5:00 p.m., Calgary time on February 1, 2012 the time at which the Undertaking set forth above (if not accepted prior thereto) will expire.

Very truly yours,

THE TORONTO-DOMINION BANK

By _____

Name: _____
Title: _____

Clark Terrell
Managing Director

By _____

Name: _____
Title: _____

Carmen Angelescu
Vice President & Director

BANK OF MONTREAL

By _____

Name: _____
Title: _____

By _____

Name: _____
Title: _____

ROYAL BANK OF CANADA

By _____

Name: _____
Title: _____

By _____

Name: _____
Title: _____

Please indicate your acceptance of the provisions hereof by signing the enclosed duplicate copy of this letter and returning same to the undersigned at or before 5:00 p.m., Calgary time on February 1, 2012, the time at which the Undertaking set forth above (if not accepted prior thereto) will expire.


Very truly yours,

THE TORONTO-DOMINION BANK

By _____
Name _____
Title _____

By _____
Name _____
Title _____

BANK OF MONTREAL

By 
Name Carol McDonaki
Title Vice President

By _____
Name _____
Title _____

ROYAL BANK OF CANADA

By _____
Name _____
Title _____

By _____
Name _____
Title _____

Please indicate your acceptance of the provisions hereof by signing the enclosed duplicate copy of this letter and returning same to the undersigned at or before 5:00 p.m. (Calgary time on February 1, 2012, the time at which the Undertaking set forth above (if not accepted prior thereto) will expire.

Very truly yours,

THE TORONTO-DOMINION BANK

By: _____
Name:
Title:

By: _____
Name:
Title:

BANK OF MONTREAL

By: _____
Name:
Title:

By: _____
Name:
Title:

ROYAL BANK OF CANADA

By: _____
Name:
Title: **GERARD A. GILLES**
General Manager

By: _____
Name:
Title:

Accepted and agreed to this 1st day of February, 2012

ALTAGAS LTD.

By _____
Name: Deborah S. Stein
Title: Senior Vice President and
Chief Financial Officer

By _____
Name: _____
Title: _____

Final Short Form Prospectus

Exhibit DSS - 2

No securities regulatory authority has expressed an opinion about these securities and it is an offence to claim otherwise. This short form prospectus constitutes a public offering of these securities only in those jurisdictions where they may lawfully be offered for sale and therein only by persons permitted to sell such securities.

The securities offered hereby have not been and will not be registered under the United States Securities Act of 1933, as amended (the "1933 Act") or any state securities laws. Accordingly, these securities may not be offered or sold within the United States of America unless registered under the 1933 Act and applicable state securities laws or an exemption from such registration is available. This short form prospectus does not constitute an offer to sell or a solicitation of an offer to buy any of these securities within the United States of America. See "Plan of Distribution".

Information has been incorporated by reference in this prospectus from documents filed with securities commissions or similar authorities in Canada. Copies of the documents incorporated herein by reference may be obtained on request without charge from the Vice President, General Counsel and Corporate Secretary of AltaGas at 1700, 355 – 4th Avenue S.W., Calgary, Alberta, T2P 0J1 (telephone (403) 691-7575) and are also available electronically at www.sedar.com.

SHORT FORM PROSPECTUS

New Issue

February 14, 2012

AltaGas

ALTAGAS LTD.

\$350,900,000

12,100,000 Subscription Receipts

each representing the right to receive one Common Share

AltaGas Ltd. ("**AltaGas**") is hereby qualifying for distribution (the "**Offering**") 12,100,000 subscription receipts ("**Subscription Receipts**") of AltaGas at a price of \$29.00 per Subscription Receipt (the "**Offering Price**"). Each Subscription Receipt will entitle the holder thereof to receive, without payment of additional consideration or further action, and subject to the terms and conditions of the Subscription Receipt Agreement (as hereinafter defined), one common share (a "**Common Share**") of AltaGas upon the closing of the acquisition (the "**Acquisition**") by AltaGas Utility Holdings (U.S.) LLC ("**Acquireco**"), an indirect wholly-owned subsidiary of AltaGas, of all of the issued and outstanding shares of common stock (the "**SEMCO Shares**") of SEMCO Holding Corporation ("**SEMCO**") from Continental Energy Systems LLC ("**Continental**") pursuant to the terms and subject to the conditions of the Stock Purchase Agreement (as hereinafter defined). See "*Acquisition of SEMCO*", "*Details of the Offering*" and "*Plan of Distribution*".

The gross proceeds from the sale of the Subscription Receipts, net of half of the Underwriters' Fee (as hereinafter defined) with respect to the Subscription Receipts (the "**Escrowed Funds**") will be held by Computershare Trust Company of Canada, as subscription receipt agent (the "**Subscription Receipt Agent**"), and invested in short-term obligations of, or guaranteed by, the Government of Canada (and other approved investments), pending satisfaction of the Escrow Release Condition (as hereinafter defined), all pursuant to the terms of a subscription receipt agreement (the "**Subscription Receipt Agreement**") to be entered into on the Closing Date (as hereinafter defined) of the Offering among AltaGas, the Subscription Receipt Agent and BMO Nesbitt Burns Inc. ("**BMO**"), on its own behalf and for and on behalf of each of RBC Dominion Securities Inc. ("**RBC**"), TD Securities Inc. ("**TD**"), CIBC World Markets Inc. ("**CIBC**"), National Bank Financial Inc. ("**National**"), Scotia Capital Inc. ("**Scotia**"),

HSBC Securities (Canada) Inc. (“**HSBC**”), Macquarie Capital Markets Canada Ltd., Beacon Securities Limited, FirstEnergy Capital Corp. and Peters & Co. Limited (collectively, the “**Underwriters**”).

Provided that the Transaction Closing Date (as hereinafter defined) occurs on or before the Deadline (as hereinafter defined), the Escrowed Funds and the interest earned thereon (less the remaining portion of the Underwriters’ Fee to be paid and the Dividend Equivalent Payment (as hereinafter defined), if any) will be released to AltaGas (such amount being the “**Released Amount**”) and each holder of a Subscription Receipt will receive one Common Share for each Subscription Receipt held, without payment of additional consideration or further action, plus an amount per Common Share, if any, equal to the amount per Common Share of any cash dividends declared by AltaGas on the Common Shares to holders of record on a date during the period from and including the Closing Date up to but not including the Transaction Closing Date, net of any applicable withholding taxes (the “**Dividend Equivalent Payment**”). See “*Details of the Offering*”. AltaGas will utilize the Escrowed Funds to pay a portion of the purchase price of the SEMCO Shares pursuant to the Acquisition. See “*Use of Proceeds*”.

If the Transaction Closing Date does not occur prior to the Deadline, or if prior to such time the Stock Purchase Agreement is terminated in accordance with its terms or AltaGas advises the Subscription Receipt Agent and BMO, on behalf of the Underwriters, or discloses to the public that it does not intend to proceed with the Acquisition (each such case being a “**Termination**”), the Subscription Receipt Agent and AltaGas will return to holders of Subscription Receipts an amount per Subscription Receipt equal to the Offering Price of the Subscription Receipts plus a *pro rata* share of the interest earned on the Escrowed Funds, net of any applicable withholding taxes. See “*Details of the Offering*”.

Price: \$29.00 per Subscription Receipt

	Price to the Public	Underwriters’ Fee ⁽¹⁾	Net Proceeds to AltaGas ⁽²⁾
Per Subscription Receipt.....	\$29.00	\$1.16	\$27.84
Total ⁽³⁾	\$350,900,000	\$14,036,000	\$336,864,000

- (1) AltaGas has agreed to pay the Underwriters a fee equal to \$1.16 per Subscription Receipt (in aggregate, the “**Underwriters’ Fee**”). The Underwriters’ Fee is payable as to 50% upon the Closing Date and 50% on the release of the Escrowed Funds to AltaGas. If the Acquisition is not completed, the Underwriters’ Fee will consist solely of the amount payable upon the Closing Date.
- (2) Before deducting the estimated expenses of the Offering of approximately \$1,500,000 and excluding interest accrued on the Escrowed Funds accruing to AltaGas, if any. The expenses of the Offering will be paid from the general funds of AltaGas.
- (3) AltaGas has granted to the Underwriters an option (the “**Over-Allotment Option**”), exercisable at any time until 5:00 p.m. (Calgary time) on the 30th day following the Closing Date, to purchase up to an additional 1,815,000 Subscription Receipts on the same terms as set forth above. If the Over-Allotment Option is exercised in full, the total price to the public, the Underwriters’ Fee and the net proceeds to AltaGas, before expenses of the Offering and excluding interest accrued on the Escrowed Funds, if any, will be \$403,535,000, \$16,141,400 and \$387,393,600, respectively. See “*Plan of Distribution*”. A purchaser who acquires Subscription Receipts forming part of the Underwriters’ over-allocation position, if applicable, acquires those Subscription Receipts under this prospectus, regardless of whether the Underwriters’ over-allocation position is ultimately filled through the exercise of the Over-Allotment Option or secondary market purchases. The Subscription Receipts that may be issued on the exercise of the Over-Allotment Option are also qualified for distribution under this prospectus.

Underwriters’ Position	Maximum Size or Number of Securities Available	Exercise Period	Exercise Price
Over-Allotment Option.....	1,815,000 Subscription Receipts	30 days after the Closing Date	\$29.00 per Subscription Receipt

The issued and outstanding Common Shares are listed on the Toronto Stock Exchange (the “**TSX**”) under the symbol “**ALA**” and the cumulative redeemable 5-year rate reset Preferred Shares, Series A of AltaGas (the “**Preferred Shares, Series A**”) are listed on the TSX under the symbol “**ALA.PR.A**”. On January

31, 2012, the last completed trading day prior to the public announcement of the Offering and the Acquisition, the closing price of the Common Shares on the TSX was \$30.28 and the closing price of the Preferred Shares, Series A on the TSX was \$26.22. On February 13, 2012, the last completed trading day prior to the date of this short form prospectus, the closing price of the Common Shares on the TSX was \$29.79 and the closing price of the Preferred Shares, Series A on the TSX was \$26.18.

The TSX has conditionally approved the listing of the Subscription Receipts distributed under this short form prospectus and the Common Shares issuable upon exchange of the Subscription Receipts on the TSX. Listing of such securities is subject to AltaGas fulfilling all of the listing requirements of the TSX on or before May 7, 2012. The Offering Price of the Subscription Receipts offered hereunder was determined by negotiation between AltaGas and BMO, RBC and TD, on behalf of the Underwriters.

There is currently no market through which the Subscription Receipts may be sold and purchasers may not be able to resell Subscription Receipts purchased under this short form prospectus. This may affect the pricing of the Subscription Receipts in the secondary market, the transparency and availability of trading prices, the liquidity of the Subscription Receipts and the extent of issuer regulation. See “Risk Factors – Risks Related to the Acquisition – Market for Securities”.

The Underwriters, as principals, conditionally offer the Subscription Receipts, subject to prior sale, if, as and when issued and delivered by AltaGas to, and accepted by, the Underwriters in accordance with the conditions contained in the Underwriting Agreement referred to under “*Plan of Distribution*”, and subject to the approval of certain legal matters on behalf of AltaGas by Stikeman Elliott LLP and on behalf of the Underwriters by Blake, Cassels & Graydon LLP (collectively, “*Counsel*”).

In the opinion of Counsel, subject to the provisions of any particular plan, the Subscription Receipts and the Common Shares issued on exchange thereof, if issued on the date hereof, generally would be qualified investments under the *Income Tax Act* (Canada) (the “*Tax Act*”) for certain tax exempt trusts. See “*Eligibility for Investment*”.

Subscriptions will be received subject to rejection or allotment in whole or in part and the Underwriters reserve the right to close the subscription books at any time without notice. It is currently anticipated that the closing date of the Offering will be February 22, 2012, or such later date as AltaGas and the Underwriters may agree but in any event not later than March 15, 2012 (the “*Closing Date*”). See “*Plan of Distribution*”. Book entry only certificates representing the Subscription Receipts will be issued in registered form to CDS Clearing and Depository Services Inc. (“*CDS*”) or its nominee and will be deposited with CDS on the Closing Date. A purchaser of Subscription Receipts will receive only a customer confirmation from a registered dealer which is a CDS Participant (as hereinafter defined) and from or through which the Subscription Receipts are purchased. See “*Depository Services*”.

Subject to applicable laws, the Underwriters may, in connection with the offering, over-allot or effect transactions which stabilize or maintain the market price of the Subscription Receipts and the Common Shares at levels other than those which might otherwise prevail on the open market. Such transactions, if commenced, may be discontinued at any time. See “*Plan of Distribution*”.

The Underwriters propose to offer the Subscription Receipts initially at the Offering Price specified above. After a reasonable effort has been made to sell all of the Subscription Receipts at the price specified, the Underwriters may subsequently reduce the selling price to investors from time to time in order to sell any of the Subscription Receipts remaining unsold. Any such reduction will not affect the proceeds received by AltaGas. See “*Plan of Distribution*”.

It is important for an investor to consider the particular risk factors that may affect the industry in which it is investing, and therefore the stability of the dividends that it receives. See “*Risk Factors*” in the AIF (as hereinafter defined) incorporated by reference in this short form prospectus and the risks identified herein under the heading “*Risk Factors*” prior to making an investment in the Subscription Receipts. These sections also describe AltaGas’ assessment of those risk factors, as well as the potential consequences to an investor if a risk should occur.

BMO, RBC, TD, CIBC, National, Scotia and HSBC are, directly or indirectly, subsidiaries or affiliates of lenders to AltaGas or its subsidiaries. In addition, affiliates of each of TD, BMO and RBC have agreed to provide the New Credit Facility (as hereinafter defined) to AltaGas in connection with financing the Acquisition. BMO also acted as financial advisor to AltaGas in connection with the Acquisition. Accordingly, AltaGas may be considered a “connected issuer” of such Underwriters for the purposes of securities regulations in certain provinces of Canada. See “*Relationship Between AltaGas and Certain of the Underwriters*”.

AltaGas’ head and registered offices are located at 1700, 355 – 4th Avenue S.W., Calgary, Alberta T2P 0J1.

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GLOSSARY

In this prospectus, the following terms have the meanings set forth below:

“1998 Indenture” means the indenture between SEMCO Energy and the trustee thereunder dated as of October 23, 1998, as amended;

“Acquireco” means AltaGas Utility Holdings (U.S.) LLC, a limited liability corporation formed under the laws of Delaware and an indirect wholly-owned subsidiary of AltaGas;

“AIF” means the annual information form of AltaGas dated March 4, 2011 for the year ended December 31, 2010;

“AltaGas LP #1” means AltaGas Holding Limited Partnership No. 1, a limited partnership created pursuant to the laws of Alberta pursuant to an amended and restated limited partnership agreement dated as of June 28, 2005 among the General Partner, Holding Trust and each person who from time to time was accepted as and became a limited partner pursuant thereto;

“AltaGas LP #2” means AltaGas Holding Limited Partnership No. 2, a limited partnership created pursuant to the laws of Alberta pursuant to a limited partnership agreement dated as of March 26, 2004 among the General Partner, AltaGas LP #1 and each person who from time to time was accepted as and became a limited partner pursuant thereto;

“APC” means Alaska Pipeline Company, an indirect wholly-owned subsidiary of SEMCO;

“Arrangement” means the arrangement, under the provisions of section 192 of the CBCA, involving the Trust, AltaGas, the General Partner, AltaGas LP #1, AltaGas LP #2, Holding Trust, New AltaGas, New AltaGas 2, Computershare Trust Company of Canada (as trustee under the voting and exchange trust agreement of the Trust) and the Securityholders, pursuant to which the business of the Trust was reorganized into AltaGas effective July 1, 2010;

“AUGI Facility” means a \$200 million unsecured extendible revolving credit facility of AltaGas Utility Group Inc. maturing November 17, 2015;

“Bbls” means stock tank barrels of ethane and NGLs, expressed in standard 42 U.S. gallon barrels or 34.972 imperial gallon barrels;

“Bbls/d” means Bbls per day;

“Bcf” means 1,000,000 Mcf of natural gas;

“Bcf/d” means Bcf per day;

“Bilateral Facility” means a \$125 million bilateral demand credit facility;

“Canadian GAAP” or **“CGAAP”** means Canadian generally accepted accounting principles and practices, including without limitation, the principles set forth in the CICA Handbook published by the Canadian Institute of Chartered Accountants or any successor institute;

“**CBCA**” means the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44, as amended from time to time, including the regulations from time to time promulgated thereunder;

“**CDS Participant**” means a participant in the CDS depository service;

“**CES Credit Agreement**” means the US\$300,000,000 credit agreement among Continental and SEMCO and a syndicate of lenders dated as of November 19, 2008, as amended;

“**CINGSA**” means Cook Inlet Natural Gas Storage Alaska, LLC;

“**CINGSA Credit Agreement**” means the credit agreement among CINGSA and a syndicate of lenders dated as of November 14, 2011, as amended;

“**CINGSA Storage Project**” means the in-field storage facility in the Cook Inlet area of Alaska that will be constructed, owned and operated by CINGSA;

“**Credit Facilities**” means the Syndicated Facility, the LC Credit Facility, the AUGI Facility and the Bilateral Facility;

“**DBRS**” means DBRS Limited;

“**Deadline**” means 5:00 p.m. (Calgary time) on November 30, 2012;

“**ENSTAR**” means the Alaska natural gas distribution business conducted by SEMCO Energy under the name ENSTAR Natural Gas Company;

“**ERGSS**” means Eaton Rapids Gas Storage System;

“**Escrow Release Condition**” means the condition to be contained in the Subscription Receipt Agreement with respect to the release of the proceeds of the Offering to AltaGas and the issuance of the Common Shares pursuant to the Subscription Receipts (which condition shall substantially be that the parties to the Stock Purchase Agreement are able to complete the Acquisition in all material respects in accordance with the terms of the Stock Purchase Agreement without amendment or waiver materially adverse to the Corporation or Acquireco) but for payment of the purchase price to be satisfied in part by the release of the Escrowed Funds);

“**GCR**” means gas cost recovery;

“**General Partner**” means AltaGas General Partner Inc., a corporation amalgamated pursuant to the CBCA and a wholly-owned subsidiary of the Trust and, prior to the commencement of the transactions contemplated by the Arrangement, the general partner of AltaGas LP #1 and AltaGas LP #2 and the delegate of the trustee of the Trust;

“**Holding Trust**” means AltaGas Holding Trust, an unincorporated investment trust, all of the beneficial interests of which were owned by the Trust, established under the laws of Alberta pursuant to the declaration of trust dated as of March 26, 2004, between Computershare Trust Company of Canada and the Trust;

“**HSR Act**” means the *Hart-Scott-Rodino Antitrust Improvements Act of 1976*, as amended;

“LC Credit Facility” means a \$75 million unsecured extendible revolving term credit facility maturing on May 30, 2015;

“LP #1 B Units” means the Class B limited partnership units of AltaGas LP #1, which were non-transferable and were exchangeable into Trust Units on a one-for-one basis;

“LP #1 B Unitholders” means holders of LP #1 B Units;

“Mcf” means a thousand cubic feet of natural gas at standard imperial conditions of measurement;

“MDEQ” means Michigan Department of Environmental Quality;

“MGP” means manufactured gas plant;

“Mmcf” means a million cubic feet of natural gas at standard conditions of measurement;

“Mmcf/d” means million cubic feet per day;

“MPSC” means the Michigan Public Service Commission;

“MW” means megawatt; one MW is 1,000,000 watts; the watt is the basic electrical unit of power;

“New AltaGas” means AltaGas Conversion Inc., a corporation incorporated pursuant to the CBCA for the sole purpose of participating in the Arrangement;

“New AltaGas 2” means AltaGas Conversion #2 Inc., a corporation incorporated pursuant to the CBCA for the sole purpose of participating in the Arrangement;

“New Credit Facility” means a US\$300 million senior unsecured revolving one year credit facility to be provided by a syndicate of Canadian banks;

“NGL” means those hydrocarbon components that can be recovered from natural gas as liquids, including, but not limited to, ethane, propane, butanes, pentanes plus, condensate and small quantities of non-hydrocarbons;

“Note Trustee” means Computershare Trust Company of Canada, as initial trustee under the Trust Indenture, and any successor thereto or replacement thereof;

“Outside Date” means March 31, 2013, subject to certain conditions and provided that if the failure of the closing of the Acquisition to occur is the result of either: (a) the Required Regulatory Approvals not having been obtained or the Required Regulatory Approvals having been obtained but subject to conditions or requirements imposing on AltaGas, Acquireco or Continental any condition or requirement that any of AltaGas, Acquireco or Continental, as applicable, is not required to accept pursuant to the Stock Purchase Agreement; or (b) the failure to receive payoff documentation from the holders of indebtedness under the CES Credit Agreement and the SEMCO Credit Agreement providing that upon repayment by Acquireco of indebtedness of SEMCO and certain of its subsidiaries thereunder, all liens securing such indebtedness shall be terminated and released to the extent such liens do not also secure indebtedness under the indenture governing the Senior Notes, the 1998 Indenture or the CINGSA Credit Agreement with respect to such indebtedness and SEMCO and certain of its subsidiaries shall be released from their obligations with respect to such indebtedness; and the parties shall not have received

documentation that SEMCO has been released from its obligations in respect of a certain credit agreement swap entered into by Continental and SEMCO and any collateral and credit support provided by SEMCO or any subsidiary in connection therewith has been cancelled or returned to SEMCO; and provided that all other conditions to closing the Acquisition have been fulfilled or are capable of being fulfilled, then the “**Outside Date**” will be June 30, 2013;

“**Part V**” means Canadian GAAP set out in Part V of the CICA Handbook – Accounting;

“**Preferred Shares**” means the preferred shares of any series in the capital of AltaGas, including without limitation the Preferred Shares, Series A;

“**RAP**” means Remedial Action Plan;

“**RCA**” means the Regulatory Commission of Alaska;

“**Required Regulatory Approvals**” means, collectively: (a) approval by the MPSC under Michigan Compiled Laws 460.6q, as added by 2008 Public Act 286; and (b) the RCA under Alaska Statutes 42.05.281 and related orders and regulations as obtained by or with respect to SEMCO or its subsidiaries and as obtained by or with respect to AltaGas or Acquireco or their subsidiaries, in each case in connection with the execution, delivery and performance of the Stock Purchase Agreement and the ancillary documents or the consummation of the Acquisition;

“**Securityholders**” means, collectively, the Unitholders and the LP #1 B Unitholders;

“**SEDAR**” means the System for Electronic Document Analysis and Retrieval;

“**SEMCO Credit Agreement**” means the credit agreement among SEMCO Energy and a syndicate of lenders dated as of November 9, 2007, as amended;

“**SEMCO Energy**” means SEMCO Energy, Inc.;

“**Senior Notes**” means US\$300 million senior secured notes of SEMCO Energy maturing April 21, 2020 bearing interest at an annual rate of 5.15%;

“**Shareholders**” means the holders of Common Shares;

“**S&P**” means Standard & Poor’s Ratings Services;

“**Stock Purchase Agreement**” means the stock purchase agreement dated February 1, 2012 by and among AltaGas, Acquireco, SEMCO and Continental pursuant to which Acquireco agreed to acquire the SEMCO Shares for an aggregate purchase price of US\$1,135,000,000, subject to adjustment, including approximately US\$355,000,000 in assumed debt, all as more particularly described under “*Acquisition of SEMCO*”;

“**Syndicated Facility**” means a \$600 million unsecured extendible revolving facility with a syndicate of Canadian chartered banks currently scheduled to mature on May 30, 2015;

“**Tcf**” means trillion cubic feet;

“**Transaction Closing Date**” means the date on which the purchase and sale of the SEMCO Shares occurs pursuant to the Stock Purchase Agreement;

“**Trust**” means AltaGas Income Trust, an unincorporated open-ended investment trust established under the laws of Alberta pursuant to a declaration of trust dated as of March 26, 2004 and dissolved pursuant to the Arrangement on July 1, 2010;

“**Trust Indenture**” means the amended and restated trust indenture dated July 1, 2010 between AltaGas and the Note Trustee providing for the issuance of debt securities;

“**Trust Units**” means trust units of the Trust;

“**TSX**” means the Toronto Stock Exchange;

“**Underwriting Agreement**” means the underwriting agreement dated February 1, 2012 between AltaGas and the Underwriters and pursuant to which AltaGas has agreed to sell an aggregate of 12,100,000 Subscription Receipts to the Underwriters and the Underwriters have severally (and not jointly or jointly and severally) agreed to purchase from AltaGas, as principals, such Subscription Receipts on the Closing Date;

“**United States**” or “**U.S.**” means the United States of America, its territories and possessions, any State of the United States, and the District of Columbia;

“**Unitholders**” means holders of Trust Units; and

“**U.S. GAAP**” means United States generally accepted accounting principles.

EXCHANGE RATE DATA

The following table sets forth, for the periods indicated, the high, low, average and period-end noon spot rates of exchange of one U.S. dollar, expressed in Canadian dollars, published by the Bank of Canada.

	Nine months ended September 30,	Year ended December 31,		
	2011	2011	2010	2009
	\$	\$	\$	\$
Highest rate during the period.....	1.0482	1.0658	1.0848	1.3066
Lowest rate during the period	0.9407	0.9407	0.9931	1.0251
Average noon spot rate for the period ⁽¹⁾	0.9781	0.9891	1.0299	1.1420
Rate at the end of the period	1.0482	1.0170	0.9946	1.0510

Note:

(1) Determined by averaging the rates on the last business day of each month during the respective period.

On February 13, 2012, the noon rate of the exchange posted by the Bank of Canada for conversion of U.S. dollars into Canadian dollars was US\$1.00 equals \$0.9996.

IMPORTANT NOTICE ABOUT INFORMATION IN THIS PROSPECTUS

Prospective investors should rely only on the information contained in or incorporated by reference into this prospectus. AltaGas has not authorized any other person to provide prospective investors with additional or different information. If anyone provides prospective investors with different or inconsistent information, prospective investors should not rely on it. AltaGas is offering to sell, and seeking offers to buy, the Subscription Receipts only in jurisdictions where offers and sales are permitted. Prospective investors should assume that the information appearing in this prospectus, as well as information AltaGas has previously filed with the securities regulatory authority in each of the provinces of Canada that is incorporated herein by reference, is accurate as of their respective dates only. AltaGas' business, financial condition, results of operations and prospects may have changed since those dates.

In this prospectus, unless otherwise specified or the context otherwise requires, all dollar amounts are expressed in Canadian dollars. References to "dollars" or "\$" are to the lawful currency of Canada. References to "U.S. dollars" or "US\$" are to the lawful currency of the United States.

Unless otherwise indicated, all financial information included and incorporated by reference in this prospectus is determined using Canadian GAAP – Part V which is in effect from time to time. The audited financial statements of SEMCO as at and for the years ended December 31, 2010 and 2009, and the unaudited financial statements of SEMCO as at and for the three and nine month periods ended September 30, 2011 and 2010 included in this prospectus have been prepared in accordance with U.S. GAAP and may not be comparable to financial statements of Canadian companies prepared in accordance with Canadian GAAP – Part V or Canadian GAAP. Reference should be made to note 13 in the audited financial statements of SEMCO as at and for the years ended December 31, 2010 and 2009, and note 10 in the unaudited financial statements of SEMCO as at and for the three and nine month periods ended September 30, 2011 and 2010 for a discussion of the principal differences between SEMCO's financial results for the periods covered by such financial results and financial condition determined under U.S. GAAP and Canadian GAAP – Part V.

For financial years commencing on or after January 1, 2012 and for the interim periods therein, AltaGas intends to prepare and file its consolidated financial statements in accordance with U.S. GAAP. Information for the comparative periods presented in the aforementioned consolidated financial statements will also be prepared in accordance with U.S. GAAP. See "*Recent Developments – Conversion to U.S. GAAP*".

DOCUMENTS INCORPORATED BY REFERENCE

Information has been incorporated by reference in this short form prospectus from documents filed with securities commissions or similar authorities in Canada. Copies of the documents incorporated herein by reference may be obtained on request without charge from the Vice President, General Counsel and Corporate Secretary of AltaGas at 1700, 355 – 4th Avenue S.W., Calgary, Alberta, T2P 0J1 (telephone (403) 691-7575). In addition, copies of the documents incorporated herein by reference may be obtained from the securities commissions or similar authorities in Canada through the SEDAR website at www.sedar.com.

The following documents of AltaGas, which have been filed with the various securities commissions or similar regulatory authorities in the provinces of Canada, are specifically incorporated into and form an integral part of this short form prospectus:

- (a) the AIF;
- (b) the amended audited consolidated financial statements of AltaGas and notes thereto as at and for the years ended December 31, 2010 and 2009 together with the auditors' report thereon filed on March 18, 2011, and the amended management's discussion and analysis of results of operations and financial condition for the year ended December 31, 2010 filed on March 18, 2011 (the "**2010 MD&A**");
- (c) the unaudited comparative consolidated financial statements of AltaGas and notes thereto as at September 30, 2011 and for the three and nine month periods ended September 30, 2011 and 2010, and the management's discussion and analysis of results of operations and financial condition for the three and nine month periods ended September 30, 2011 (the "**2011 Q3 MD&A**");
- (d) the information circular dated May 4, 2010 relating to the Annual and Special Meeting of holders of Trust Units and holders of LP #1 B Units held on June 3, 2010;
- (e) the information circular dated March 15, 2011 relating to the Annual General Meeting of holders of Common Shares held on April 20, 2011;
- (f) the material change report dated October 31, 2011 relating to the proposed acquisition of Pacific Northern Gas Ltd. ("**PNG**") described under "*Recent Developments – Acquisition of Pacific Northern Gas Ltd.*";
- (g) the material change report dated December 21, 2011 relating to the acquisition of PNG described under "*Recent Developments – Acquisition of Pacific Northern Gas Ltd.*"; and
- (h) the material change report dated February 6, 2012 relating to the Acquisition described under "*Acquisition of SEMCO*".

Any documents of the type required by National Instrument 44-101 — *Short Form Prospectus Distributions* to be incorporated by reference in a short form prospectus including any material change reports (excluding material change reports filed on a confidential basis), comparative interim financial statements, comparative annual financial statements and the auditors' report thereon, management's discussion and analysis of financial condition and results of operations, information circulars, annual information forms, business acquisition reports and any press release containing financial information for periods more recent than the most recent annual or interim financial statements filed by AltaGas with the securities commissions or similar authorities in the provinces of Canada subsequent to the date of this short form prospectus and prior to the termination of this distribution, are deemed to be incorporated by reference in this short form prospectus.

Any statement contained in a document incorporated or deemed to be incorporated by reference herein shall be deemed to be modified or superseded for the purposes of this short form prospectus to the extent that a statement contained herein or in any other subsequently filed document which also is, or is deemed to be, incorporated by reference herein modifies or supersedes such statement. The modifying or superseding statement need not state that it has modified or superseded a prior statement or include any other information set forth in the document that it modifies or supersedes. The making of a modifying or superseding statement shall not be deemed an admission for any purposes that the modified or superseded statement, when made, constituted a misrepresentation, an untrue statement of a material fact or an

omission to state a material fact that is required to be stated or that is necessary to make a statement not misleading in light of the circumstances in which it was made. Any statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this short form prospectus.

NOTE REGARDING FORWARD-LOOKING STATEMENTS

This prospectus and the documents incorporated by reference herein contain forward-looking statements. When used in this prospectus and the documents incorporated by reference herein, the words “may”, “would”, “could”, “will”, “intend”, “plan”, “anticipate”, “believe”, “seek”, “propose”, “estimate”, “expect” and similar expressions, as they relate to AltaGas or an affiliate of AltaGas, are intended to identify forward-looking statements. In particular, this prospectus and the documents incorporated by reference herein contain forward-looking statements with respect to, among other things, business objectives, expected growth, results of operations, performance, business projects and opportunities and financial results.

Specifically, and as at the date hereof, such forward-looking statements are set forth in respect of AltaGas’ overall strategy under the heading “*AltaGas’ Strategy*” in the AIF, including with respect to the relative contribution of the gas, power and utility businesses to revenue growth, statements as they relate to gas opportunities with respect to: expectations for the Western Canada Sedimentary Basin (“WCSB”); growth opportunities from plant modifications, increasing interests, acquiring and constructing infrastructure and growing demand; the anticipated impact of the Harmattan Co-Stream Project and the Gordondale project; the contribution of AltaGas’ extraction infrastructure to throughput, utilization and profitability; the availability of opportunities to build or acquire gathering, processing, extraction or transmission infrastructure and generate operating synergies; and the impact of growing natural gas production in northeast British Columbia and northwest Alberta; statements as they relate to power opportunities with respect to: power demand growth and price recovery; the timing of new power generation and the impact of the planned decommissioning of thermal plants in Alberta, opportunities to develop new clean power generation capacity, the anticipated impact of the northwest British Columbia run-of-river hydro-electricity projects, including the Forrest Kerr Project; and statements as they relate to utility opportunities to build or expand natural gas distribution infrastructure in Alberta, British Columbia, Nova Scotia or the Northwest Territories. In addition, such forward-looking statements are set forth under:

- “*Gas Division – Extraction and Transmission*”, including in respect of expectations for volume commitments for 2011 and thereafter in relation to Suffield and the extension of the life of the Kahntah pipeline asset;
- “*Gas Division – Field Gathering and Processing*”, including in respect of expectations with respect to levels of producer activity and demand for gathering and processing facilities and services and AltaGas’ competitiveness in the midstream marketplace;
- “*Power Division*”, including in respect of expectations for growth through renewable energy projects, the timing of construction and completion of the Forrest Kerr Project, the timing of development and the environmental attributes of the Glenridge Wind Development project, the timing of development and construction for the McLymont Creek, Volcano, Log Creek and Kookipi Creek run-of-river projects, the ability to generate further growth for the power infrastructure business with its renewable energy portfolio, the long-term price environment for power, the drivers of growth in the power

business and the timing of development and intentions with respect to the development of AltaGas' hydroelectric and other wind power development projects in Canada and the United States; and

- “*Utility Division*”, including in respect of expectations for growth in new service sites and activations, capital expenditures for 2011 and access to adequate supplies of natural gas,

in the AIF incorporated by reference herein and under the headings “*Strategy*”; “*Gas Business – Description of Assets – Capitalizing on Opportunities*”; “*Gas Business – Gas Outlook*”; “*Power Business – Description of Assets – Capitalizing on Opportunities*”; “*Power Business – Power Outlook*”; “*Utility – Description of Assets – Capitalizing on Opportunities*”; “*Utility – Utility Outlook*”; “*Growth Capital*”; “*Consolidated Outlook*”; and “*Corporate – Corporate Outlook*” in the 2010 MD&A and comparable sections in the 2011 Q3 MD&A.

This prospectus also contains forward-looking statements with respect to:

- the Offering, including in respect of the use of proceeds from the Offering and the expected Closing Date of the Offering;
- expected AltaGas financial performance;
- the Acquisition of SEMCO (as set forth under “*Acquisition of SEMCO*”), including:
 - the expected Transaction Closing Date of the Acquisition;
 - the aggregate cash consideration payable by Acquireco in connection therewith and the anticipated sources of financing thereof;
 - expected future debt and Preferred Share financings;
 - anticipated benefits of the Acquisition, including:
 - expectations regarding the strategic fit of SEMCO with AltaGas' existing business and its contribution to earnings, consolidated EBITDA and future cash flows, including expected accretion thereof;
 - expectations regarding the stability of cash flows from SEMCO's business, including the proportion of EBITDA derived from regulated and long-term contracted assets; and
 - the growth opportunities associated with SEMCO's business, including:
 - expected growth of SEMCO's customer base in Michigan, its rate base and the expectations relating to Michigan's economy improving;

- expectations relating to customer conversions from alternative fuel sources to natural gas in Michigan and expectations regarding the relative costs of natural gas and other fuel sources;
- expected growth of ENSTAR's customer base and rate base and the contribution to such growth from expected activity levels in the resource sector;
- growth projects in Alaska, including pursuant to system enhancements and expansions and the potential to expand the CINGSA Storage Project;
- the anticipated in-service date of CINGSA, its benefits in relation to ENSTAR's ability to meet seasonal customer demands and the capital expenditures associated therewith and the storage capacity thereof; and
- expectations with respect to the completion and submission of RAPs to MDEQ in relation to MGP sites and the accruals made by SEMCO in relation thereto;
- the entrance into, the terms of, and the anticipated indebtedness to be incurred under, the New Credit Facility; and
- the expected in service dates of the projects associated with recent electricity purchase agreements entered into by AltaGas (as set forth under "*Recent Developments – Electricity Purchase Agreements for McLymont Creek and Volcano Creek Hydro-electric Projects*") as well as the in service date with respect to the Forrest Kerr run-of-river power project currently under construction.

These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. Such statements reflect AltaGas' then current views with respect to future events based on certain material facts and assumptions and are subject to certain risks and uncertainties, including without limitation changes in market, competition, governmental or regulatory developments and general economic conditions and the other factors described under the heading "*Risk Factors*" in the AIF and this prospectus. The material assumptions in making these forward-looking statements are disclosed in the AIF and the 2010 MD&A, respectively, as may be modified or superseded by documents incorporated or deemed to be incorporated by reference herein, under the headings set forth above and comparable sections in the 2011 Q3 MD&A and, in respect of the Acquisition of SEMCO, set forth under "*Acquisition of SEMCO*".

Many factors could cause AltaGas' or any of its business segment's actual results, performance or achievements to vary from those described in this prospectus and the documents incorporated by reference herein, including without limitation those listed above as well as the assumptions upon which they are based proving incorrect. These factors should not be construed as exhaustive. Should one or more of these risks or uncertainties materialize, or should assumptions underlying forward-looking statements prove incorrect, actual results may vary materially from those described in this prospectus and the documents incorporated by reference herein as intended, planned, anticipated, believed, sought, proposed, estimated or expected, and such forward-looking statements should not be unduly relied upon. These statements speak only as of the date of this prospectus or as of the date specified in the documents incorporated by reference herein, as the case may be. AltaGas does not intend, and does not assume any

obligation, to update these forward-looking statements except as required by law. The forward-looking statements contained in this prospectus and the documents incorporated by reference herein are expressly qualified by these cautionary statements.

Financial outlook information contained in this prospectus and the documents incorporated by reference herein about prospective results of operations, financial position or cash flows is based on assumptions about future events, including economic conditions and proposed courses of action, based on management's assessment of the relevant information currently available. Readers are cautioned that such financial outlook information contained in this prospectus and the documents incorporated by reference herein should not be used for the purposes other than for which it is disclosed herein or therein, as the case may be.

NON-GAAP FINANCIAL MEASURES

This prospectus and the documents incorporated by reference herein contain references to certain financial measures that do not have a standardized meaning prescribed by Part V and may not be comparable to similar measures presented by other entities. These measures provide additional information that management believes is meaningful regarding AltaGas' operational performance, liquidity and its capacity to fund dividends, capital expenditures and other investing activities. Investors are cautioned, however, that these measures should not be construed as an alternative to net earnings, cash from operations or other cash flow measures, as applicable, determined in accordance with Part V as an indication of AltaGas' performance.

References to net revenue, operating income, EBITDA, adjusted net income and funds from operations throughout this prospectus and/or the documents incorporated by reference herein have the following definitions and business rationale:

- Net revenue, which is revenue less the cost of commodities purchased for sale and shrinkage, is a better reflection of performance than revenue, since changes in the market price of natural gas and power affect both revenue and cost of sales;
- Operating income is a measure of AltaGas' profitability from its principal operating activities prior to how these activities are financed, how the results are taxed, or the impact of unrealized gains or losses on risk management contracts. The measure is used by management to assess the operating performance of the business segments since it is a better indicator of operating performance than net income. Operating income is calculated from the Consolidated Statements of Income using revenue adjusted for unrealized gains or losses on risk management contracts less operating and administrative expenses;
- EBITDA is a measure of AltaGas' operating profitability without the impact of risk management contracts and prior to how business activities are financed, assets are amortized or how earnings are taxed. AltaGas does not speculate on commodity prices, but rather enters into financial instruments to manage risk, and therefore evaluates company performance excluding unrealized gains or losses from risk management contracts. EBITDA is calculated from the Consolidated Statements of Income using revenue adjusted for unrealized gains or losses on risk management contracts, cost of sales and operating and administrative expenses;
- Adjusted net income is a better reflection of actual business performance than net income since changes in value of risk management contracts are subject to end of period prices for equities,

commodities, interest rates and foreign exchange. Management evaluates the overall performance of AltaGas' business prior to accounting for unrealized gains or losses from risk management activities. Adjusted net income is calculated from the Consolidated Statements of Income and is defined as net income adjusted for unrealized gains or losses on risk management contracts and related income tax expenses; and

- Funds from operations are used to assist management and investors in analyzing financial performance without regard to changes in non-cash working capital in the period. Funds from operations are calculated from the Consolidated Statements of Cash Flows and are defined as cash provided by operating activities before changes in non-cash working capital and expenditures incurred to settle asset retirement obligations.

Reconciliations of such Non-Part V financial measures are provided in AltaGas' 2010 MD&A and 2011 Q3 MD&A for the periods set out therein.

ALTAGAS LTD.

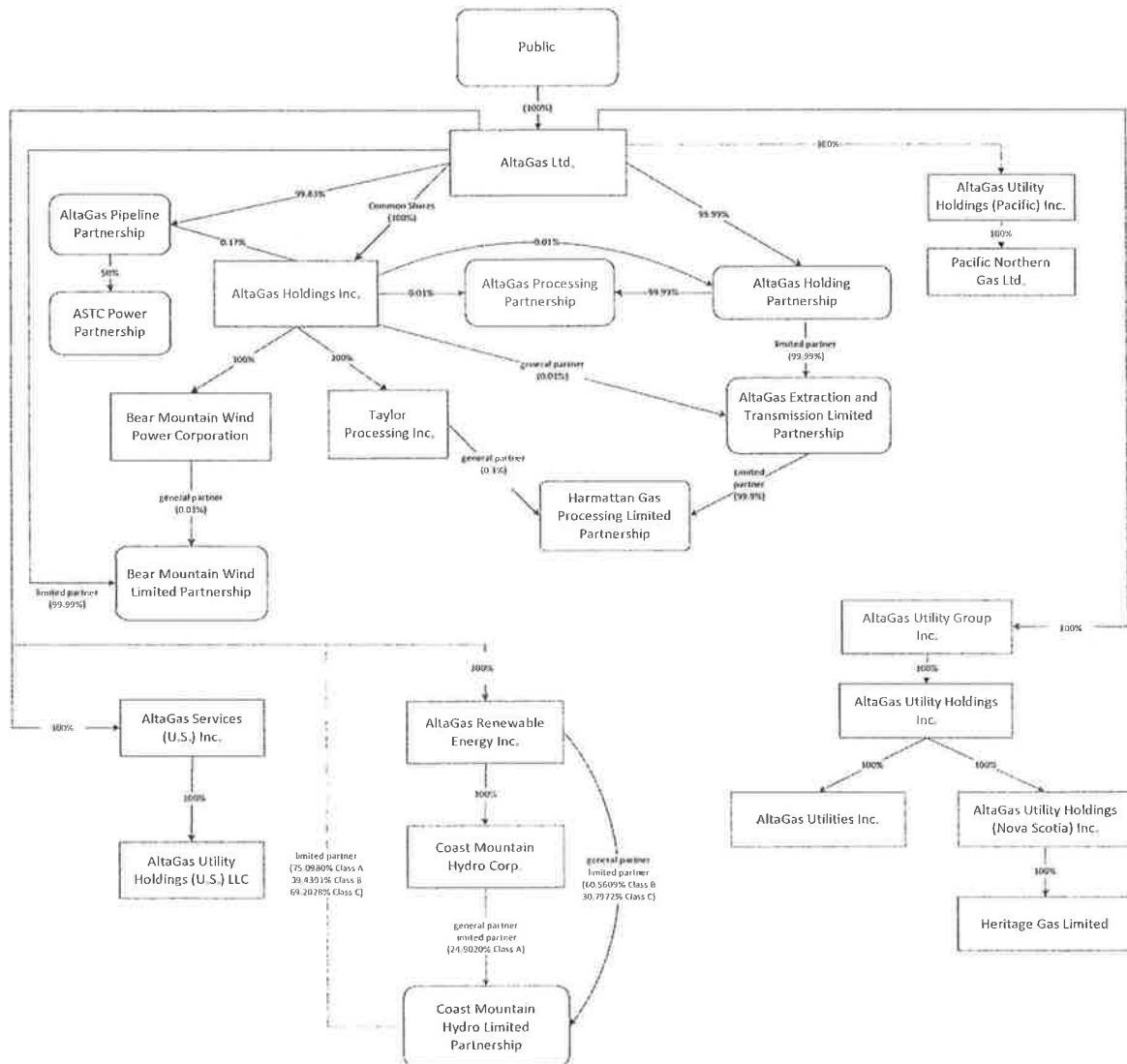
General

AltaGas is the successor to the Trust following the completion of the reorganization of the Trust from an income trust structure to a corporate structure by way of the Arrangement on July 1, 2010. The Arrangement involved, among other things, the exchange, on a one-for-one basis, of all outstanding Trust Units and LP #1 B Units, for Common Shares. In addition, each of AltaGas LP #1 and AltaGas LP #2 were liquidated and dissolved and the Trust and Holding Trust were wound-up. AltaGas is the continuing corporation resulting from the amalgamation of AltaGas Ltd. (as it then was), AltaGas Conversion Inc. and AltaGas Conversion #2 Inc. pursuant to the Arrangement.

AltaGas' head and registered offices are located at 1700, 355 – 4th Avenue S.W., Calgary, Alberta T2P 0J1.

Structure of AltaGas

The following chart describes the inter-corporate relationships among the entities within the structure of AltaGas.



Note:

- (1) Each corporation listed above (other than Taylor Processing Inc., AltaGas Renewable Energy Inc., AltaGas Services (U.S.) Inc., AltaGas Utility Holdings (U.S.) LLC, Coast Mountain Hydro Corp., AltaGas Utility Holdings (Nova Scotia) Inc. and Pacific Northern Gas Ltd.) is a corporation incorporated or formed by amalgamation or continuance under the CBCA. Each of Taylor Processing Inc. and AltaGas Utility Holdings (Nova Scotia) Inc. is a corporation incorporated under the *Business Corporation Act* (Alberta), each of AltaGas Renewable Energy Inc., Coast Mountain Hydro Corp. and Pacific Northern Gas Ltd. is a corporation incorporated under the *Business Corporation Act* (British Columbia) and each of AltaGas Services (U.S.) Inc. and AltaGas Utility Holdings (U.S.) LLC is a corporation formed under the laws of Delaware. Each partnership listed above (other than AltaGas Holding Partnership, Bear Mountain Wind Limited Partnership and Coast Mountain Hydro Limited Partnership) was established under the laws of Alberta. AltaGas Holding Partnership was established under the laws of Ontario and each of Bear Mountain Wind Limited Partnership and Coast Mountain Hydro Limited Partnership was established under the laws of British Columbia.

Business of AltaGas

AltaGas' vision is to be a leading North American energy infrastructure company with a focus in Canada and the northern and western United States. AltaGas' overall objective is to generate superior economic returns by investing in low-risk, long-life energy assets underpinned by contracts with strong counterparties or regulated returns. Over the past eighteen years AltaGas has built a portfolio of assets that provide the platform to support its future growth. AltaGas will continue to seek to invest in projects that provide returns that are accretive to cash flow and earnings and which in turn provide stable and growing dividends and capital appreciation.

AltaGas is an energy infrastructure business with a focus on natural gas, power and regulated utilities. With physical and economic links along the energy value chain together with its efficient and reliable assets, market knowledge and financial discipline, AltaGas has provided strong, stable and predictable returns for its investors. AltaGas focuses on maximizing the profitability of its assets, providing services that are complementary to its existing businesses, and growing through the acquisition and development of energy infrastructure.

At the end of 2010, AltaGas completed an internal reorganization that formally established three operating divisions, Gas, Power and Utility. AltaGas' Gas business touches more than 2 Bcf/d of gas and includes natural gas gathering and processing, extraction, transmission and storage assets and businesses. The Power business includes conventional power generation assets located in Alberta and renewable power generation assets located in British Columbia. The Utility business is a business in which earnings are driven primarily by regulated rates of return and cost-of-service recovery and comprised of natural gas transmission and distribution assets.

At December 31, 2010, AltaGas reported consolidated financial and operating results on the basis of four reporting segments:

- Gas
 - Extraction and Transmission consists of AltaGas' interests in ethane and NGL extraction plants and natural gas and NGL transmission systems;
 - Field Gathering and Processing includes AltaGas' natural gas gathering and processing business; and
 - Energy Services consists of two main businesses: energy management services and gas services.
- Power
 - AltaGas' interests in coal-fired and gas-fired generation, wind power, run-of-river power and interests in wind and run-of-river renewable power projects under development.
- Utility
 - Natural gas transmission and distribution facilities in Alberta, Nova Scotia and the Northwest Territories, Canada.

- Corporate
 - Corporate includes the cost of providing services and general corporate overhead, investments in public and private entities and the effects of the changes in the value of risk management assets and liabilities.

In support of its vision and overarching goal of creating long-term shareholder value, AltaGas' strategy has remained focused on four key themes:

- Optimize its existing businesses by focusing on safe and reliable service to its customers and capitalizing on the strategic location of its current assets;
- Grow and diversify its Gas, Power and Utility infrastructure platform;
- Maintain its financial strength and flexibility; and
- Continue to develop its organizational capability to support the strategy.

AltaGas' board of directors reviews the strategy annually, consistent with its mandate of overseeing and directing AltaGas' strategic direction. AltaGas continually assesses the macro-economic and micro-economic trends impacting its business and seeks opportunities to generate value for shareholders, including acquisitions, dispositions or other strategic transactions. Opportunities that AltaGas determines to pursue must meet strategic, operating and financial criteria.

ACQUISITION OF SEMCO

The Acquisition

On February 1, 2012, AltaGas and Acquireco entered into the Stock Purchase Agreement with Continental and SEMCO pursuant to which Acquireco agreed to acquire all of the issued and outstanding SEMCO Shares for aggregate consideration of US\$1,135,000,000, subject to adjustment, including approximately US\$355,000,000 in assumed debt. See "*Acquisition of SEMCO – The Acquisition Agreement*". SEMCO is the sole shareholder of SEMCO Energy, a privately held regulated public utility company headquartered in Port Huron, Michigan with natural gas distribution operations in Alaska and Michigan.

The audited financial statements of SEMCO as at and for the years ended December 31, 2010 and 2009, the unaudited financial statements of SEMCO as at and for the three and nine month periods ended September 30, 2011 and 2010 and AltaGas' unaudited *pro forma* consolidated financial statements for the year ended December 31, 2010 and as at and for the nine month period ended September 30, 2011, in each case after giving effect to the Acquisition and the related financing assumptions as described in the *pro forma* consolidated financial statements which are included in this prospectus as if such occurred January 1, 2010 and the related financing assumptions as described in the *pro forma* consolidated financial statements, are included as an appendix to this prospectus. See "*Acquisition of SEMCO – Selected Unaudited Pro Forma Consolidated Financial Information*".

The closing of the Acquisition is subject to receipt of the Required Regulatory Approvals, approvals under the HSR Act and the satisfaction or waiver of certain closing conditions. The closing of the Acquisition is expected to occur in the third quarter of 2012. See "*Acquisition of SEMCO – The Acquisition Agreement – Closing Conditions*".

AltaGas expects that cash to close the Acquisition of approximately US\$780 million will be provided from a combination of equity and debt; specifically: (i) the net proceeds from the Offering; (ii) the New Credit Facility; (iii) the Credit Facilities; and (iv) future debt and Preferred Share financings. See “*Acquisition of SEMCO – The Acquisition Agreement*”, “*– Financing the Acquisition*” and “*Use of Proceeds*”.

Business of SEMCO

SEMCO’s primary business is regulated gas distribution (the “**Gas Distribution Business**”). The Gas Distribution Business accounted for approximately 99% of SEMCO’s 2010 consolidated operating revenues. SEMCO has other businesses, including operations and investments in propane distribution, intrastate natural gas pipelines and a natural gas storage facility in Michigan. The Gas Distribution Business purchases, transports, distributes and sells natural gas and related gas distribution services to residential, commercial and industrial customers and is SEMCO’s largest business segment.

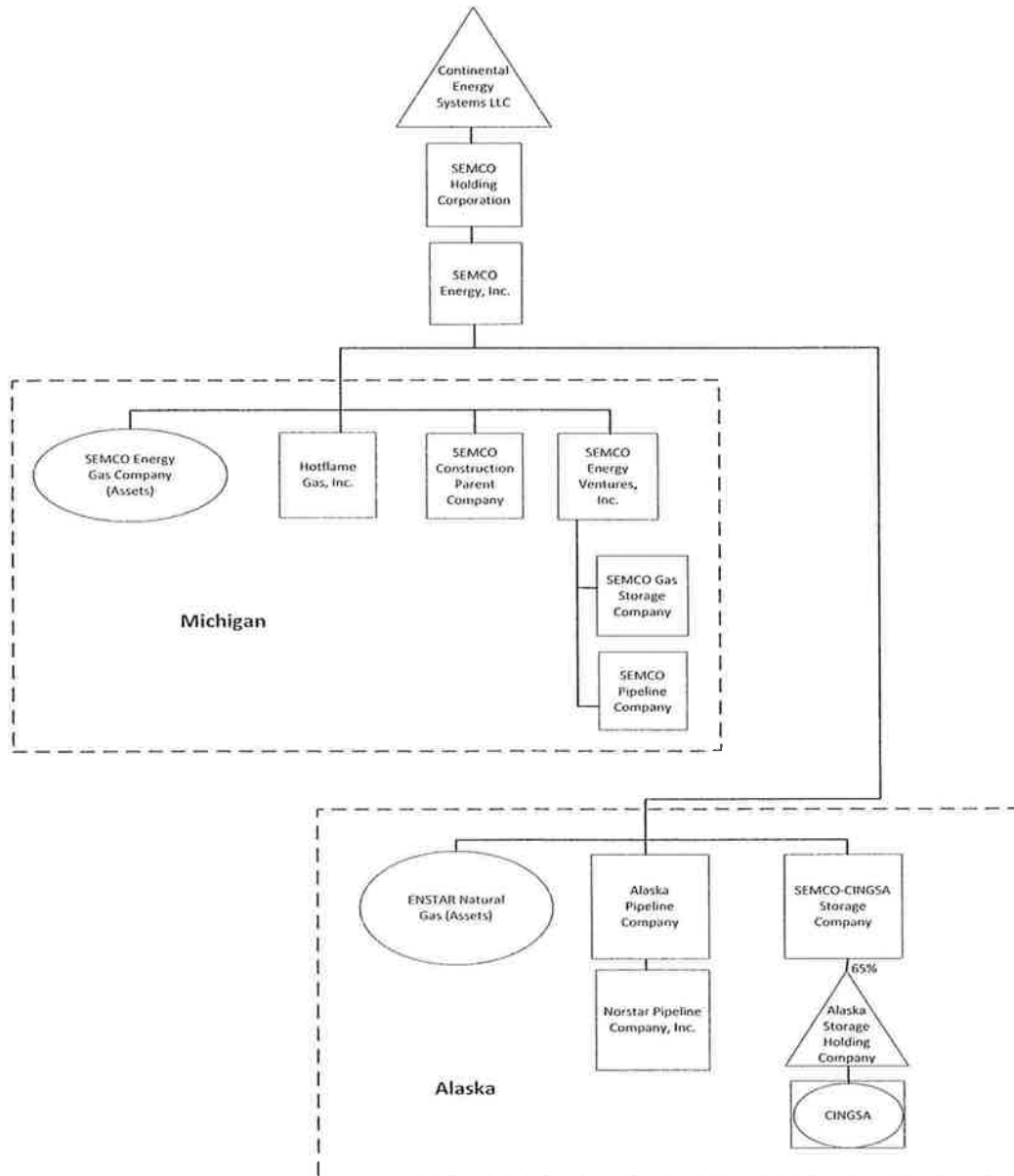
SEMCO also owns five underground gas storage facilities, together with related measuring, compressor and transmission facilities in Michigan and is indirectly involved, through CINGSA, in the construction, ownership and operation of the CINGSA Storage Project in Alaska.

The Gas Distribution Business and the CINGSA Storage Project are subject to regulation. The MPSC has jurisdiction over the regulatory matters related, directly or indirectly, to SEMCO’s provision of service to its Michigan customers. The RCA has jurisdiction over the regulatory matters related, directly or indirectly, to SEMCO’s provision of service to its Alaska customers, including the CINGSA Storage Project. These regulatory agencies have jurisdiction over, among other things, rates, accounting procedures and standards of service.

Gas sales revenue is generated by SEMCO primarily through the delivery and sale of natural gas to residential and commercial customers. These customers use natural gas mainly for space heating. Consequently, weather has a significant impact on SEMCO’s gas sales revenue. As a result of the impact of weather on the Gas Distribution Business and the way in which revenues are currently collected from customers (based, in part, on volumetric distribution rates), most of SEMCO’s gas sales revenue is generated in the first and fourth quarters of the calendar year. Gas sales revenue accounted for 93% of consolidated operating revenues in 2010 and 94% in 2009 and 2008. See “*Risk Factors – SEMCO’s earnings and cash flow are sensitive to decreases in customer consumption resulting from warmer than normal temperatures and customer conservation*”.

The Gas Distribution Business also provides transportation service to large-volume commercial and industrial customers in Michigan and Alaska. Customers using this service purchase gas directly from third-party suppliers. The natural gas purchased by customers from third-party suppliers is then transported on SEMCO’s gas transmission and distribution system to the customers. Unlike charges for gas sales service, the amount SEMCO charges its transportation service customers does not include the cost of gas, because these customers are not purchasing natural gas from SEMCO.

The following chart describes the inter-corporate relationships within the structure of SEMCO:



SEMCO Energy (Alaska)

SEMCO Energy's natural gas distribution business in Alaska, ENSTAR, distributes natural gas to approximately 132,000 customers in the metropolitan Anchorage area and surrounding Cook Inlet area, approximately 91% of which are residential. The remaining gas sales customers include hospitals, universities and government buildings. ENSTAR also provides gas transportation service to power plants, a liquefied natural gas plant, a refinery and a military base. ENSTAR's natural gas delivery system (including Alaska Pipeline Company's natural gas transmission system) includes approximately

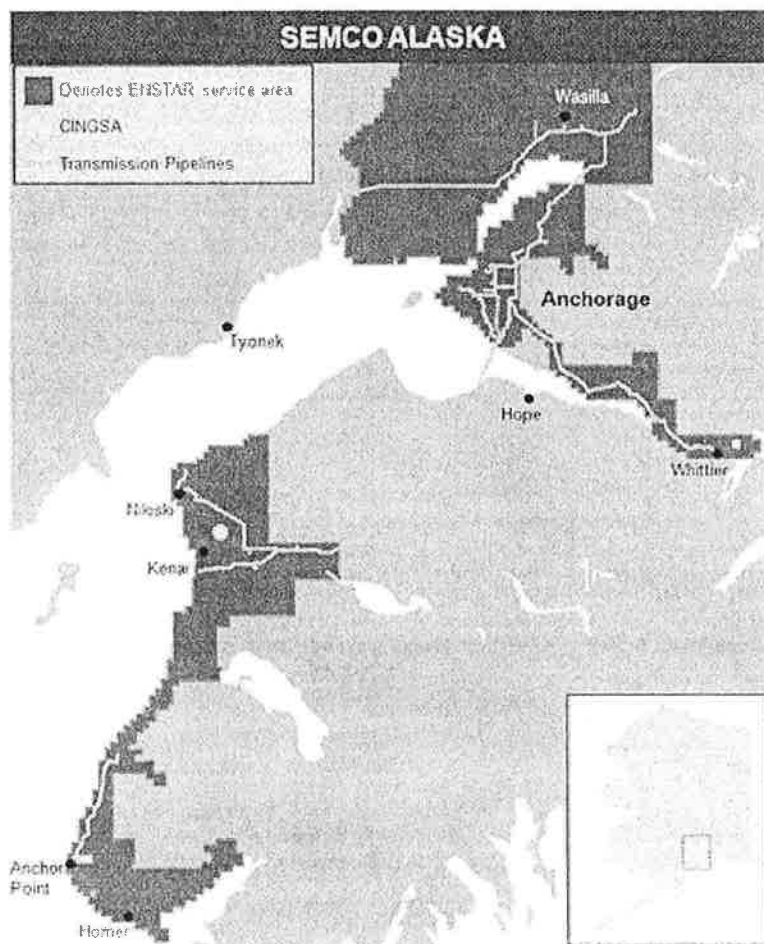
414 miles of gas transmission pipelines and 2,800 miles of gas distribution mains. ENSTAR's pipelines and mains are located in Anchorage and the Cook Inlet area of Alaska.

ENSTAR currently has access to natural gas supplies located in close proximity to its service territory. ENSTAR's distribution system, including the APC transmission-level pipeline system, is not linked to major interstate and intrastate pipelines and thus to natural gas supplies elsewhere in Alaska, Canada, or the lower 48 states. As a result, ENSTAR generally procures natural gas supplies under RCA-approved gas supply agreements from producers in and near the Cook Inlet area of Alaska.

In July 2010, SEMCO Energy, through a subsidiary, entered into a joint venture agreement to invest in CINGSA. CINGSA was formed to construct, own and operate an in-field storage facility in the Cook Inlet area of Alaska otherwise known as the CINGSA Storage Project. The joint venture interest holders of CINGSA are the subsidiary of SEMCO Energy (65%), MidAmerican Energy Holdings Company (26.5%) and Cook Inlet Region Inc. and certain other Alaska native corporations (8.5%). The CINGSA Storage Project is currently under construction and AltaGas anticipates it will have, upon completion, an initial working capacity of 11 Bcf of natural gas with potential future expansion to 18 Bcf and the ability to inject and withdraw natural gas at a rate of 150 Mmcfd. Natural gas would be injected into the storage facility during each summer and withdrawn as needed for use each winter.

Four utilities, including ENSTAR Energy (78%), Chugach Electric Association (16%), Anchorage Municipal Light & Power (5%) and Alaska Electric and Energy Cooperative (1%), have entered into 20 year contracts for 100% of the initial storage capacity of CINGSA.

AltaGas estimates total project costs to operational status for CINGSA to be US\$150 million (approximately US\$100 million of which will be to SEMCO Energy's account), although a US\$180 million cost of the storage facility was previously approved by the RCA. The final cost to build the facility will be reconciled with the RCA 45 days prior to commercial operation date. Initial natural gas injections are anticipated by AltaGas to begin in April 2012, with withdrawal capabilities expected by AltaGas to be available to customers by November 2012. SEMCO Energy is currently constructing and will operate the facility when in service.



SEMCO Energy (Michigan)

In Michigan, SEMCO Energy distributes natural gas to approximately 286,000 customers located in both Southern Michigan and Michigan's Upper Peninsula, approximately 91% of which are residential. The remaining customers include power plants, food production facilities, furniture manufacturers and other industrial customers. SEMCO Energy's natural gas transmission and delivery system in Michigan includes approximately 150 miles of gas transmission pipelines and 5,866 miles of gas distribution mains. The pipelines and mains are located throughout the southern half of Michigan's Lower Peninsula (including in and around the cities of Albion, Battle Creek, Holland, Niles, Port Huron and Three Rivers) and also in the central, eastern and western areas of Michigan's Upper Peninsula.

SEMCO has access to natural gas supplies throughout the United States and Canada via interstate and intrastate pipelines in and near Michigan. SEMCO has pipeline capacity contracts with ANR Pipeline Company, Great Lakes Gas Transmission Limited Partnership, Northern Natural Gas Company, Panhandle Eastern Pipe Line Company, Michigan Consolidated Gas Company, Consumers Energy Company and SEMCO Pipeline Company and SEMCO also owns or leases capacity at various underground storage facilities in Michigan.

To provide gas to SEMCO customers in Michigan, SEMCO has negotiated standard terms and conditions for the purchase of natural gas under the North American Energy Standards Board form of agreement with a variety of suppliers.

The distribution mains of SEMCO Energy's gas distribution business are, generally, located on or under public streets, alleys, highways and other public places, or on private property not owned by SEMCO Energy with permission or consent, except to an inconsequential extent, of the individual property owners. The distribution mains located on or under public streets, alleys, highways and other public places were installed under valid rights and consents granted by appropriate local authorities.

The gas distribution business also owns meters and service lines, gas regulating and metering stations, garages, warehouses and other buildings necessary and useful in conducting its business. In addition, the gas distribution business leases a significant portion of its transportation equipment and certain buildings.

SEMCO Energy's regulated gas distribution business owns five underground gas storage facilities, together with related measuring, compressor and transmission facilities, the two largest of which are the Morton Storage Field (2.0 Bcf) and the Collin Storage Field (1.7 Bcf). The storage facilities are all located in Michigan. The aggregate working capacity of the storage system is approximately 4.9 Bcf.

In addition, SEMCO Energy owns other unregulated businesses, organized as subsidiaries that generally complement the gas distribution business. SEMCO Energy owns a propane distribution business known as "Hotflame". Hotflame typically supplies approximately three million gallons of propane annually to approximately 6,000 retail customers in Michigan's Upper Peninsula and northeast Wisconsin. All non-regulated businesses contribute less than 2% of revenues of SEMCO Energy on an annual basis.

SEMCO Energy's other pipelines and storage business consists of three pipelines and a gas storage facility, all of which are located in Michigan. The three pipelines are:

- the Greenwood Pipeline, a 17-mile pipeline that connects an interstate pipeline with the DTE Energy Greenwood Power Plant located near Port Huron, Michigan. The pipeline provides transportation services to the Greenwood Power Plant and also supplies customers of the gas distribution business in the service area north of Port Huron, Michigan.
- the Eaton Rapids Pipeline, a 33-mile pipeline that delivers gas from the ERGSS to the gas distribution business' systems in Battle Creek and Albion, Michigan, and to an ethanol plant located near Albion, Michigan; and
- a 33% interest in the Litchfield Lateral, a 31-mile pipeline located in southwest Michigan. This pipeline, which is leased entirely to ANR Pipeline Company, links the ERGSS with interstate pipeline supplies.

In addition, SEMCO Energy owns, through a subsidiary, a 50% equity interest in the ERGSS. This natural gas storage system, located near Eaton Rapids, Michigan, became operational in March 1990 and consists of approximately 12.8 Bcf of underground storage capacity. The gas distribution business leases 6.5 Bcf of the capacity under a long-term contract that expires in 2015. ERGSS contributes approximately US\$3 million in EBITDA on an annual basis.



Benefits of the Acquisition

In AltaGas management's view, the key investment highlights of the Acquisition are as follows:

- Generally, the Acquisition:
 - Fits with AltaGas' vision of being one of North America's leading energy infrastructure companies, and aligns with AltaGas' strategy of growing by adding stable, regulated, long-life assets;
 - Is consistent with AltaGas' strategy to grow in the northern United States and establishes a significant foothold in areas with growth potential and in proximity to assets and operations AltaGas owns today;

- Significantly increases natural gas distribution rate base by approximately US\$725 million and allows AltaGas to continue to add customers as natural gas continues to be more competitively priced compared to other fuels used for space heating;
- Is expected to be accretive to earnings and cash flow per share by more than 10% and is expected to add approximately US\$130 million in incremental EBITDA in 2013, the first full year of ownership;
- Is expected to result in AltaGas' utility business, on a *pro forma* basis, being approximately 40% of consolidated EBITDA until 2014 when the 195 MW Forrest Kerr run-of-river power project in British Columbia is scheduled to come into commercial operation. At that time, based on AltaGas' current plans, the Power, Utility and Gas businesses are expected to be more equally weighted;
- Is expected to result in approximately two-thirds of annualized EBITDA in 2013 coming from AltaGas' regulated or long-term contracted assets;
- Will provide stable regulated cash flows to further support both AltaGas' dividend and capital growth projects in the United States and Canada;
- Approximately 99% of SEMCO's revenues are derived from regulated natural gas distribution and storage utilities;
- Will result in no direct natural gas cost exposure due to pass-through mechanisms at both SEMCO natural gas distribution utilities;
- Will strengthen AltaGas' business profile with a significant increase in expected cash flow stability; and
- Will result in a continued conservative payout as a percentage of funds from operations. AltaGas will continue to monitor its dividend payout ratio as a percentage of funds from operations and net income. Dividend growth is expected to be modest until 2014 when the 195 MW Forrest Kerr run-of-river power project in British Columbia is scheduled to come into commercial operation. AltaGas expects to continue to deliver strong returns to shareholders in the form of dividend growth and potential capital appreciation.

SEMCO – Summary Information

- Alaska
 - ENSTAR has an approved regulated rate of return on equity of 12.55% on prescribed equity of 51.40% on a rate base of approximately US\$200 million;
 - ENSTAR serves 132,000 primarily residential customers and is the largest natural gas distributor in Alaska through approximately 414 miles of natural gas transmission pipelines and 2,800 miles of natural gas distribution mains in the Anchorage and Cook Inlet area;

- ENSTAR has experienced 2.5% compounded annual growth over the past 10 years in customer and net plant growth and is expected to continue to grow as Alaska continues to benefit from the significant activity in the natural resource sector;
 - The addition of natural gas storage capacity through CINGSA is expected to allow ENSTAR to cost effectively meet the needs of its customers during peak usage in the winter months;
 - CINGSA has an approved regulated rate of return on equity of 12.55% on prescribed equity of 50% upon completion of construction in 2012. SEMCO's share of rate base is approximately US\$100 million;
 - Potential to expand the CINGSA Storage Project from currently contemplated 11 Bcf of working natural gas capacity to estimated reservoir potential of 18 Bcf of working natural gas capacity; and
 - Growth projects are available in Alaska, including various system enhancements and expansions.
- Michigan
 - The Michigan natural gas distribution utility has an approved regulated rate of return on equity of 10.35% on prescribed equity of 50% on a rate base of approximately US\$425 million;
 - SEMCO's largely residential 286,000 customer base has remained stable through the recent economic downturn and is anticipated to have stable customer growth of approximately 1% to 2% over the long term as the Michigan economy, and in particular the local economies in SEMCO's service areas, improve;
 - SEMCO's Michigan utility has experienced consistent net plant growth of approximately 2% compounded annually over the last 10 years and rate base is anticipated to continue to grow at a similar rate in the near term;
 - Customer conversions from alternative fuel sources to natural gas have increased in the recent past and are expected to continue in light of low natural gas prices relative to the cost of alternative fuel sources; and
 - There is potential for new customer growth driven by industrial and commercial activities in Michigan.

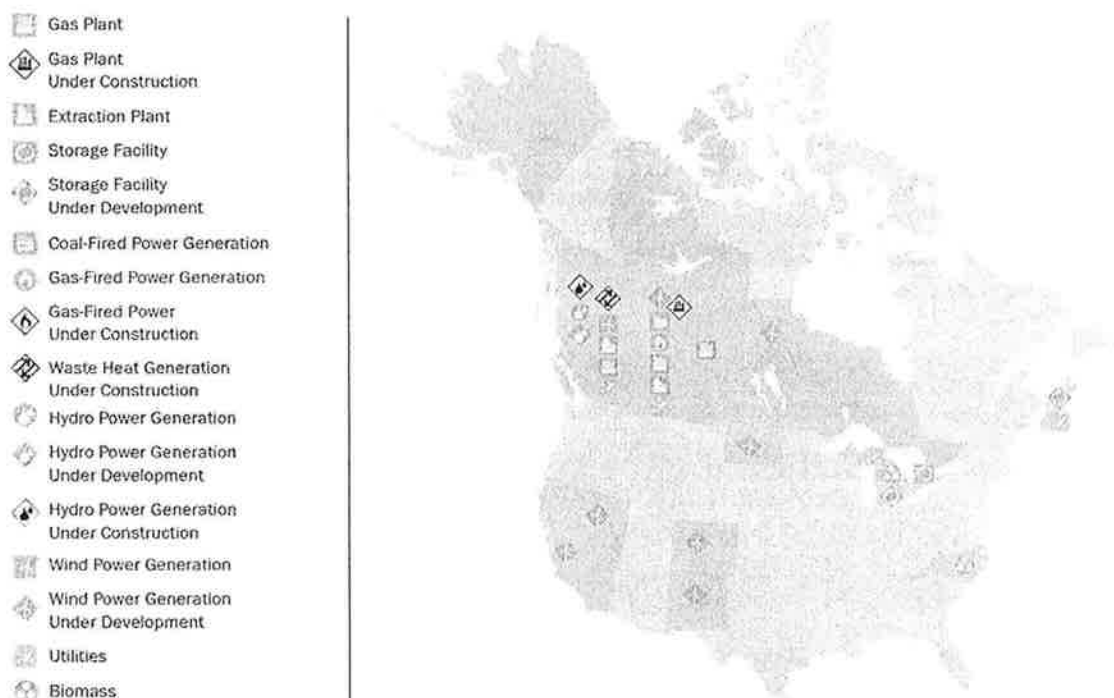
AltaGas Following Completion of the Acquisition

The following map depicts AltaGas' geographic footprint after including the addition of the Michigan and Alaska assets to be acquired through, and assumes the completion of, the Acquisition. The Gas business will include interests in six natural gas liquids extraction facilities with 1.6 Bcf/d of inlet capacity and 86,000 Bbls/d of NGL production capacity. AltaGas also owns eight transmission pipelines with 554 Mmcf/d of natural gas and 152,000 Bbls/d of NGL transportation capacity. AltaGas also has more than 70 gas processing facilities with 1.2 Bcf/d of gas processing capacity and approximately 6,500 kilometres

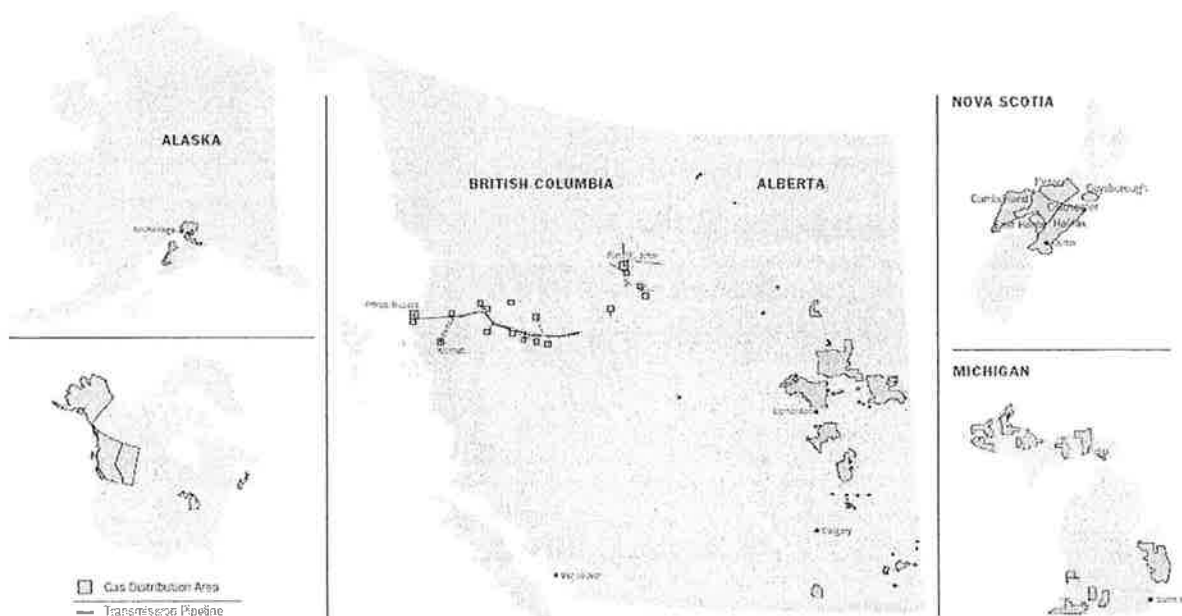
of gathering lines serving producers in the WCSB and a 50% interest in a 5.3 Bcf gas storage asset in Sarnia, Ontario as well as storage under development in Michigan, Nova Scotia and Alberta.

The Power business has over 500 MW of installed power capacity, comprised of 353MW of power generation capacity through a 50% ownership interest in the Sundance B power purchase arrangement, 54 MW of gas fired generation in Alberta, 102 MW of wind power and 12 MW of run-of-river generation. The Power business also has approximately 1,500 MW of wind power generation under development, the 195 MW run-of-river Forrest Kerr project under construction and an additional 200 MW run-of-river under development.

Prior to the Acquisition, the Utility business distributes natural gas to over 110,000 customers in communities in Alberta, British Columbia, Nova Scotia and the Northwest Territories. The Acquisition is expected to add approximately 420,000 customers in Michigan and Alaska.



The North American Utility map below shows AltaGas' utility assets across North America, including the assets in Michigan and Alaska to be acquired through the Acquisition.



Selected Unaudited Pro Forma Consolidated Financial Information

The following tables set forth AltaGas' selected *pro forma* consolidated financial information (i) for the year ended December 31, 2010 and (ii) as at and for the nine month period ended September 30, 2011, in each case after giving effect to the Acquisition and the related financing assumptions as described in the *pro forma* consolidated financial statements which are included in this prospectus.

The selected *pro forma* consolidated financial information for the year ended December 31, 2010 has been derived from and should be read in conjunction with (a) AltaGas' audited consolidated financial statements as at and for the year ended December 31, 2010 which are incorporated by reference in this prospectus, (b) the audited financial statements of SEMCO as at and for the year ended December 31, 2010 prepared in accordance with U.S. GAAP with a reconciliation to Part V and which are included in this prospectus, and (c) AltaGas' unaudited *pro forma* consolidated financial statements for the year ended December 31, 2010 giving effect to the Acquisition and the related financing assumptions as described in the *pro forma* consolidated financial statements which are included in this prospectus.

The *pro forma* consolidated financial information set forth below and the unaudited *pro forma* consolidated financial statements of AltaGas included in this prospectus are not necessarily indicative of results of operations that would have occurred in the year ended December 31, 2010 or the nine months ended September 30, 2011 had the Acquisition been effective January 1, 2010, or of the results of operations expected in 2011 and future years.

(\$000s)

	Year ended December 31, 2010		
	AltaGas	SEMCO ⁽¹⁾	Pro Forma Consolidated
Operating Revenue	1,352,427	597,439	1,949,866
Operating expenses	1,202,154	536,942	1,739,096
Net Income Applicable to Common Shares ⁽²⁾	97,224	21,770	112,033

Notes:

- (1) SEMCO results have been adjusted to Part V as per the reconciliation in SEMCO's audited annual financial statements as at and for the year ended December 31, 2010 and also converted to Canadian dollars at an average exchange rate of \$1.0299.
- (2) Pro Forma Consolidated Net Income Applicable to Common Shares includes pro forma adjustments reflected in Notes 3.j, 3.k and 3.l to the *pro forma* consolidated financial statements for the year ended December 31, 2010 which are included in this prospectus.

The selected *pro forma* consolidated financial information for the nine month period ended September 30, 2011 has been derived from and should be read in conjunction with (i) AltaGas' unaudited consolidated financial statements as at and for the nine month period ended September 30, 2011 prepared in accordance with Part V which are incorporated by reference in this prospectus, (ii) the unaudited financial statements of SEMCO as at and for the nine month period ended September 30, 2011 prepared in accordance with U.S. GAAP with a reconciliation to Part V and which are included in this prospectus, and (iii) AltaGas' unaudited *pro forma* consolidated financial statements as at and for the nine month period ended September 30, 2011 giving effect to the Acquisition and the related financing assumptions as described in the *pro forma* consolidated financial statements which are included in this prospectus.

(\$000s)

	Nine months ended September 30, 2011		
	AltaGas	SEMCO ⁽¹⁾	Pro Forma Consolidated
Operating Revenue	1,164,673	417,530	1,582,203
Operating expenses	1,030,504	370,380	1,400,884
Net Income Applicable to Common Shares ⁽²⁾	53,699	16,554	65,940

Notes:

- (1) SEMCO results have been adjusted to Part V as per the reconciliation in SEMCO's unaudited interim financial statements as at and for the nine months ended September 30, 2011 and also converted to Canadian dollars at an average exchange rate of \$0.9783.
- (2) Pro Forma Consolidated Net Income Applicable to Common Shares includes pro forma adjustments reflected in Notes 3.m, 3.n and 3.o to the *pro forma* consolidated financial statements as at and for the nine month period ended September 30, 2011 which are included in this prospectus.

The Acquisition Agreement

On February 1, 2012, AltaGas and Acquireco entered into the Stock Purchase Agreement with Continental and SEMCO pursuant to which Acquireco agreed to acquire all of the issued and outstanding SEMCO Shares for aggregate consideration of US\$1,135,000,000, subject to adjustment, including approximately US\$355,000,000 in assumed debt.

Representations and Warranties

Under the Stock Purchase Agreement, each of AltaGas, Acquireco, Continental and SEMCO have made various customary representations and warranties.

Continental's representations and warranties relate to, among other things, organization, standing and power, authority to enter into the Stock Purchase Agreement, execution, delivery and enforceability thereof, no conflict, consents and approvals, the SEMCO Shares, the involvement of brokers and the absence of litigation or regulatory proceedings.

Continental's and SEMCO's representations and warranties relate to, among other things, organization, standing and power, authority to enter into the Stock Purchase Agreement, execution, delivery and enforceability thereof, no conflict, consents and approvals, the subsidiaries of SEMCO and the capital structure of SEMCO and such subsidiaries, and the absence of any options or similar rights in relation to the capital thereof, the SEMCO financial statements, the absence of any material adverse effect subsequent to the most recent balance sheet, its real and personal property, taxes, employee benefits, the absence of litigation or regulatory proceedings, compliance with applicable law, environmental matters, governmental authorizations, identifying material contracts and the lack of defaults thereunder, title to property and assets, intellectual property rights, insurance, the involvement of brokers, SEMCO's regulation as a utility, its bank accounts and transactions with affiliates.

AltaGas and Acquireco's representations and warranties relate to, among other things, organization, standing and power, authority to enter into the Stock Purchase Agreement, execution, delivery and enforceability thereof, no conflict, consents and approvals, the involvement of brokers, the absence of litigation or regulatory proceedings, its capital resources and the relationship between AltaGas and Acquireco and the absence of prior business activities by Acquireco.

Covenants

The Stock Purchase Agreement contains customary negative and affirmative covenants on the part of the parties to the Stock Purchase Agreement, including, without limitation, that SEMCO and any subsidiary thereof will conduct their respective businesses in the ordinary course and in substantially the same manner as previously conducted, provide reasonable access and information in relation to SEMCO's business, and use reasonable best efforts to do or cause to be done all things necessary, proper or advisable to consummate the Acquisition, including without limitation to obtain all material authorizations and to make all necessary filings with the relevant government authorities as required under the Stock Purchase Agreement.

The Stock Purchase Agreement also contains specific restrictive covenants as to certain impermissible activities of SEMCO prior to the completion of the Acquisition, which provide that, subject to certain exceptions, including as required or permitted by the Stock Purchase Agreement, SEMCO will not take certain actions without AltaGas' prior written consent (which consent will not be unreasonably withheld, delayed or conditioned), including: amendments to SEMCO's certificate of incorporation, bylaws or other organizational documents; amendments to terms of its securities or capital stock; issuances, sales, recapitalizations or splits of its securities; repurchases or redemptions of securities; acquisitions or dispositions; making of loans; incurrence of indebtedness; actions related to entry into or amendment or termination of material contracts; increases in compensation or amendments to benefit plans; changes to accounting policies; authorizations of capital expenditures; adoption of any plan of liquidation; or institute or settle material litigation.

Closing of the Acquisition is subject to satisfaction or waiver of various conditions prior to the Outside Date, including termination or expiry of any waiting period under the HSR Act and receipt of the Required Regulatory Approvals. See "*Closing Conditions*" below.

Pursuant to the Stock Purchase Agreement each party shall use its reasonable best efforts to take, or cause to be taken, all actions, and to do, or cause to be done, and to assist and cooperate with the other parties in doing, all things necessary, proper or advisable to consummate and make effective, in the most expeditious manner practicable, the Acquisition, including: (i) causing the waiting period under the HSR Act to terminate or expire at the earliest possible date; and (ii) obtaining in the most expeditious manner practicable all other necessary actions or nonactions, consents, governmental authorizations and orders (including with respect to the Required Regulatory Approvals) from governmental entities in connection with the Acquisition.

Pursuant to the Stock Purchase Agreement, each of AltaGas and Acquireco agrees to take, or cause to be taken, any and all steps and to make, or cause to be made, any and all undertakings necessary to avoid or eliminate each and every impediment asserted by any governmental entity in connection with obtaining the Required Regulatory Approvals applicable to AltaGas, Acquireco, SEMCO or any of its subsidiaries so as to enable the closing of the Acquisition to occur as promptly as practicable and, including (i) agreeing to conditions imposed by any governmental entity and proposing, negotiating, committing to and effecting, by consent decree, hold separate order or otherwise, the sale, divestiture, licensing or disposition of assets or businesses of AltaGas, Acquireco or SEMCO or any of their respective subsidiaries or (ii) accepting any operational restrictions, including restrictions on the ability to change rates or charges or standards of service, or otherwise taking or committing to take actions that limit any of AltaGas', Acquireco's or their respective subsidiaries' freedom of action with respect to, or its ability to retain or freely operate, any of the assets, properties, licenses, rights, product lines, operations or businesses of AltaGas, Acquireco, SEMCO or any of their respective subsidiaries, in each case as may be required in order to obtain the Required Regulatory Approvals or to avoid the entry of, or to effect the lifting or dissolution of, any injunction, temporary restraining order or other order in any suit or proceeding, which would otherwise have the effect of preventing or delaying the closing of the Acquisition. Notwithstanding the foregoing, AltaGas and Acquireco shall not be required to, and Continental and SEMCO shall not, in connection with obtaining any consents or approvals hereunder, or in connection with otherwise complying with any provisions of the Stock Purchase Agreement, consent to or take any action of the types described above, including agreeing to conditions, proposing or making any divestiture or other undertaking or proposing, accepting or entering into any consent decree, hold separate order or operational restriction, in each case, that (i) individually or in the aggregate, would reasonably be expected to have a material adverse effect on SEMCO and its subsidiaries, taken as a whole, (ii) individually or in the aggregate, would reasonably be expected to have a material adverse effect on AltaGas and its subsidiaries, taken as a whole but determined without giving effect to the Acquisition, or (iii) individually or in the aggregate, would reasonably be expected to have a material adverse effect on AltaGas and its subsidiaries, taken as a whole and determined after giving effect to the Acquisition, taken as a whole. See "*Risk Factors – Satisfaction of Conditions Precedent*".

Indemnification

Pursuant to the Stock Purchase Agreement, Continental has agreed to indemnify Acquireco and its affiliates and their respective officers, directors, employees, stockholders, agents and representatives (the "**Acquireco Indemnified Parties**") against and hold them harmless from, among other things, all taxes of SEMCO and its subsidiaries for any period prior to the Transaction Closing Date and any liabilities in relation thereto. Acquireco, SEMCO and its subsidiaries have similarly agreed to indemnify Continental and its affiliates and their respective officers, directors, employees, stockholders, agents and representatives (the "**Continental Indemnified Parties**") against and hold them harmless from, among other things, all taxes of SEMCO and its subsidiaries for any period subsequent to the Transaction Closing Date and any liabilities in relation thereto.

In addition, Continental has agreed to indemnify the Acquireco Indemnified Parties from any losses arising out of any misrepresentation in or breach of any representation or warranty by Continental or SEMCO or any breach of nonfulfillment of any covenant, agreement or other obligation of Continental or SEMCO in the Stock Purchase Agreement. Acquireco and AltaGas have similarly agreed to indemnify the Continental Indemnified Parties from any losses arising out of any misrepresentation in or breach of any representation or warranty by Acquireco or AltaGas or any breach of nonfulfillment of any covenant, agreement or other obligation of Acquireco or AltaGas in the Stock Purchase Agreement or any discontinuance, suspension or modification of a benefit plan or agreement after the Transaction Closing Date.

Neither the Acquireco Indemnified Parties nor the Continental Indemnified Parties can assert any claim for indemnification except to the extent that any such claim is in an amount in excess of US\$10,000 and unless and until the aggregate amount of such claims by the Acquireco Indemnified Parties or the Continental Indemnified Parties, as applicable, under the Stock Purchase Agreement exceeds US\$10,000,000. If the US\$10,000,000 basket is exceeded, then the Acquireco Indemnified Parties or the Continental Indemnified Parties, as applicable, may assert claims for the entire amount of such aggregate claims without regard to that basket; provided that in no event will the aggregate liability of AltaGas or Continental for claims of losses exceed US\$114,000,000, subject to certain exceptions.

Closing Conditions

The Stock Purchase Agreement provides that the obligations of each of the parties to complete the Acquisition are subject to the fulfillment of a number of mutual conditions, each of which may be waived by such party, including the following:

- Antitrust Approval. Any waiting period (and any extension thereof) under the HSR Act shall have been terminated or shall have expired;
- No Injunctions or Restraints. No order, decree or ruling issued by any governmental entity of competent jurisdiction or other law preventing the consummation of the Acquisition will be in effect; provided, that each party shall have used its reasonable best efforts to prevent the entry of any such injunction or other order and to appeal as promptly as possible any such injunction or other order that may be entered before asserting the condition;
- Regulatory Approvals. Orders granting the Required Regulatory Approvals shall have been obtained and no conditions or requirements shall be contained in any such order imposing on AltaGas, Acquireco or Continental any condition or requirement that any of AltaGas, Acquireco or Continental, as applicable, is not required to accept pursuant to the Stock Purchase Agreement; and
- Repayment of Indebtedness. The parties will have received payoff documentation from the holders of indebtedness under the CES Credit Agreement and the SEMCO Credit Agreement providing that upon repayment by Acquireco of indebtedness of SEMCO and certain of its subsidiaries thereunder, all liens securing such indebtedness shall be terminated and released to the extent such liens do not also secure indebtedness under the indenture governing the Senior Notes, the 1998 Indenture or the CINGSA Credit Agreement with respect to such indebtedness and SEMCO and certain of its subsidiaries shall be released from their obligations with respect to such indebtedness; and the parties shall have received documentation that

SEMCO has been released from its obligations in respect of a certain credit agreement swap entered into by Continental and SEMCO and any collateral and credit support provided by SEMCO or any subsidiary in connection therewith has been cancelled or returned to SEMCO.

The Stock Purchase Agreement provides that the obligations of AltaGas and Acquireco to complete the Acquisition are subject to the fulfillment of a number of conditions including, but not limited to:

- Representations and Warranties. The accuracy of Continental's and SEMCO's representations and warranties;
- Covenants. The performance by Continental and SEMCO of their respective obligations under the Stock Purchase Agreement; and
- Material Adverse Effect. No material adverse effect in respect of SEMCO prior to the Transaction Closing Date.

The Stock Purchase Agreement provides that the obligations of Continental to complete the Acquisition are subject to the fulfillment of a number of conditions including, but not limited to:

- Representations and Warranties. The accuracy of AltaGas' and Acquireco's representations and warranties; and
- Covenants. The performance by AltaGas and Acquireco of their respective obligations under the Stock Purchase Agreement.

Termination

The Stock Purchase Agreement may be terminated at any time prior to the Transaction Closing Date:

- by mutual written consent;
- if the Transaction Closing Date has not occurred by the Outside Date;
- if any governmental entity has issued an order, decree or ruling or taken any other action enjoining, restraining or otherwise prohibiting the Acquisition, and such order, decree or ruling has become final;
- if any condition to the obligation of such party to consummate the Acquisition becomes incapable of satisfaction prior to the Outside Date, subject to certain conditions;
- if a regulatory entity issues an order that shall have become final or non-appealable and imposes on AltaGas, Acquireco or Continental any condition or requirement that any of AltaGas, Acquireco or Continental, as applicable, is not required to accept pursuant to the Stock Purchase Agreement; or
- if a party has breached or failed to perform any of its representations, warranties, covenants or agreements contained in the Stock Purchase Agreement and any such breach shall not have been cured, subject to certain conditions.

Financing the Acquisition

For purposes of financing the Acquisition, AltaGas obtained a commitment on February 1, 2012 from TD, BMO and RBC for the New Credit Facility.

AltaGas expects that cash to close the Acquisition of approximately US\$780 million will be provided from a combination of equity and debt; specifically: (i) the net proceeds from the Offering; (ii) the New Credit Facility; (iii) the Credit Facilities; and (iv) future debt and Preferred Share financings.

The New Credit Facility will rank *pari passu* with AltaGas' senior unsecured obligations, including the existing Credit Facilities, and will have a one year term from the date on which the credit agreement for the New Credit Facility is executed. Subject to the satisfaction of certain conditions precedent customary for a financing of this type, funds will be available to be drawn under the New Credit Facility.

AltaGas will have the option to borrow under the New Credit Facility using a Canadian prime rate, a bankers' acceptance rate, U.S. base rate or LIBOR rate. The margins above the applicable rate will be based on AltaGas' then applicable ratings from S&P and DBRS. Customary fees will be payable by AltaGas in respect of the New Credit Facility.

Prepayments will be permitted at AltaGas' option at any time without premium or penalty.

The New Credit Facility will be in substantially the same form as the Syndicated Facility, as amended concurrent with the execution of the New Credit Facility, and will contain representations and warranties, affirmative and negative covenants (including requirements to meet certain financial ratios on an ongoing basis) and events of default that are customary for bank credit facilities of this nature.

Following completion of the Acquisition, SEMCO and its subsidiaries will continue to have outstanding: (i) US\$300 million of Senior Notes; (ii) US\$5 million secured medium term notes bearing interest at an annual rate of 7.03% and maturing on November 25, 2013; and (iii) an estimated US\$75 million secured loan facility maturing November 2015 related to CINGSA in which SEMCO has a 65% interest.

RECENT DEVELOPMENTS

Acquisition of Pacific Northern Gas Ltd.

On December 20, 2011, AltaGas completed the acquisition of all of the issued and outstanding common shares in the capital of PNG at a price of \$36.75 in cash per PNG common share pursuant to a court-approved statutory plan of arrangement under the provisions of the *Business Corporations Act* (British Columbia).

Pacific Northern Gas Ltd.

PNG owns and operates rate-regulated natural gas transmission and distribution systems in British Columbia.

PNG's western transmission line is comprised of approximately 1,180 kilometres of distribution pipelines and extends from the Spectra Energy gas transmission system north of Prince George to tidewater at Kitimat and Prince Rupert, providing service to 12 communities and a number of industrial facilities. PNG currently has exclusive franchise agreements with the municipalities of Fraser Lake, Prince Rupert, Port Edward, Kitimat, Terrace, Smithers, Burns Lake, Houston and Vanderhoof, entitling it to distribute natural gas within those municipalities. PNG also has operating agreements with the municipalities of Fort St. James and Telkwa that entitle it to install and operate gas distribution facilities in those municipalities.

In the northeast, PNG's subsidiary Pacific Northern Gas (N.E.) Ltd. ("**PNGNE**") provides gas distribution service in the Dawson Creek, Fort St. John and Tumbler Ridge areas through connections with the Spectra Energy pipeline system at several locations. The entire Northeast system consists of approximately 160 kilometres of transmission lines, 1,490 kilometres of distribution lines and a gas processing plant near Tumbler Ridge with a capacity of 120 10³m³ per day. PNGNE has exclusive franchise agreements with the District of Taylor, the Cities of Dawson Creek and Fort St. John and the Village of Pouce Coupe.

PNG also operates and owns a 97% interest in the 9.8 megawatt McNair Creek hydro-electricity generation facility located on B.C.'s Sunshine Coast.

Electricity Purchase Agreements for McLymont Creek and Volcano Creek Hydro-electric Projects

On November 2, 2011, AltaGas signed Electricity Purchase Agreements (the "**EPAs**") with BC Hydro for the McLymont Creek and Volcano Creek run-of-river hydroelectric projects, with a combined capacity of approximately 82 MW.

Together with the Forrest Kerr project, the three projects total approximately 277 MW (the "**Northwest Projects**") and will be the anchor tenants for the Northwest Transmission Line, which will form the backbone of electrical infrastructure in northwest BC.

The terms of these EPAs are similar in all material respects to the EPA signed for the Forrest Kerr project on May 28, 2010. The Northwest Projects are located in close proximity approximately 1,000 km north of Vancouver, BC. AltaGas will take advantage of synergies and shared construction infrastructure between the projects, and is now targeting an in service date in the fall of 2015 for both the McLymont Creek and Volcano Creek projects. AltaGas expects the Forrest Kerr project, currently under construction, to come into service in July 2014.

The Northwest Projects will be constructed solely within Tahltan Nation traditional territory. AltaGas and the Tahltan Nation have signed Impact Benefit Agreements for all three projects and have established a strong working relationship that will provide the people of the Tahltan Nation with employment, business opportunities, and economic participation.

Once completed, the Northwest Projects will provide enough electricity for approximately 95,000 homes in British Columbia and will offset more than 780,000 tonnes of greenhouse gas equivalents annually.

Conversion to U.S. GAAP

The Canadian Institute of Chartered Accountants' Accounting Standards Board ("**AcSB**") confirmed in February 2008 that International Financial Reporting Standards ("**IFRS**") would replace CGAAP for publicly accountable enterprises for financial periods beginning on or after January 1, 2011.

On September 10, 2010, the AcSB amended the introduction to Part I of the CICA Handbook – Accounting to permit, but not to require, qualifying entities with Rate-Regulated Activities ("**RRA**") to adopt IFRS for the first time no later than the interim and annual financial statements relating to interim and annual periods beginning on or after January 1, 2012, thereby providing a one year deferral. The Canadian Securities Administrators provide for a similar one year deferral pursuant to National Instrument 52-107 – *Acceptable Accounting Principles and Auditing Standards* ("**NI 52-107**").

AltaGas is a qualifying entity for the deferral period permitted by AcSB and NI 52-107, based on the activities of AltaGas Utilities Inc., PNG and Heritage Gas Limited.

AltaGas elected to use the deferral offered by the AcSB and NI 52-107, given the uncertainty with respect to the application of IFRS to RRA, and has prepared and will continue to prepare its consolidated financial statements for the remainder of 2011 in accordance with CGAAP. AltaGas also reassessed the accounting policy choices available and determined that the most appropriate decision for AltaGas' business activities is the use of U.S. GAAP effective January 1, 2012.

Pursuant to NI 52-107, U.S. GAAP reporting is generally permitted for companies subject to reporting obligations under United States' securities laws. However, given that AltaGas is not subject to such reporting obligations and could not therefore rely on the provisions of NI 52-107 to that effect, AltaGas sought, and obtained on July 4, 2011, exemptive relief by the securities regulatory authorities in Alberta and Ontario to permit it to prepare its financial statements in accordance with U.S. GAAP. Absent an extension to its term, the exemption will terminate on or after the earlier of January 1, 2015 and the date on which AltaGas ceases to have activities subject to rate regulation, at which time AltaGas will be required to comply with NI 52-107 in respect of the appropriate accounting principles to be applied, which could include the adoption of IFRS.

For the first financial year in which the change from Canadian GAAP – Part V to U.S. GAAP takes place, the notes to AltaGas' annual financial statements will:

- (a) explain the material differences between Canadian GAAP – Part V and U.S. GAAP that relate to recognition, measurement and presentation;
- (b) quantify the effect of those material differences, including a tabular reconciliation between the net income reported in the financial statements and the net income computed in accordance with Canadian GAAP – Part V; and
- (c) provide information consistent with disclosure requirements of Canadian GAAP – Part V to the extent not already reflected in the financial statements.

USE OF PROCEEDS

The net proceeds to AltaGas from the Offering will be approximately \$335,364,000, after deducting the Underwriters' fee of \$14,036,000 and estimated expenses of the Offering of \$1,500,000. If the Underwriters exercise the Over-Allotment Option in full, the net proceeds from the Offering will be approximately \$385,893,600 after deducting the Underwriters' fee of \$16,141,400 and estimated expenses of the Offering of \$1,500,000. The expenses of the Offering will be paid from the general funds of AltaGas.

The net proceeds of the Offering, together with funds to be advanced pursuant to some combination of the Credit Facilities and the New Credit Facility and the proceeds of future debt and Preferred Share financings, as determined by AltaGas, will be used to finance the purchase price of the Acquisition. See "*Acquisition of SEMCO – Financing the Acquisition*". The Escrowed Funds will be held in escrow pending the Escrow Release Condition being satisfied. See "*Details of the Offering*".

DESCRIPTION OF SECURITIES

The authorized capital of AltaGas consists of an unlimited number of Common Shares and such number of Preferred Shares issuable in series at any time as have aggregate voting rights either directly or on conversion or exchange that in the aggregate represent less than 50% of the voting rights attaching to the then issued and outstanding Common Shares.

The following description sets forth certain general terms and provisions of the existing share capital of AltaGas. The summary below is subject to, and qualified by reference to, AltaGas' articles and by-laws.

Common Shares

Holders of Common Shares are entitled to one vote per share at meetings of shareholders of AltaGas, to receive dividends if, as and when declared by the board of directors of AltaGas and to receive the remaining property and assets of AltaGas upon its dissolution or winding-up, subject to the rights of shares having priority over Common Shares.

Preferred Shares

The directors of AltaGas may divide any unissued Preferred Shares into series and fix the number of shares in each series and the designation, rights, privileges, restrictions and conditions thereof. The Preferred Shares of each series will rank on a parity with Preferred Shares of every other series with respect to accumulated dividends and return of capital and entitled to a preference over the Common Shares and over any other shares of AltaGas ranking junior to the Preferred Shares with respect to the priority in the payment of dividends and in the distribution of assets in the event of liquidation, dissolution or winding-up of AltaGas, whether voluntary or involuntary.

The rights, privileges, restrictions and conditions attaching to the Preferred Shares as a class may be repealed, altered, modified, amended or amplified or otherwise varied only with the sanction of the holders of the Preferred Shares given in such manner as may then be required by law, subject to a minimum requirement that such approval be given by resolution in writing executed by all holders of Preferred Shares entitled to vote on that resolution or passed by the affirmative vote of at least 66⅔% of the votes cast at a meeting of holders of Preferred Shares duly called for such purpose.

CAPITALIZATION OF ALTAGAS

The following table sets forth the unaudited consolidated capitalization of AltaGas as at September 30, 2011, and the unaudited *pro forma* consolidated capitalization of AltaGas as at September 30, 2011 after giving effect to: (i) the Offering (assuming the Over-Allotment Option is not exercised); (ii) the completion of the Acquisition and related advances under the Credit Facilities and/or the New Credit Facility; and (iii) the acquisition of PNG. The financial information set out below should be read in conjunction with the unaudited consolidated financial statements of AltaGas as at and for the nine months ended September 30, 2011 incorporated by reference in this prospectus and the unaudited *pro forma* financial statements of AltaGas included in this prospectus and, in each case, the notes thereto.

(\$000s except share amounts)

		Outstanding as at September 30, 2011	Outstanding as at September 30, 2011 after giving effect to the Offering, the acquisition of PNG and completion of the Acquisition and related advances under the Credit facilities ⁽¹⁾
Debt	Authorized		
Credit facilities ⁽²⁾		67,089	456,310
Medium Term Notes ⁽³⁾		975,000	1,075,000
Other Long Term Debt		7,532	7,532
Assumed Debt of PNG ⁽⁴⁾		Nil	85,628
Assumed Debt of SEMCO ⁽⁵⁾		Nil	392,508
Share Capital			
Common Shareholders' Equity ⁽⁶⁾⁽⁷⁾	Unlimited	1,009,749 (83,840,365 Common Shares)	1,474,495 (100,850,865 Common Shares)
Preferred Shares ⁽⁸⁾	Unlimited	194,126 (8,000,000 Preferred Shares, Series A)	199,126 (8,000,000 Preferred Shares, Series A, 200,000 PNG Preferred Shares)
Total Capitalization		2,253,496	3,690,599

Notes:

- (1) Based on the issuance of 12,100,000 Subscription Receipts pursuant to the Offering for net proceeds to AltaGas from the Offering of approximately \$335,364,000, after deducting the Underwriters' Fee of \$14,036,000 and estimated expenses of the Offering of \$1,500,000. If the Underwriters exercise the Over-Allotment Option in full, the net proceeds from the Offering will be approximately \$385,893,600 after deducting the Underwriters' Fee of \$16,141,400 and estimated expenses of the Offering of \$1,500,000. The expenses of the Offering will be paid from the general funds of AltaGas. See "Plan of Distribution".
- (2) Includes the Credit Facilities and the New Credit Facility. See "Relationship Between AltaGas and Certain of the Underwriters" for a description of the Credit Facilities and "Acquisition of SEMCO – Financing the Acquisition" for a description of the New Credit Facility. The pro forma amount has been adjusted to include the incremental drawdown of approximately \$140 million under the Credit Facilities for the acquisition of PNG, the repayment of the \$100 million 5.07% medium term notes that matured on January 19, 2012 and a net drawdown under the Credit facilities of approximately \$488 million for the Acquisition (see note 3(f)(iii) of the unaudited pro forma financial statements), reduced by the proceeds of the \$200 million of 4.55% medium term notes issued in October 2011 and the net proceeds of the 4,910,500 Common Shares issued on November 15, 2011.
- (3) Medium term notes consist of: (a) \$100 million of 5.07% medium term notes due January 19, 2012 (and which have since been repaid subsequent to September 30, 2011); (b) \$200 million of 7.42% medium term notes due April 29, 2014; (c) \$100 million of 6.94% medium term notes due June 29, 2016; (d) \$200 million of 5.49% medium term notes due March 27, 2017; (e) \$175 million of 4.60% medium term notes due January 15, 2018; (f) \$200 million of 4.10% medium term notes due March 24, 2016; and (g) \$200 million of 4.55% medium term notes due January 17, 2019 (and which were issued subsequent to September 30, 2011).
- (4) The Assumed Debt of PNG consists of the bank indebtedness and long term debt including the current portion as disclosed in PNG's unaudited interim consolidated financial statements for the three and nine months ended September 30, 2011.
- (5) Assumed Debt of SEMCO consists of the long term debt as disclosed in SEMCO's unaudited consolidated financial statements as of September 30, 2011 and September 30, 2010 and for the three and nine month periods ended September 30, 2011 and September 30, 2010 translated to the Canadian dollar equivalent at an exchange rate of 1.0482 and adjusted for the transaction as described in Note 3(f)(i) and (ii) to the unaudited pro forma financial statements.
- (6) Includes the issuance of an aggregate of 4,910,500 Common Shares at a price of \$29.30 per Common Share on November 15, 2011 pursuant to a prospectus offering. See "Prior Sales".
- (7) As at September 30, 2011, 4,573,065 options under AltaGas' stock option plan were outstanding with a weighted average exercise price of \$20.62 per Common Share.
- (8) Preferred Shares have been adjusted to include the 200,000 6 ¾% cumulative redeemable preferred shares assumed as part of the acquisition of PNG. On January 23, 2012, PNG announced that it would redeem all of the 6 ¾% cumulative redeemable preferred shares on February 27, 2012.

PRIOR SALES

AltaGas has not sold or issued any Common Shares, or securities convertible into Common Shares, during the twelve month period prior to the date hereof other than as follows:

- (a) an aggregate of 1,390,709 Common Shares pursuant to AltaGas' Dividend Reinvestment and Optional Common Share Purchase Plan at a weighted average issue price of \$25.25 per Common Share, for aggregate consideration of approximately \$35.1 million, in accordance with the following:

<u>Date</u>	<u>Issue Price (\$)</u>	<u>Number of Common Shares</u>
February 15, 2011	21.37	120,122
March 15, 2011	23.81	116,724
April 15, 2011	24.79	121,263
May 16, 2011	23.72	125,686
June 15, 2011	23.48	128,289
July 15, 2011	25.02	132,268
August 15, 2011	23.99	128,437
September 15, 2011	26.01	110,467
October 17, 2011	25.78	109,368
November 15, 2011	28.33	113,254
December 15, 2011	29.70	97,027
January 16, 2012	29.58	87,804

- (b) an aggregate of 1,154,750 options to acquire 1,154,750 Common Shares at an average exercise price of \$29.23 pursuant to AltaGas' share option plan, in accordance with the following:

<u>Date</u>	<u>Exercise Price (\$)</u>	<u>Number of Common Shares</u>
April 25, 2011	25.06	1,500
May 9, 2011	24.67	2,500
May 12, 2011	24.92	75,000
May 16, 2011	25.16	2,500
June 8, 2011	24.45	2,500
August 2, 2011	26.46	35,000
September 13, 2011	27.03	30,000
September 15, 2011	27.33	25,000
October 6, 2011	26.94	45,000
November 25, 2011	29.85	861,250
December 20, 2011	31.12	67,500
December 22, 2011	31.82	7,000

- (c) an aggregate of 397,045 Common Shares at an average exercise price of \$17.92 on the exercise of options granted pursuant AltaGas' share option plan, for aggregate consideration of approximately \$7.1 million, in accordance with the following:

Date	Exercise Price (\$)	Number of Common Shares
February 7, 2011	14.24	2,625
February 7, 2011	18.15	2,500
February 9, 2011	14.24	500
February 16, 2011	14.24	250
March 1, 2011	14.24	3,000
March 4, 2011	14.24	3,500
March 8, 2011	14.24	2,500
March 10, 2011	14.24	3,000
March 15, 2011	14.24	4,875
March 18, 2011	14.24	4,000
March 21, 2011	14.24	500
March 29, 2011	14.24	1,000
March 29, 2011	13.65	1,000
April 5, 2011	14.24	250
April 7, 2011	25.00	3,750
April 11, 2011	14.24	1,000
April 15, 2011	14.24	250
April 15, 2011	18.00	500
April 20, 2011	24.10	2,500
April 20, 2011	14.24	5,000
April 29, 2011	14.24	5,000
May 9, 2011	14.24	13,000
May 9, 2011	15.09	1,250
May 11, 2011	14.24	500
May 17, 2011	14.24	2,000
May 30, 2011	14.24	2,000
June 2, 2011	14.24	1,000
June 6, 2011	17.10	12,500
June 13, 2011	14.24	610
June 14, 2011	14.24	3,750
June 15, 2011	14.24	2,000
June 22, 2011	14.24	4,200
June 29, 2011	14.24	11,500
July 5, 2011	14.24	1,875
July 5, 2011	25.54	2,000
July 7, 2011	25.54	3,000
July 7, 2011	14.24	5,200
July 11, 2011	18.00	500
July 11, 2011	14.24	4,500
July 11, 2011	17.89	2,500
July 11, 2011	18.15	1,250
July 26, 2011	14.24	500
August 3, 2011	14.24	1,100
August 3, 2011	18.15	3,750
August 3, 2011	23.80	100
August 17, 2011	14.24	1,875
August 17, 2011	17.10	1,875

<u>Date</u>	<u>Exercise Price (\$)</u>	<u>Number of Common Shares</u>
September 6, 2011	14.24	12,500
September 6, 2011	23.80	1,000
September 6, 2011	25.54	1,500
September 8, 2011	14.24	1,000
September 8, 2011	17.90	500
September 15, 2011	14.24	4,100
September 15, 2011	23.35	500
September 19, 2011	14.24	2,500
September 21, 2011	23.35	1,000
September 21, 2011	14.24	2,500
September 21, 2011	25.00	3,750
September 21, 2011	17.10	1,875
September 23, 2011	14.24	1,500
September 28, 2011	14.24	5,000
October 4, 2011	14.24	1,000
October 14, 2011	14.24	3,000
October 14, 2011	23.35	1,500
October 20, 2011	14.24	1,000
October 27, 2011	23.35	2,250
October 28, 2011	25.54	1,000
October 28, 2011	25.00	750
November 9, 2011	14.24	1,500
November 9, 2011	25.89	3,000
November 9, 2011	23.35	3,750
November 9, 2011	25.89	1,875
November 10, 2011	16.23	1,000
November 10, 2011	17.10	1,250
November 10, 2011	23.35	1,500
November 10, 2011	25.89	750
November 14, 2011	14.24	12,000
November 14, 2011	25.54	5,000
November 14, 2011	24.56	1,000
November 17, 2011	14.24	710
November 17, 2011	7.25	2,500
November 17, 2011	23.35	1,500
November 18, 2011	23.80	4,000
November 18, 2011	25.54	1,000
November 18, 2011	25.00	375
November 21, 2011	14.24	1,000
November 21, 2011	24.10	1,000
November 21, 2011	23.80	1,500
November 24, 2011	25.54	1,000
November 24, 2011	24.56	6,500
November 24, 2011	25.00	3,000
December 1, 2011	23.80	2,000
December 1, 2011	7.25	1,000
December 1, 2011	25.54	1,500

Date	Exercise Price (S)	Number of Common Shares
December 1, 2011	25.00	3,000
December 6, 2011	25.00	4,750
December 6, 2011	23.35	1,875
December 6, 2011	14.24	3,750
December 6, 2011	17.90	500
December 6, 2011	7.25	1,000
December 6, 2011	23.35	5,000
December 8, 2011	28.86	3,500
December 8, 2011	25.00	1,500
December 8, 2011	14.24	1,000
December 12, 2011	14.24	29,000
December 14, 2011	14.24	6,750
December 14, 2011	25.00	1,000
December 15, 2011	23.35	5,625
December 15, 2011	14.24	3,000
December 16, 2011	24.10	1,000
December 16, 2011	14.24	4,750
December 16, 2011	21.05	2,000
December 16, 2011	25.00	125
December 16, 2011	23.80	150
December 16, 2011	23.35	5,625
December 19, 2011	14.24	4,000
December 19, 2011	21.05	2,375
December 19, 2011	25.54	1,000
December 19, 2011	25.00	1,500
December 19, 2011	23.35	1,875
December 20, 2011	21.05	1,000
December 20, 2011	14.24	5,500
December 20, 2011	23.35	4,500
January 5, 2012	21.05	3,000
January 5, 2012	23.35	5,625
January 5, 2012	14.24	9,050
January 5, 2012	28.86	7,000
January 5, 2012	25.00	2,750
January 5, 2012	25.54	1,000
January 9, 2012	14.24	11,000
January 9, 2012	21.05	250
January 11, 2012	28.86	500
January 11, 2012	25.89	375
January 11, 2012	14.24	1,500
January 11, 2012	21.05	200
January 13, 2012	21.05	250
January 13, 2012	14.24	500
January 16, 2012	14.24	1,875
January 17, 2012	14.24	500
January 20, 2012	21.05	750
January 20, 2012	24.10	1,000

<u>Date</u>	<u>Exercise Price</u> <u>(\$)</u>	<u>Number of Common Shares</u>
January 26, 2012	25.00	1,000

- (d) an aggregate of 4,910,500 Common Shares at a price of \$29.30 per Common Share on November 15, 2011 pursuant to a prospectus offering.

PRICE RANGE AND TRADING VOLUME

Common Shares

The Common Shares are listed and posted for trading on the TSX under the trading symbol "ALA". The following table sets forth the price range for and trading volume of the Common Shares on the TSX for the period from January 2011 through February 13, 2012, as reported by the TSX.

	<u>Price Range</u>		<u>Volume</u>
	<u>High (\$)</u>	<u>Low (\$)</u>	
2011			
January	22.69	21.16	4,230,807
February	24.96	21.89	5,213,437
March	25.95	23.35	4,091,524
April	26.66	24.70	2,909,768
May	25.56	24.41	2,091,347
June	26.07	24.05	4,607,888
July	27.10	25.65	3,287,392
August	27.62	21.25	5,322,737
September	28.67	26.26	5,600,749
October	30.13	25.69	3,730,326
November	31.29	29.04	5,144,131
December	32.67	30.22	5,148,006
2012			
January	32.37	28.23	5,237,701
February (1-13)	30.40	29.50	2,383,461

On February 13, 2012, the closing price of the Common Shares on the TSX was \$29.79.

Preferred Shares, Series A

The Preferred Shares, Series A are listed and posted for trading on the TSX under the trading symbol "ALA.PR.A". The following table sets forth the price range for and trading volume of the Preferred Shares, Series A on the TSX for the period from January 2011 through February 13, 2012, as reported by the TSX.

	<u>Price Range</u>		<u>Volume</u>
	<u>High (\$)</u>	<u>Low (\$)</u>	
2011			
January	26.04	25.55	246,053
February	25.94	25.46	244,895
March	25.89	25.24	142,729

	Price Range		Volume
	High (\$)	Low (\$)	
April	25.83	25.45	127,363
May	25.90	25.50	109,145
June	25.93	25.30	121,514
July	25.91	25.49	112,591
August	25.94	25.35	159,582
September	25.90	25.47	128,584
October	25.83	24.99	149,834
November	26.12	25.63	82,501
December	26.15	25.50	72,726
2012			
January	26.65	25.76	178,635
February (1-13)	26.29	26.00	69,443

On February 13, 2012, the closing price of the Preferred Shares, Series A on the TSX was \$26.18.

DETAILS OF THE OFFERING

The following is a summary of the material attributes and characteristics of the Subscription Receipts. This summary does not purport to be complete and is subject to, and qualified in its entirety by reference to the terms of the Subscription Receipt Agreement.

The Subscription Receipts will be issued on the Closing Date pursuant to the Subscription Receipt Agreement. The Escrowed Funds will be delivered to and held by the Subscription Receipt Agent and invested in short term obligations of or guaranteed by, the Government of Canada (or other approved investments) pending satisfaction of the Escrow Release Condition.

Provided that the Transaction Closing Date occurs on or before the Deadline, the Escrowed Funds and the interest earned thereon (less the remaining portion of the Underwriters Fee' to be paid and the Dividend Equivalent Payment, if any) will be released to AltaGas and each holder of a Subscription Receipt will receive one Common Share for each Subscription Receipt held (subject to any applicable adjustment), without payment of additional consideration or further action, plus an amount per Common Share, if any, equal to the Dividend Equivalent Payment. AltaGas will utilize the Escrowed Funds to pay a portion of the purchase price of the SEMCO Shares pursuant to the Acquisition. See "Use of Proceeds".

In connection with the closing of the Acquisition, the Subscription Receipt Agent will release to AltaGas the Released Amount against: (i) an irrevocable direction of AltaGas to the Subscription Receipt Agent (in its capacity as registrar and transfer agent of the Common Shares) to issue the Common Shares to holders of record of Subscription Receipts as at the Transaction Closing Date; and (ii) a notice from AltaGas to the Subscription Receipt Agent, confirming that the Escrow Release Condition has been satisfied. Further, AltaGas shall issue a press release confirming that the Acquisition and the Offering have been completed, setting out the Transaction Closing Date, confirming that the Common Shares have been issued and stating the date on which the Subscription Receipt transfer register will close.

If the Transaction Closing Date does not occur prior to the Deadline, or if prior to such time the Stock Purchase Agreement is terminated in accordance with its terms or AltaGas advises the Subscription Receipt Agent and BMO, on behalf of the Underwriters, or discloses to the public that it does not intend to proceed with the Acquisition, the Subscription Receipt Agent and AltaGas will return to holders of Subscription Receipts an amount per Subscription Receipt equal to the Offering Price of the Subscription

Receipts plus a *pro rata* share of the interest earned on the Escrowed Funds, net of any applicable withholding taxes. The Escrowed Funds will be applied toward payment of such amount.

If the Transaction Closing Date occurs prior to a Termination and holders of Subscription Receipts become entitled to receive Common Shares pursuant to the Subscription Receipt Agreement, such holders will be entitled to receive an amount per Common Share equal to the Dividend Equivalent Payment. All or a portion of the Dividend Equivalent Payment will be satisfied by the payment by the Subscription Receipt Agent to holders of Subscription Receipts of interest earned on the Escrowed Funds, net of any applicable withholding taxes. The difference, if any, between the amount of interest earned on the Escrowed Funds and the dividends that would have been payable on the Common Shares will be paid by AltaGas. If holders of Subscription Receipts become entitled to receive Common Shares, the Subscription Receipt Agent and AltaGas will pay such amounts to holders on the later of the date the Common Shares are issued and the date such dividend(s) is paid to shareholders. For greater certainty, if the Transaction Closing Date occurs on a date that is a dividend record date, holders of Subscription Receipts shall not be entitled as such to receive a payment in respect of the cash dividend as holders of Subscription Receipts for such record date but shall instead be deemed to be holders of Common Shares on such date and will be entitled as Shareholders to receive such dividend.

The Corporation has covenanted in the Subscription Receipt Agreement that, from the Closing Date to the earlier of a Termination and the Transaction Closing Date, it will not subdivide or redivide the outstanding Common Shares into a greater number of Common Shares; reduce, combine or consolidate the outstanding Common Shares into a smaller number of Common Shares; issue any assets, securities or evidence of AltaGas or any other entity to holders of all or substantially all of the outstanding Common Shares by way of a dividend or distribution; or reclassify the Common Shares or undertake a reorganization of AltaGas or a consolidation, amalgamation, arrangement or merger of AltaGas with any other person or other entity; or a sale or conveyance of the property and assets of AltaGas as an entirety or substantially as an entirety to any other person or entity or a liquidation, dissolution or winding-up of AltaGas.

Subject to applicable law, AltaGas will be entitled to purchase the Subscription Receipts in the open market or by private agreement or otherwise.

The Subscription Receipt Agreement provides for modifications and alternations to the Subscription Receipts issued thereunder by way of an extraordinary resolution. The term “extraordinary resolution” is defined in the Subscription Receipt Agreement to mean, in effect, a resolution proposed at a meeting of holders of Subscription Receipts duly convened for that purpose and held in accordance with the Subscription Receipt Agreement at which there are present in person or by proxy at least one holder of Subscription Receipts entitled to receive more than 25% of the then outstanding Subscription Receipts and passed by the affirmative votes of holders of Subscription Receipts holding not less than 66% of the then outstanding Subscription Receipts represented at the meeting and voted on the poll upon such resolution.

Under the Subscription Receipt Agreement, original purchasers of Subscription Receipts under the Offering will have a contractual right of rescission following the issuance of the Common Shares to such purchaser upon the exchange of the Subscription Receipts, to receive the amount paid for the Subscription Receipts if this prospectus (including the documents incorporated by reference herein) and any amendment contains a misrepresentation or is not delivered to such purchaser, provided such remedy for rescission is exercised within 180 days of closing of the Offering.

Holders of Subscription Receipts are not Shareholders and do not have rights as Shareholders, including the right to vote at meetings of Shareholders. Holders of Subscription Receipts are entitled only to receive Common Shares on exchange of their Subscription Receipts or to a return of the price for the Subscription Receipts together with any payments in lieu of interest or dividends, as applicable, as described above.

PLAN OF DISTRIBUTION

Pursuant to the terms of the Underwriting Agreement, AltaGas has agreed to issue and sell 12,100,000 Subscription Receipts (13,915,000 Subscription Receipts if the Over-Allotment Option is exercised in full) to the Underwriters, and the Underwriters have severally (and not jointly or jointly and severally) agreed to purchase such Subscription Receipts on the Closing Date, at a price of \$29.00 per Subscription Receipt.

Delivery of the Subscription Receipts is conditional upon payment on closing of \$29.00 per Subscription Receipt by the Underwriters to the Subscription Receipt Agent (less 50% of the aggregate Underwriters' Fee). Completion of the Offering is also subject to a number of customary conditions, including the receipt of all required regulatory approvals and the approval of the TSX. The Underwriting Agreement provides that AltaGas will pay the Underwriters' Fee of \$1.16 per Subscription Receipt for Subscription Receipts issued under the Offering in consideration for their services in connection with the Offering. The Underwriters' Fee is payable as to 50% upon the closing of the Offering and 50% upon closing of the Acquisition. If a Termination occurs, the Underwriters' Fee in respect of the Subscription Receipts will consist solely of the amount paid upon closing of the Offering. The terms of the Offering were determined by negotiation between AltaGas and BMO, RBC and TD, on their own behalf and on behalf of the other Underwriters.

AltaGas has granted the Underwriters the Over-Allotment Option which is exercisable at the Underwriters' discretion, to purchase from AltaGas, up to an additional 1,815,000 Subscription Receipts at a price equal to the Offering Price, to cover over-allocations, if any, and for market stabilization purposes. The Over-Allotment Option is exercisable in whole or in part, at any time from closing of the Offering up to the date that is 30 days following the date of closing of the Offering. If the Underwriters exercise the Over-Allotment Option in full, the total Price to the Public, Underwriters' Fee, and Net Proceeds to AltaGas will be \$403,535,000, \$16,141,400 and \$387,393,600, respectively. This prospectus qualifies the grant of the Over-Allotment Option and the distribution of any Subscription Receipts issued or sold pursuant to the exercise of the Over-Allotment Option. A subscriber who acquires Subscription Receipts forming part of the Underwriters' over-allocation position acquires such Subscription Receipts under this prospectus, regardless of whether the over-allocation position is ultimately filled through the exercise of the Over-Allotment Option or secondary market purchases.

The obligations of the Underwriters under the Underwriting Agreement are several and not joint, and may be terminated at their discretion upon the occurrence of certain stated events. The obligations of AltaGas and the Underwriters under the Underwriting Agreement to complete the purchase and sale of the Subscription Receipts will terminate automatically if a Termination occurs. If an Underwriter fails to purchase the Subscription Receipts which it has agreed to purchase, the remaining Underwriter(s) may terminate their obligation to purchase their allotment of Subscription Receipts, or may, but are not obligated to, purchase the Subscription Receipts not purchased by the Underwriter or Underwriters which fail to purchase; provided, however, that in the event that the percentage of the total number of Subscription Receipts which one or more Underwriters has failed or refused to purchase is less than 8% of the total number of the Subscription Receipts which the Underwriters have agreed to purchase, the other Underwriters shall be obligated severally to purchase on a *pro rata* basis the Subscription Receipts

which would otherwise have been purchased by the one or more Underwriters which failed or refused to purchase. The Underwriters are, however, obligated to take up and pay for all Subscription Receipts if any are purchased under the Underwriting Agreement. The Underwriting Agreement also provides that AltaGas will indemnify the Underwriters and their directors, officers, agents, shareholders and employees against certain liabilities and expenses.

The Subscription Receipts will be issued in “book entry only” form and must be purchased or transferred through a Participant. See “*Depository Services*”.

Pursuant to policy statements of certain provincial securities regulators, the Underwriters may not, throughout the period of distribution, bid for or purchase Subscription Receipts or Common Shares for the purpose of creating actual or apparent active trading in, or raising the price of, the Subscription Receipts or Common Shares. Exceptions to these policy statements include a bid or purchase permitted under the Universal Market Integrity Rules of the Investment Industry Regulatory Organization of Canada, relating to market stabilization and passive market making activities and a bid or purchase made for and on behalf of a customer where the order was not solicited during the period of distribution. Pursuant to the first mentioned exception, in connection with the Offering, the Underwriters may over-allot or effect transactions which stabilize or maintain the market price of the Subscription Receipts and Common Shares at levels other than those which otherwise might prevail on the open market. Such transactions, if commenced, may be discontinued at any time.

The Underwriters propose to offer the Subscription Receipts initially at the Offering Price specified herein. After a reasonable effort has been made to sell all of the Subscription Receipts at the price specified, the Underwriters may subsequently reduce the selling prices to investors from time to time in order to sell any of the Subscription Receipts remaining unsold. In the event the Offering Price of the Subscription Receipts is reduced, the compensation received by the Underwriters will be decreased by the amount the aggregate price paid by the purchasers for the Subscription Receipts is less than the gross proceeds paid by the Underwriters to AltaGas for the Subscription Receipts. Any such reduction will not affect the proceeds received by AltaGas.

AltaGas has agreed that, subject to certain exceptions, it shall not issue or agree to issue any Common Shares or other securities convertible into, or exchangeable for, Common Shares during the period ending 90 days after the Closing Date without the prior consent of BMO, RBC and TD, on their own behalf and on behalf of the other Underwriters, which consent shall not be unreasonably withheld.

The TSX has conditionally approved the listing of the Subscription Receipts distributed under this short form prospectus and the Common Shares issuable upon exchange of the Subscription Receipts on the TSX. Listing of such securities is subject to AltaGas fulfilling all of the listing requirements of the TSX on or before May 7, 2012.

Subscriptions will be received subject to rejection or allotment in whole or in part and the Underwriters reserve the right to close the subscription books at any time without notice. It is currently anticipated that the Closing Date of the Offering will be February 22, 2012, or such later date as AltaGas and the Underwriters may agree but in any event not later than March 15, 2012.

The Subscription Receipts offered hereby and the Common Shares issuable on exchange thereof (collectively, the “**Securities**”) have not been and will not be registered under the 1933 Act, or any state securities laws, and accordingly may not be offered or sold within the United States except in transactions exempt from the registration requirements of the 1933 Act and applicable state securities laws. Except as

permitted in the Underwriting Agreement, the Underwriters will not offer or sell the Subscription Receipts within the United States. The Underwriting Agreement permits the Underwriters to offer and resell the Subscription Receipts that they have acquired pursuant to the Underwriting Agreement to qualified institutional buyers (as defined in Rule 144A under the 1933 Act), in the United States, provided such offers and sales are made in transactions exempt from the registration requirements of the 1933 Act in accordance with Rule 144A thereunder and similar exemptions under applicable state securities laws. The Underwriting Agreement also provides that the Underwriters will offer and sell the Subscription Receipts outside the United States only in accordance with Regulation S under the 1933 Act.

In addition, until 40 days after the commencement of the Offering, an offer or sale of Securities within the United States by any dealer (whether or not participating in the Offering) may violate the registration requirements of the 1933 Act if such offer or sale is made otherwise than in accordance with an exemption from the registration requirements of the 1933 Act.

DEPOSITORY SERVICES

The Subscription Receipts will be issued in “book entry only” form and must be purchased or transferred through a CDS Participant. AltaGas will cause a global certificate or certificates representing any newly issued Subscription Receipts to be delivered to, and registered in the name of, CDS or its nominee. All rights of holders of Subscription Receipts must be exercised through, and all payments or other property to which such holder of Subscription Receipts, as the case may be, is entitled, will be made or delivered by, CDS or the CDS Participant through which the holder of Subscription Receipts holds such Subscription Receipts. Each person who acquires Subscription Receipts will receive only a customer confirmation of purchase from the registered dealer from or through which the Subscription Receipts are acquired in accordance with the practices and procedures of that registered dealer. The practices of registered dealers may vary, but generally customer confirmations are issued promptly after execution of a customer order. CDS is responsible for establishing and maintaining book entry accounts for its CDS Participants having interests in the Subscription Receipts.

The ability of a beneficial owner of Subscription Receipts to pledge such securities or otherwise take action with respect to such owner’s interest in such shares (other than through a CDS Participant) may be limited due to the lack of a physical certificate.

AltaGas has the option to terminate registration of the Subscription Receipts through the book entry only system, in which event certificates for Subscription Receipts in fully registered form will be issued to the beneficial owners of such securities or their nominees.

Neither AltaGas nor the Underwriters will assume any liability for: (a) any aspect of the records relating to the beneficial ownership of the Subscription Receipts held by CDS or the payments relating thereto; (b) maintaining, supervising or reviewing any records relating to the Subscription Receipts; or (c) any advice or representation made by or with respect to CDS and those contained in this prospectus and relating to the rules governing CDS or any action to be taken by CDS or at the direction of its CDS Participants. The rules governing CDS provide that it acts as the agent and depository for the CDS Participants. As a result, CDS Participants must look solely to CDS and persons, other than CDS Participants, having an interest in the Subscription Receipts must look solely to CDS Participants for payments made by or on behalf of AltaGas to CDS in respect of the Subscription Receipts.

If (i) required by applicable law, (ii) the book entry only system ceases to exist, (iii) CDS advises AltaGas that it is no longer willing or able to discharge properly its responsibilities as depository with respect to

the Subscription Receipts and AltaGas is unable to locate a qualified successor, or (iv) AltaGas, at its option, decides to terminate the book entry only system, then certificates representing the Subscription Receipts, as applicable, will be made available.

Upon the occurrence of any of the events described in the immediately preceding paragraph, the Subscription Receipt Agent must notify CDS, for and on behalf of CDS Participants and beneficial owners of the Subscription Receipts of the availability through CDS of certificates. Upon surrender by CDS of the global certificates representing the Subscription Receipts and receipt of instructions from CDS for the new registrations, the Subscription Receipt Agent will deliver the Subscription Receipts in the form of certificates and thereafter AltaGas will recognize the holders of such certificates as securityholders under the Subscription Receipt Agreement.

RELATIONSHIP BETWEEN ALTAGAS AND CERTAIN OF THE UNDERWRITERS

BMO, RBC, TD, CIBC, National, Scotia and HSBC are, directly or indirectly, subsidiaries or affiliates of certain lenders which are lenders to AltaGas or its subsidiaries. In addition, TD, BMO and RBC are affiliates of Canadian chartered banks that have agreed to provide the New Credit Facility to AltaGas in connection with financing the Acquisition. BMO also acted as financial advisor to AltaGas in connection with the Acquisition. Accordingly, pursuant to applicable securities legislation, AltaGas may be considered a “connected issuer” of such Underwriters. As at November 30, 2011, neither AltaGas nor its subsidiaries were indebted under the Syndicated Facility or the AUGI Facility. As at November 30, 2011, AltaGas or its subsidiaries were indebted to a lender affiliate of each of TD and CIBC in the approximate amount of \$58.8 million (including letters of credit) under the LC Credit Facility and to a non-affiliated lender in the approximate amount of \$124.3 million (including letters of credit) under the Bilateral Facility. The Credit Facilities are unsecured. AltaGas and its subsidiaries are presently in compliance with the terms of such Credit Facilities and none of the lenders has waived a breach of the agreements governing such Credit Facilities since their execution. The consolidated financial position of AltaGas has not changed materially since the indebtedness under such Credit Facilities was incurred. None of the lenders were involved in the decision to offer the Subscription Receipts or were involved in the determination of the terms of the distribution of the Subscription Receipts. As a consequence of the sale of the Subscription Receipts, each of the Underwriters will receive a fee in respect of Subscription Receipts sold through such Underwriter. See “*Use of Proceeds*”.

ELIGIBILITY FOR INVESTMENT

In the opinion of Counsel, subject to the provisions of any particular plan and provided that the Subscription Receipts and Common Shares are listed on a designated stock exchange (which includes the TSX), the Subscription Receipts and the Common Shares issuable on the exchange of the Subscription Receipts, if issued on the date hereof, generally would be qualified investments under the Tax Act and the regulations thereunder (the “**Regulations**”) for a trust governed by a registered retirement savings plan (a “**RRSP**”), a registered retirement income fund (a “**RRIF**”), a registered education savings plan, a registered disability savings plan, a deferred profit sharing plan, or a tax-free savings account (a “**TFSA**”).

Notwithstanding that the Subscription Receipts and Common Shares issuable on the exchange of Subscription Receipts may be qualified investments for a trust governed by a TFSA, RRSP or RRIF, the holder of a TFSA or the annuitant of a RRSP or RRIF will be subject to a penalty tax on the Subscription Receipts and Common Shares and other tax consequences may result if the Subscription Receipts or Common Shares are a “prohibited investment” for the TFSA, RRSP or RRIF, as the case may be. The Subscription Receipts and Common Shares will generally be a “prohibited investment” if the holder of a

TFSA or the annuitant of a RRSP or RRIF does not deal at arm's length with AltaGas for purposes of the Tax Act or has a "significant interest" (as defined in the Tax Act) in AltaGas or a corporation, partnership or trust with which AltaGas does not deal at arm's length for purposes of the Tax Act. Prospective purchasers who intend to hold Subscription Receipts or Common Shares in a TFSA, RRSP or RRIF should consult their own tax advisors regarding their particular circumstances.

CANADIAN FEDERAL INCOME TAX CONSIDERATIONS

In the opinion of Counsel, the following is a general summary of the principal Canadian federal income tax considerations generally applicable to a holder who acquires Subscription Receipts pursuant to the Offering and who, for the purposes of the Tax Act, and at all relevant times, is or is deemed to be resident in Canada, deals at arm's length with, and is not affiliated with, AltaGas and holds or will hold the Subscription Receipts and any Common Shares issuable on the exchange of the Subscription Receipts as capital property. Generally, the Subscription Receipts and the Common Shares will be considered to be capital property to a holder provided the holder does not hold the Subscription Receipts and the Common Shares in the course of carrying on a business and has not acquired them in a transaction or transactions considered to be an adventure in the nature of trade. Certain holders whose Common Shares might not otherwise qualify as capital property may, in certain circumstances, make the irrevocable election under subsection 39(4) of the Tax Act to have their Common Shares and every "Canadian security" (as defined in the Tax Act) owned by such holder in the taxation year of the election, and in all subsequent years, deemed to be capital property. This election is not available in respect of the Subscription Receipts.

The Tax Act contains provisions (the "**Mark-to-Market Rules**") relating to securities held by certain financial institutions, registered securities dealers and corporations controlled by one or more of the foregoing. This summary does not take into account the Mark-to-Market Rules and taxpayers that are "financial institutions" as defined for the purposes of the Mark-to-Market Rules should consult their own tax advisors. This summary is not applicable to a purchaser that is a "specified financial institution" or an interest in which is a "tax shelter investment", all as defined in the Tax Act, or to a purchaser whose functional currency for purposes of the Tax Act is the currency of a country other than Canada. Such purchasers should consult their own tax advisors.

This summary is based upon the provisions of the Tax Act and Regulations in force as at the date hereof, all specific proposals (the "**Tax Proposals**") to amend the Tax Act and the Regulations that have been publicly announced by or on behalf of the Minister of Finance (Canada) prior to the date hereof and Counsel's understanding of the current published administrative practices and assessing policies of the Canada Revenue Agency. This summary assumes that the Tax Proposals will be enacted in the form proposed. However, no assurance can be given that the Tax Proposals will be enacted in the form proposed, if at all. Except for the Tax Proposals, this summary does not take into account or anticipate any changes in applicable law, whether by legislative, governmental or judicial decision or action, nor does it take into account any changes in the administrative practices or assessing policies of the Canada Revenue Agency. This summary does not take into account provincial, territorial or foreign tax laws or considerations, which might differ significantly from those discussed herein.

This summary is of a general nature only and is not intended to be, nor should it be construed to be, legal or tax advice or representations to any particular holder. This summary is not exhaustive of all possible income tax considerations under the Tax Act that may affect a holder. The income tax consequences of acquiring and disposing of Subscription Receipts and Common Shares will vary depending on a number of factors, including the legal status of the holder as an individual, corporation, trust or partnership. Accordingly, prospective holders of Subscription Receipts and Common Shares should consult their own

tax advisors with respect to their particular circumstances and the tax consequences to them of holding and disposing of Subscription Receipts and Common Shares.

Exchange of Subscription Receipts

No gain or loss will be realized by a holder on the exchange of Subscription Receipts for Common Shares.

The cost of a Common Share issued to a holder of a Subscription Receipt acquired pursuant to the Offering will be equal to the cost of the Subscription Receipt to the holder. The cost to the holder of the Common Shares so acquired generally must be averaged with the cost of all other Common Shares owned at that time by the holder as capital property to determine the adjusted cost base of each Common Share held.

Termination of Subscription Receipts

As described above under “*Details of the Offering*”, if the Transaction Closing Date does not occur prior to the Deadline, or if prior to such time the Stock Purchase Agreement is terminated in accordance with its terms or AltaGas advises the Subscription Receipt Agent and BMO, on behalf of the Underwriters, or discloses to the public that it does not intend to proceed with the Acquisition, the Subscription Receipt Agent and AltaGas will return to holders of Subscription Receipts an amount per Subscription Receipt equal to the Offering Price of the Subscription Receipts plus a *pro rata* share of the interest earned on the Escrowed Funds, net of any applicable withholding taxes. In that event, a holder of Subscription Receipts that is a corporation will be required to include in computing its income for a taxation year any interest on the Escrowed Funds (i) that accrues or that is deemed to accrue to it to the end of the particular taxation year, or (ii) that has become receivable by or is received by the holder before the end of that taxation year, except to the extent that such interest was included in computing the holder’s income for a preceding taxation year. Any other holder of Subscription Receipts, including an individual, will be required to include in computing income for a taxation year all interest on the Escrowed Funds that is received or receivable by the holder in that taxation year (depending upon the method regularly followed by the holder in computing income), except to the extent that the interest was included in the holder’s income for a preceding taxation year.

Payment of Dividend Equivalent

As described above under “*Details of the Offering*”, if Common Shares are issued in exchange for Subscription Receipts, and if dividends have been declared on the Common Shares of AltaGas to holders of record on a date during the period from the Closing Date to the date of such issuance of Common Shares, AltaGas will make a cash payment to the holders of Subscription Receipts in respect of each Subscription Receipt in an amount equal to the per share amount of such dividend. Any such payment equivalent to such dividends paid to a holder of Subscription Receipts by AltaGas must be included in the income of the holder. Any amount so included will be taxed as ordinary income and not as a dividend and, as such, will not be subject to the gross-up and dividend tax credit rules described below.

Other Dispositions of Subscription Receipts

A disposition or deemed disposition by a holder of a Subscription Receipt, other than on the exchange of a Subscription Receipt for a Common Share or a disposition of the Subscription Receipt to AltaGas in the event that the Transaction Closing Date does not occur prior to the Deadline, or if prior to such time the

Stock Purchase Agreement is terminated in accordance with its terms or AltaGas advises the Subscription Receipt Agent and BMO, on behalf of the Underwriters, or discloses to the public that it does not intend to proceed with the Acquisition, will generally result in the holder realizing a capital gain (or a capital loss) equal to the amount by which the proceeds of disposition of the Subscription Receipt exceed (or are less than) the aggregate of the holder's adjusted cost base of the Subscription Receipt and any reasonable costs of disposition. See below under the heading "*Tax Treatment of Capital Gains and Losses*".

Dividends on Common Shares

Dividends received on Common Shares by a holder who is an individual will be included in the individual's income and will be subject to the gross-up and dividend tax credit rules normally applicable to taxable dividends received from taxable Canadian corporations, including the enhanced gross-up and dividend tax credit for "eligible dividends". A dividend will be eligible for the enhanced gross-up and dividend tax credit if the paying corporation designates the dividend as an eligible dividend. There may be limitations on the ability of a corporation to designate dividends as eligible dividends. On its website, AltaGas has advised its shareholders that all dividends paid on the Common Shares will be designated as eligible dividends. Taxable dividends received by an individual may give rise to alternative minimum tax under the Tax Act, depending on the individual's circumstances.

Dividends received on Common Shares by a holder that is a corporation will be included in income and normally will be deductible in computing such corporation's taxable income. However, such dividends received by a corporation that was, at any time in the taxation year in which such dividends were received, a "private corporation" as defined in the Tax Act, or a corporation resident in Canada that is controlled by or for the benefit of an individual (other than a trust) or a related group of individuals (other than trusts), generally will be subject to a refundable tax of 33½% under Part IV of the Tax Act to the extent that such dividends are deductible in computing the corporation's taxable income.

Disposition of Common Shares

In general, a disposition or a deemed disposition of a Common Share will give rise to a capital gain (or a capital loss) equal to the amount by which the proceeds of disposition of the Common Share, net of any reasonable costs of disposition, exceed (or are less than) the adjusted cost base to the holder of the Common Share immediately before the disposition. See below under the heading "*Tax Treatment of Capital Gains and Losses*".

Tax Treatment of Capital Gains and Losses

Generally, one-half of any capital gain (a "**taxable capital gain**") realized by a holder in a taxation year will be included in computing the holder's income for such year, and one-half of any capital loss (an "**allowable capital loss**") realized by a holder in a taxation year must be deducted by the holder against taxable capital gains realized by the holder in the year. Allowable capital losses for a taxation year in excess of taxable capital gains for that year generally may be carried back and deducted against net taxable capital gains in any of the three preceding years or carried forward and deducted against net taxable capital gains in any subsequent year, in accordance with the rules contained in the Tax Act. Capital gains realized by an individual may give rise to a liability for alternative minimum tax.

The amount of any capital loss realized on the disposition or deemed disposition of a Common Share by a holder that is a corporation may be reduced by the amount of dividends received by the holder on the Common Share to the extent and in the circumstances prescribed by the Tax Act. Similar rules may apply

where a corporation is a member of a partnership or a beneficiary of a trust that owns Common Shares and where a trust is a member of a partnership that owns Common Shares or a partnership or trust is a beneficiary of a trust that owns Common Shares. Holders to whom these rules may be relevant should consult their own tax advisors.

Additional Refundable Tax

A holder that is a “Canadian-controlled private corporation” (as defined in the Tax Act) may be liable to pay an additional refundable tax of 6 $\frac{2}{3}$ % on certain investment income, including amounts in respect of taxable capital gains and interest (but not dividends deductible in computing taxable income).

RISK FACTORS

An investment in the Subscription Receipts is subject to certain risks. Investors should carefully consider the risks described under the heading “Risk Factors” in the AIF incorporated herein by reference, as well as the risk factors set out below prior to making an investment in the Subscription Receipts.

Risks Related to the Acquisition

Possible Failure to Realize Anticipated Benefits of the Acquisition.

A variety of factors, including those risk factors set forth in this prospectus and the documents incorporated by reference herein, may adversely affect the ability to achieve the anticipated benefits of the Acquisition.

Satisfaction of Conditions Precedent.

The completion of the Acquisition is subject to a number of conditions precedent, certain of which are outside the control of AltaGas or other parties to the Stock Purchase Agreement, including obtaining the Required Regulatory Approvals. There is no certainty, nor can AltaGas provide any assurance, that these conditions will be satisfied or, if satisfied, when they will be satisfied.

Pursuant to the Stock Purchase Agreement, AltaGas and Acquireco must use their reasonable best efforts to agree to conditions to completion of the Acquisition that may be imposed by governmental entities, including divestitures of assets of SEMCO, and to accept operational restrictions relating to SEMCO unless such would have a material adverse effect on SEMCO and its subsidiaries, taken as a whole, or AltaGas and its subsidiaries, taken as a whole. There can be no assurance that in order to satisfy their obligations under the Stock Purchase Agreement that AltaGas and Acquireco will not be required to accept one or more such conditions or restrictions that could have a material effect on the business, operations and assets of SEMCO or AltaGas.

Additionally, AltaGas expects that closing of the Acquisition will occur in third quarter, 2012. However, the Outside Date allows the transaction to close as late as June 2013 in certain circumstances. While during the period prior to closing SEMCO is to carry on business in the ordinary course, given the potentially long period prior to closing the Acquisition there can be no assurance that the business, operations and assets of SEMCO may not be adversely affected by intervening events. While it is a condition to closing the Acquisition that SEMCO not be subject to a material adverse effect, it is possible that the business of SEMCO could be significantly affected prior to such a condition being breached. During the period prior to closing the Acquisition, AltaGas and Acquireco will have no right to control or

direct the operations of SEMCO and SEMCO shall exercise complete unilateral control and supervision over its business operations, subject to the terms of the Stock Purchase Agreement and therefore AltaGas will, indirectly be reliant on the business judgment and decisions of the board and management of SEMCO prior to closing the Acquisition.

Regulatory Risk.

The Acquisition is conditional upon, among other things, all waiting periods applicable to the Acquisition under the HSR Act having expired or been terminated and the receipt of all Required Regulatory Approvals. A substantial delay in obtaining satisfactory approvals or the imposition of unfavourable terms or conditions in the approvals could have a material adverse effect on AltaGas' ability to complete the Acquisition and on AltaGas' or SEMCO's business, financial condition or results of operations. See "*The Acquisition Agreement — Termination*".

Exchange Rate Risk.

In addition to the net proceeds from the Offering, advances under some combination of the Credit Facilities and the New Credit Facility, among other things, are anticipated to be used to fund the purchase price of the Acquisition. The closing of the Acquisition is expected to occur in the third quarter of 2012, but may close at any time up to and including June 30, 2013. As AltaGas anticipates funding a portion of the purchase price of the Acquisition from a combination of Canadian and U.S. dollar denominated securities and credit lines, and the purchase price of the Acquisition is denominated in U.S. dollars, a significant decline in the value of the Canadian dollar relative to the U.S. dollar could increase the cost to AltaGas of funding the purchase price of the Acquisition.

Possible Failure to Complete the Acquisition.

The Acquisition is subject to normal commercial risk that the Acquisition may not be completed on the terms negotiated or at all. If the Acquisition is not completed prior to the Deadline, then the Subscription Receipts will be cancelled and the holders of Subscription Receipts will be entitled to receive a refund of their subscription price and their *pro rata* entitlement to interest accrued thereon, net of any applicable withholding taxes. The purchaser would not be entitled to participate in any growth in the trading price of the Common Shares. Further, the purchaser would be restricted from using the funds devoted to the acquisition of the Subscription Receipts for any other investment opportunities until the Escrowed Funds are returned to the purchaser. In addition, if closing of the Acquisition does not take place as contemplated, AltaGas could suffer adverse consequences, including the loss of investor confidence. The discovery or quantification of any material liabilities could have a material adverse effect on AltaGas' business, financial condition or future prospects. In addition, the Acquisition Agreement limits the amount for which AltaGas is indemnified. See "*The Acquisition Agreement — Indemnification*".

Potential Undisclosed Liabilities Associated with the Acquisition.

In connection with the Acquisition, there may be liabilities that AltaGas failed to discover or was unable to quantify in its due diligence which it conducted prior to the execution of the Stock Purchase Agreement and which could have a material adverse effect on AltaGas' business, financial condition or future prospects. In addition, AltaGas and Acquireco may not be indemnified for some or all of these liabilities. Continental will have no liability to purchasers of Subscription Receipts pursuant to this Offering if the disclosure relating to the Acquisition, the SEMCO business and the Stock Purchase Agreement contain a misrepresentation. See "*The Acquisition Agreement — Indemnification*".

Market for Securities.

There is currently no market through which the Subscription Receipts may be sold and purchasers may not be able to resell Subscription Receipts purchased under this short form prospectus. There can be no assurance that an active trading market will develop for the Subscription Receipts after completion of the Offering, or if developed, that such a market will be sustained at the price level of the Offering.

Increased Indebtedness.

If the Acquisition is completed on the terms contemplated in the Acquisition Agreement, AltaGas anticipates borrowing approximately \$488 million in aggregate under the Credit Facilities and the New Credit Facility. Such borrowings will represent a material increase in AltaGas' consolidated indebtedness. AltaGas expects to have \$2.017 billion of consolidated indebtedness as at September 30, 2011, outstanding on a *pro forma* basis after giving effect to the Acquisition and certain other transactions. See "*Acquisition of SEMCO – Financing the Acquisition*", "*Use of Proceeds*" and "*Consolidated Capitalization*". Such additional indebtedness will increase AltaGas' interest expense and debt service obligations and may have a negative effect on AltaGas' results of operations or credit ratings. The increased indebtedness will also make AltaGas' results more sensitive to increases in interest rates.

AltaGas' degree of leverage could have other important consequences for purchasers, including the following:

- have a negative effect on the current credit ratings on AltaGas' rated long term debt
- it may limit AltaGas' ability to obtain additional financing for working capital, capital expenditures, debt service requirements, acquisitions and general corporate or other purposes;
- it may limit AltaGas' ability to declare dividends on the Common Shares;
- certain of AltaGas' borrowings are at variable rates of interest and expose AltaGas to the risk of increased interest rates;
- it may limit AltaGas' ability to adjust to changing market conditions and place AltaGas at a competitive disadvantage compared to its competitors that have less debt;
- AltaGas may be vulnerable in a downturn in general economic conditions; and
- AltaGas may be unable to make capital expenditures that are important to its growth and strategies.

Under the terms of both the New Credit Facility and the Credit Facilities, AltaGas is permitted to incur additional debt in certain circumstances. However, doing so could increase the risks described above. Such credit facilities contain certain financial covenants requiring AltaGas on a consolidated basis to satisfy specified interest coverage and debt to total capitalization ratios. Such credit facilities also contain covenants restricting AltaGas' ability to incur liens on its assets, incur additional debt, effect acquisitions or dispositions or fundamental changes in its business or pay dividends on the Common Shares. These covenants will limit AltaGas' discretion in the operation of its business.

The availability to AltaGas of borrowings under the New Credit Facility and the Credit Facilities is subject to various conditions AltaGas must satisfy. If AltaGas is unable to satisfy the conditions under such credit facilities, that inability could have a material adverse effect on AltaGas and its ability to complete the Acquisition.

AltaGas' ability to borrow under the New Credit Facility and, to a lesser degree, the Credit Facilities, is subject to certain customary conditions that AltaGas must satisfy. If AltaGas is unable to satisfy one or more of those conditions and such conditions are not waived, AltaGas will not be able to borrow amounts under the New Credit Facility or the Credit Facilities to fund the Acquisition. It is not a condition to AltaGas' obligation to complete the Acquisition that it has necessary sources of financing to do so. If AltaGas cannot borrow under the New Credit Facility or the Credit Facilities, it is possible that alternative sources of financing may not be available, which could result in AltaGas' breach of the Stock Purchase Agreement or that alternative sources, if available, may be on terms that are less favourable than the terms of the New Credit Facility or the Credit Facilities. See "*Acquisition of SEMCO – Financing the Acquisition*".

Increased Exposure to Fluctuations in Exchange Rate Between U.S. and Canadian Dollars.

AltaGas' consolidated results of operations may be negatively impacted by foreign currency fluctuations. As a result of the Acquisition, a substantial portion of AltaGas' revenues will be earned in U.S. dollars. For purposes of U.S. GAAP, which AltaGas' intends to prepare and file its consolidated financial statements in accordance with for financial years commencing on or after January 1, 2012 and for the interim periods therein, revenues and expenses denominated in non-U.S. currencies are translated into U.S. dollars at the average exchange rates prevailing during the year. If the U.S. dollar were to strengthen relative to the Canadian dollar, the amount of net income reported in AltaGas' consolidated statement of operations from non-U.S. dollar denominated business would decrease.

Subscription Receipt Structure.

The Subscription Receipts will be automatically exchanged for Common Shares upon the occurrence of the Escrow Release Condition. AltaGas may, in its sole discretion but subject to the limitations imposed by the Subscription Receipt Agreement, waive certain closing conditions in AltaGas' favour in the Stock Purchase Agreement or agree with Continental to amend the Stock Purchase Agreement and consummate the Acquisition on terms that may be substantially different from those contemplated in this prospectus. As a result, the expected benefits of the Acquisition may not be fully realized. See "*Acquisition of SEMCO – The Acquisition Agreement*". There can be no assurance that the Escrow Release Condition will be satisfied on or prior to the Deadline. Until the Escrow Release Condition is satisfied and the Common Shares are delivered pursuant to the Subscription Receipt Agreement, holders of Subscription Receipts have the rights as described under "*Details of the Offering*".

Obligation to Repurchase Senior Notes.

Following completion of the Acquisition, SEMCO Energy will continue to be liable for the obligations under its US\$300 million of Senior Notes. There is some ambiguity in the indenture for the Senior Notes as to whether the Acquisition would be a change of control for purposes of the indenture. If the Acquisition would be a change of control for those purposes, and the Acquisition is accompanied or followed within a specified period of time by a downgrade in ratings of the Senior Notes by at least two rating agencies to a below investment grade rating, holders of the Senior Notes will have the right to require SEMCO Energy to make an offer to repurchase the Senior Notes for cash at a price equal to 101% of their aggregate principal amount, plus accrued and unpaid interest, if any. If SEMCO Energy is obligated to make an offer in the circumstances set forth above, SEMCO Energy or AltaGas (or another subsidiary of AltaGas) may incur additional indebtedness to fund such obligation, with the potential ramifications discussed above under “*Increased Indebtedness*”. SEMCO Energy and AltaGas’ ability to pay cash to holders of the Senior Notes upon a repurchase may be limited by SEMCO Energy and AltaGas’ financial resources at the time of such repurchase. SEMCO Energy’s failure to purchase the Senior Notes in connection with a change of control and a ratings downgrade of the nature described above would result in a default under the indenture. Such a default may, in turn, constitute a default under SEMCO Energy or AltaGas’ existing debt, and may constitute a default under future debt as well. Any sources of financing that SEMCO Energy may obtain to finance the repurchase of the Senior Notes may be on terms that are less favourable than the terms of the Senior Notes. Accordingly, triggering SEMCO Energy’s obligation to repurchase the Senior Notes could have a material adverse effect on SEMCO Energy and AltaGas’ business, financial condition or future prospects.

Risks Related to the Business of SEMCO

The risk factors set forth in the AIF and in this short form prospectus relating to the business and operations of AltaGas’ natural gas distribution business apply equally in respect of SEMCO’s business. In addition, purchasers should carefully consider the incremental risks in relation to SEMCO’s business as set forth below.

SEMCO is subject to extensive and complex regulations and legislation that affect its business, financial position and results of operations.

SEMCO is subject to extensive and complex regulations and laws enforced by various regulatory agencies. These regulatory agencies include the MPSC, RCA, and the U.S. Environmental Protection Agency. SEMCO is also subject to regulation by other federal, state and local agencies. Regulations affect almost every aspect of SEMCO’s business and limit its ability to make and implement independent management decisions, including about business combinations, disposing of operating assets, setting rates charged to customers, issuing debt and engaging in transactions between SEMCO and its affiliates.

Regulations and laws are subject to ongoing policy initiatives, and SEMCO cannot predict the future course of regulations or legislation and their respective ultimate effects. Such changes could materially impact SEMCO’s business, financial position and results of operations.

SEMCO’s gas distribution business is subject to rate regulation, and certain actions of applicable regulatory bodies may reduce SEMCO’s revenues, earnings and cash flow.

SEMCO is currently regulated by the MPSC in Michigan and the RCA in Alaska. These regulatory bodies have jurisdiction over, among other things, rates, accounting procedures and standards of service.

While SEMCO currently has settlements with the MPSC and the RCA setting base rates in these jurisdictions, there is no guarantee that SEMCO would prevail in seeking rate increases in future rate cases. SEMCO also has no guarantee that it will be successful in its gas cost recovery cases filed periodically with various regulatory bodies. The possibility of a rate decrease, the failure to grant any requested rate increase, cost disallowances, the precise timing of any rate increase, decrease or any other action by the regulators, may reduce SEMCO's revenues, earnings and cash flow.

The increased cost of purchasing natural gas during periods in which natural gas prices are rising significantly could adversely impact SEMCO's liquidity and earnings.

One component of the regulation of SEMCO's rates is a mechanism to recover the cost of purchasing natural gas. In general, the costs of natural gas purchased for customers are recovered on a dollar-for-dollar basis (in the absence of disallowances), without a profit component. The recovery of these gas costs is accomplished through regulatory body-approved GCR pricing mechanisms whereby customer rates are periodically adjusted for increases and decreases in the cost of gas purchased by SEMCO for sale to its customers. Under the GCR pricing mechanisms, the gas commodity charge portion of gas rates charged to customers (which is also referred to as the "GCR rate") for the Michigan service areas may be adjusted upward and downward on a monthly basis if actual natural gas costs incurred by SEMCO are different than the prices set in the MPSC-approved GCR plan. The GCR rate for Alaska is adjusted quarterly to reflect the estimated cost of gas purchased for the upcoming 3-month GCR period.

Increases in natural gas prices and corresponding increases in GCR rates may contribute, in varying amounts, depending on the way in which these costs are recovered in customer rates in each jurisdiction in which SEMCO does business, to: (i) increased costs associated with lost and unaccounted for gas; (ii) higher customer bad debt expense for uncollectible accounts; (iii) higher working capital requirements; and (iv) reduced sales volumes and related margins due to lower customer consumption.

Volatility in the price of natural gas could result in large industrial customers switching to alternative energy sources or shifting production to facilities outside SEMCO's service area, which could reduce revenues, earnings and cash flow.

The market price of alternative energy sources such as coal, electricity, oil and steam is the primary competitive factor affecting the demand for SEMCO's gas transportation services in Michigan. Certain large industrial customers have, or may acquire, the capacity to be able to use one or more alternative energy sources or shift production to facilities outside SEMCO's service area if the price of SEMCO-provided natural gas and delivery services increases significantly compared to prices charged for such services elsewhere. Natural gas has typically been less expensive than these alternative energy sources. However, at certain times natural gas prices have been higher than prices for alternative fuels and more volatile, making some of these alternative energy sources more economical or, for other reasons, more attractive than natural gas. During these periods, certain of SEMCO's large Michigan industrial customers have periodically switched to alternative energy sources, and some customers have the ability to shift production to other facilities if energy costs at those facilities are lower than at facilities served by SEMCO.

To reduce the possibility of fuel-switching or production-shifting by industrial customers, SEMCO offers flexible contract terms and additional services, such as gas storage and balancing. Partially offsetting the impact of this price sensitivity among certain large industrial customers has been the use of natural gas to reduce emissions from their plants. It is not possible to predict the future trend of natural gas prices with certainty nor make any assurances that the impact of environmental legislation or any special services

SEMCO offers will outweigh the negative effects of natural gas price increases and volatility. Should these customers decide to use another form of energy or shift production elsewhere, SEMCO's revenues, earnings and cash flow would be adversely affected.

SEMCO's liquidity and earnings could be adversely affected by the MPSC's disallowance of costs after retrospective reviews of SEMCO's gas procurement practices.

In Michigan, SEMCO's gas procurement practices are subject to an annual retrospective MPSC review. If costs are disallowed in this review process, such costs would be expensed in the cost of gas but would not be recovered by SEMCO in rates. MPSC reviews of SEMCO's gas procurement practices create the potential for the disallowance of SEMCO's recovery, through its GCR rates, of some of its costs of purchasing gas. Such disallowances could affect SEMCO's liquidity and earnings.

SEMCO's earnings and cash flow are sensitive to decreases in customer consumption resulting from warmer than normal temperatures and customer conservation.

SEMCO's gas sales revenue is generated primarily through the sale and delivery of natural gas to residential and commercial customers who use natural gas mainly for space heating. Consequently, temperatures impact sales and revenues. Most of SEMCO's gas sales revenue is generated in the first and fourth quarters of the calendar year and SEMCO typically experiences losses in the non-heating season, which occurs in the second and third fiscal quarters of the year. In addition, conservation has resulted in reduced demand for natural gas from SEMCO's customers.

Variations in normal temperatures and conservation may adversely affect the earnings and cash flow of the gas distribution business. In SEMCO's Michigan service area, the temperature was approximately 5.4% warmer than normal in 2010 and 3.8% and 3.0% colder than normal during 2009 and 2008, respectively. The temperature was approximately 0.5% warmer than normal in the Alaska service area during 2010 and 2.8% and 10.5% colder than normal in the Alaska service area during 2009 and 2008, respectively.

In addition, the average annual natural gas consumption of customers has been decreasing because, among other things, new homes and appliances are typically more energy efficient than older homes and appliances, and customers appear to be continuing a pattern of conserving energy by utilizing energy efficient heating systems, insulation, alternative energy sources, and other energy savings devices and techniques. In addition, state-mandated or state-sponsored energy efficiency and conservation programs have been put in place in both Michigan and Alaska that encourage and fund some of these energy efficiency and conservation measures. This pattern of declining use per customer reduces SEMCO's non-gas revenues because a substantial portion of the base rate revenues are derived from volumetric distribution rates. Consequently, a mild winter, as well as continued or increased conservation, in any of SEMCO's service areas can have a significant adverse impact on demand for natural gas and, consequently, earnings and cash flow.

SEMCO's earnings are substantially dependent on its current customers maintaining a certain level of consumption as well as on customer growth.

During the past several years, average annual per customer gas consumption has been relatively stable. However, SEMCO has experienced decreased average annual per customer gas consumption in the past when natural gas prices were higher and it is reasonable to expect that, should natural gas prices rise significantly, SEMCO's customers may focus on greater energy conservation by utilizing efficient

heating systems, insulation, alternative energy sources and other energy saving devices and techniques, with a corresponding decrease in natural gas consumption. Significant declines in consumption by SEMCO's current customers, without an increase in the number of customers or adjustments to its rates or rate design, may negatively impact SEMCO's earnings.

In an RCA order issued in 2010 and in an MPSC order issued in January 2011, SEMCO's residential base rates were set using lower annual use per residential customer billing determinants that recognize that per customer residential consumption has been steadily declining. Continued and significant declines in consumption by SEMCO's customers, however, without adjustments to its rates or the way in which costs are collected from customers (or "rate design"), may adversely impact SEMCO's earnings.

In addition, SEMCO's earnings growth is substantially dependent on customer growth. Over the past 10 years, SEMCO's Michigan operations have experienced modest 0.7% compounded annual customer growth, while SEMCO's Alaska operations have experienced 2.5% compounded annual customer growth. If SEMCO is unable to achieve sufficient customer growth within its existing service territories or add additional customers by expanding service territories, SEMCO's earnings growth may be negatively impacted.

SEMCO's customers may be able to acquire natural gas without using SEMCO's distribution system, which would reduce revenues and earnings.

There is potential risk that Michigan industrial customers located in close proximity to interstate and intrastate natural gas pipelines will bypass SEMCO's transmission and distribution system and connect directly to such pipelines and thus have direct access to gas supplies provided by third parties. Such bypass efforts would reduce SEMCO's revenues and earnings. From time to time, customers raise the issue of bypass and SEMCO attempts to address their concerns. No assurances can be made that SEMCO's customers will not bypass SEMCO's distribution system or that SEMCO could successfully retain such customers.

Declining production from the Cook Inlet gas fields may result in potential deliverability problems in ENSTAR's service area.

ENSTAR's gas distribution system, including the APC pipeline system, is not linked to major interstate and intrastate pipelines or natural gas supplies in the lower 48 states of the United States or in Canada. As a result, ENSTAR procures natural gas supplies under long-term RCA-approved contracts from producers in and near the Cook Inlet area. Production from the Cook Inlet area gas fields is declining and new discoveries have been modest. As of December 2009 and based on a decline curve analysis, the Cook Inlet area had approximately 863 Bcf of total proved developed producing natural gas reserves remaining according to the most recently available information contained in the December 2009 Preliminary Engineering and Geological Evaluation of Remaining Cook Inlet Gas Reserves report of the Department of Natural Resources, Division of Oil and Gas and Division of Geological and Geophysical Surveys. Based on the Department's reported 2009 net production of 138 Bcf, there was a reserve life at January 1, 2010, of approximately 6.3 years in the Cook Inlet area, although shortages of daily deliverability have occurred resulting in curtailment of some industrial loads (which were not served by ENSTAR) during cold weather periods. There is ongoing exploration for natural gas in the Cook Inlet area, including producers that have supply contracts with ENSTAR. On June 28, 2011, the United States Geological Survey estimated that the Cook Inlet area contains an estimated mean of another approximately 19 Tcf of undiscovered, technically recoverable natural gas (reflecting the mean between 4.976 Tcf with 95% probability to 39.737 Tcf with 5% probability, respectively), but there are no assurances that any of this

natural gas will be discovered and, if discovered, can be produced economically and secured by ENSTAR on terms and conditions that would be acceptable to the RCA. While the completion of CINGSA is expected to mitigate deliverability constraints by regulating gas supply to match demand, there are no assurances that absent future discoveries and commercial production of natural gas, CINGSA alone will be sufficient to ensure future deliverability.

Activity also continues with respect to the possible construction of a natural gas pipeline that would extend from Alaska's North Slope, through central Alaska and Canada, to the lower 48 states of the United States. Assuming this pipeline and a spur line to the Anchorage area are built, the flow of natural gas through it could not be expected to begin before the middle of the next decade, at the earliest. There are no assurances, however, with respect to these gas supply-related matters, including when such pipelines might be constructed and put in service or whether natural gas supplies transported by such pipelines would be available to ENSTAR's customers and secured by ENSTAR on terms and conditions that would be acceptable to the RCA.

SEMCO's operations and business are subject to environmental laws and regulations that may increase SEMCO's cost of operations, impact or limit SEMCO's business plans or expose SEMCO to environmental liabilities.

SEMCO's operations and businesses are subject to laws and regulations that relate to the environment and health and safety, including those that impose liability for the costs of investigation and remediation of contamination resulting from, and for damages to natural resources due to, past spills, on- and off-site waste disposal and other releases of hazardous materials or regulated substances. In particular, under applicable environmental requirements, SEMCO may be responsible for the investigation and remediation of environmental conditions at currently owned or leased sites, as well as formerly owned, leased, operated or used sites. SEMCO may be subject to associated liabilities, including liabilities resulting from lawsuits alleging property damage or personal injury brought by private litigants related to the operation of SEMCO's facilities or the land on which such facilities are located, regardless of whether SEMCO leases or owns the facility, and regardless of whether such environmental conditions were created by SEMCO or by a prior owner or tenant, or by a third party or a neighbouring facility whose operations may have affected SEMCO's facility or land.

Prior to the construction of major interstate natural gas pipelines, gas for heating and other uses was manufactured from processes involving coal, coke or oil. Residual by-products of these processes may have caused environmental conditions that require investigation and remediation. SEMCO owns three sites in Michigan where such MGPs were located and recently disposed of four other properties where such MGPs were located. Even though SEMCO never operated MGPs at four of the sites, and did so at one site for only a brief period of time, SEMCO is subject to local, state and federal laws and regulations that require, among other things, the investigation and, if necessary, the remediation of contamination associated with these sites, irrespective of fault, legality of initial activity, or ownership, and which may impose liability for damage to natural resources. AltaGas understands that SEMCO has complied with the applicable MDEQ requirements, which require current landowners to mitigate unacceptable risks to human health from the by-products of MGP operations and to notify the MDEQ and adjacent property owners of potential contaminant migration, and is investigating these sites and anticipates conducting any necessary additional investigatory and remediation activities as appropriate. SEMCO has previously remediated and closed a site related to one of the MGP sites, with the MDEQ's approval.

SEMCO has conveyed four MGP sites to a prior owner of the sites, pursuant to a settlement entered into in July 2011. In 2008, SEMCO received approximately US\$1.9 million from an insurer in exchange for a

release of the insurer from liability for claims related to all of SEMCO's MGP sites. SEMCO is also attempting to identify other potentially responsible parties to bear some or all of the costs and liabilities associated with the investigatory and remediation activities at several of these sites and also is pursuing recovery of the costs of these activities from insurance carriers. SEMCO is unable to predict, however, whether and to what extent it will be successful in involving other potentially responsible parties in investigatory or remediation activities, or in bearing some or all of the costs thereof, or in securing insurance recoveries for some or all of the costs associated with these sites.

Given the nature of the past operations conducted by SEMCO and others at SEMCO's properties, particularly those involving former MGP sites, there can be no assurance that all potential instances of soil or groundwater contamination have been identified, even for those properties where environmental site assessments or other investigations have been or will be conducted. Changes in existing laws or policies or their enforcement, future spills or accidents or the discovery of currently unknown contamination may give rise to environmental liabilities which may be material.

SEMCO accrues for costs associated with environmental investigation and remediation obligations when such costs are probable and reasonably estimable. Accruals for estimated costs for environmental remediation obligations are generally recognized no later than the completion of SEMCO's RAP for a site. Such accruals are expected to be adjusted as further information becomes available or circumstances change. At three of the sites, SEMCO has begun efforts to determine the extent of remediation, if any, that must be performed, with the expectation of completing and submitting a RAP for each of the sites to the MDEQ. As a result of investigational work performed to date, SEMCO's Consolidated Statements of Financial Position include an accrual and a corresponding regulatory asset in the amount of US\$5.3 million at September 30, 2011, for estimated environmental investigation and remediation costs that it believes are probable at these three sites. SEMCO has not discounted this accrual to its present value. The accrued costs are expected to be paid out over the next few years.

The accrual of US\$5.3 million represents what SEMCO believes is probable and reasonably estimable. However, SEMCO also believes that it is reasonably possible that there could be up to an estimated US\$5.9 million of environmental investigation and remediation costs for these three sites, in addition to the US\$5.3 million already accrued. It is also reasonably possible that the amount accrued or the reasonably possible range of costs may change in the future as SEMCO's investigation of these sites continues and any remediation activities are undertaken. SEMCO's cost estimates have been developed using probabilistic modeling, advice from outside consultants, and judgment by management of SEMCO. The liabilities estimated by SEMCO are based on a current understanding of the costs of investigation and remediation. Actual costs, which may differ materially from these estimates, may vary depending on, among other factors, the environmental conditions at each site, the level of any remediation required, and changes in applicable environmental laws.

In accordance with an MPSC accounting order, the payment by SEMCO of environmental assessment and remediation costs associated with certain MGP sites are deferred and amortized over ten years. Rate recognition of the related amortization expense does not begin until the costs are subject to review in a base rate case. To the extent that any costs are not fully recoverable from customers through regulatory proceedings or from insurance or other potentially responsible parties, these costs would reduce SEMCO's earnings and results of operations.

Compliance with the requirements and terms and conditions of the environmental licenses, permits and other approvals that are required for the operation of SEMCO's business may cause SEMCO to incur substantial capital costs and operating expenses and may impose restrictions or limitations on the

operation of SEMCO's business, all of which could be substantial. Environmental, health and safety regulations may also require SEMCO to install pollution control equipment, modify its operations or perform other corrective actions at its facilities.

SEMCO's operations and business may be subject to future environmental laws and regulations that could increase SEMCO's cost of operations and impact or limit SEMCO's business.

SEMCO faces uncertainties related to future environmental laws and regulations affecting its business and operations. Existing environmental laws and regulations may be revised or interpreted more strictly, and new laws or regulations may be adopted or become applicable to SEMCO, which may result in increased compliance costs or additional operating restrictions, each of which could reduce SEMCO's earnings and adversely affect SEMCO's business, particularly if the related costs are not fully recoverable from customers through rates.

In particular, changes in laws and regulations relating to GHG emissions could require SEMCO, in addition to complying with GHG monitoring and reporting requirements applicable to its operations, to (i) comply with stricter emissions standards for internal combustion engines used to run compressors on SEMCO's natural gas transmission and distribution systems in Michigan and Alaska; (ii) take additional steps to control transmission and distribution system leaks; (iii) install new emission controls on SEMCO equipment or replace such equipment; and/or (iv) reduce SEMCO's GHG emissions or, depending on the requirements enacted, acquire emissions allowances or pay taxes on the GHGs emitted in connection with its operations. SEMCO's business could also be indirectly impacted by GHG laws and regulations that affect its customers or suppliers, to the extent such changes result in reductions in the use of natural gas by its customers or limit the operations of, or increase the costs of goods and services acquired from SEMCO suppliers, such as interstate pipelines and natural gas producers.

It is uncertain at the present time what form GHG laws or regulations may take if eventually enacted, and whether and in what ways SEMCO, customers, and others may be affected by any new requirements or obligations relating to GHG emissions. It is reasonably possible, however, that future legislative, regulatory or judicial actions could result in increased costs or changes in SEMCO's operations and/or could affect the demand for natural gas, which could reduce SEMCO's earnings and adversely impact SEMCO's business. While SEMCO may be able to include some or all of the costs associated with new or changed environmental laws and regulations in the rates charged to customers, SEMCO's ability to recover such costs is uncertain and may depend on events beyond its control, such as the outcome of future rate proceedings before the MPSC and RCA and the final provisions of any new legislation and regulations.

Substantial operational risks are involved in operating natural gas distribution, pipeline and storage system and propane distribution businesses, and such operational risks could adversely affect SEMCO's revenues, earnings, cash flow and financial condition.

There are substantial risks associated with the operation of natural gas distribution, pipeline and storage systems, and propane distribution businesses, such as operational hazards and unforeseen interruptions caused by events beyond SEMCO's control. These include adverse weather conditions, accidents, the breakdown or failure of equipment or processes, the performance of pipeline facilities below expected levels of capacity and efficiency, actions taken to interrupt service to portions of the gas transmission and distribution system to prevent more widespread outages, and catastrophic events such as explosions, fires, earthquakes, floods, landslides or other similar events beyond SEMCO's control. These risks could result in injury or loss of life, property damage, business interruption or environmental pollution, which in turn

could lead to substantial financial losses to SEMCO. In accordance with customary industry practice, SEMCO maintains insurance against some, but not all, of these risks. Liabilities incurred that are not fully covered by insurance could adversely affect SEMCO's earnings, cash flow and financial condition. Additionally, interruptions to the operation of SEMCO's gas distribution, pipeline or storage systems caused by such an event could reduce SEMCO's revenues, earnings and cash flow.

Earnings and cash flow may be adversely affected by downturns in the economy.

SEMCO's operations are affected by the condition and overall strength of the national, regional and local economies, which affect the amount of residential, industrial and commercial growth and gas consumption by SEMCO's customers. Many of SEMCO's commercial and industrial customers use natural gas in the production of their products. During economic downturns, these customers may see a decrease in demand for their products or services, which in turn may lead to a decrease in the amount of natural gas they require for production or operations. In addition, during periods of slow or little economic growth, customer energy conservation efforts often increase and the amount of uncollectible customer accounts and customer bankruptcies also often increase. The amount of uncollectible accounts also is affected by rules governing SEMCO's ability to shut off service for non-payment and the availability of private and public funds to assist customers in paying their bills for service. These and similar factors may reduce earnings and cash flow.

Recent U.S. health reform legislation could adversely affect SEMCO's operations and financial condition.

On March 23, 2010, President Obama signed into law the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act of 2010 (collectively, referred to as the "**Affordable Care Act**"). The Affordable Care Act makes widespread reform to the health care system, including substantial revision to the Medicare and Medicaid programs, establishment of individual mandates for healthcare coverage, incentives for employer-based insurance, formation of health insurance exchanges, changes in mandatory health benefit coverage, and taxes on certain device and drug manufacturers. Certain provisions of the Affordable Care Act took effect immediately while other provisions do not take effect until 2014 or later. Litigation has been initiated in various states to challenge the constitutionality of the Affordable Care Act, particularly the provisions relating to the individual insurance mandates and the expansion of coverage under the Medicaid program. The challenges are expected to be heard by the United States Supreme Court in 2012.

If all of the provisions of the Affordable Care Act are implemented in their current form, incremental costs may be incurred by SEMCO and, to the extent unable to be recovered in customer rates in each jurisdiction in which SEMCO does business, may adversely affect SEMCO's operations and financial condition.

The CINGSA Storage Project may be delayed and/or does not perform to design specifications.

The CINGSA Storage Project is currently under construction and the designed injection and withdrawal rates of 150 Mmcfd and 11 Bcf of working capacity have not yet been tested in operation and may not be achieved. The project is subject to normal construction and commissioning risk that the project may not be completed on the expected date. While the project has been designed and constructed by qualified and experienced gas storage professionals and the project has been extensively reviewed by project lenders, there are no assurances when put into service that the CINGSA Storage Project will perform to design rates and achieve storage capacity levels as anticipated.

AUDITORS, TRANSFER AGENT AND REGISTRAR

The auditors of AltaGas are Ernst & Young LLP, Chartered Accountants, 1000, 440 - 2nd Avenue S.W., Calgary, Alberta, T2P 5E9. Ernst & Young LLP is independent of AltaGas in accordance with the Rules of Professional Conduct as outlined by the Institute of Chartered Accountants of Alberta.

AltaGas' transfer agent and registrar is Computershare Investor Services Inc., 600, 530 - 8th Avenue S.W., Calgary, Alberta T2P 3S8.

LEGAL MATTERS

Certain legal matters in connection with the issuance of the Subscription Receipts will be passed upon on behalf of AltaGas by Stikeman Elliott LLP and on behalf of the Underwriters by Blake, Cassels & Graydon LLP. As at the date of this prospectus, the partners and associates of Stikeman Elliott LLP, as a group, and the partners and associates of Blake, Cassels & Graydon LLP, as a group, beneficially own, directly or indirectly, less than 1% of the outstanding Common Shares of AltaGas.

PURCHASERS' STATUTORY RIGHTS

Securities legislation in certain of the provinces of Canada provides purchasers with the right to withdraw from an agreement to purchase securities. This right may be exercised within two business days after receipt or deemed receipt of a prospectus and any amendment. In several of the provinces, the securities legislation further provides a purchaser with remedies for rescission or, in some jurisdictions, revision of the price or damages if the prospectus and any amendment thereto contains a misrepresentation or is not delivered to the purchaser, provided that the remedies for rescission, revision of the price or damages are exercised by the purchaser within the time limit prescribed by the securities legislation of the purchaser's province. The purchaser should refer to any applicable provisions of the securities legislation of the purchaser's province for the particulars of these rights or consult with a legal advisor.

CONSENT OF ERNST & YOUNG LLP

We have read the short form prospectus dated February 14, 2012 of AltaGas Ltd. (the “**Company**”) relating to the issuance of 12,100,000 subscription receipts (an additional 1,815,000 subscription receipts if the underwriters’ over-allotment option is exercised in full) (the “**Prospectus**”) of the Company. We have complied with Canadian generally accepted standards for an auditor’s involvement with offering documents.

We consent to the incorporation by reference in the Prospectus of our report to the shareholders of the Company on the amended consolidated balance sheets of the Company as at December 31, 2010 and 2009, and the amended consolidated statements of income, comprehensive income and accumulated other comprehensive (loss) income, shareholders’ equity and cash flows for each of the years in the two-year period ended December 31, 2010. Our report is dated February 22, 2011.

Calgary, Canada
February 14, 2012

(signed) “*Ernst & Young LLP*”
Chartered Accountants

CONSENT OF PRICEWATERHOUSECOOPERS LLP

We have read the short form prospectus of AltaGas Ltd. (“**AltaGas**”) dated February 14, 2012 relating to the issue and sale of 12,100,000 subscription receipts (13,915,000 subscription receipts if the underwriters’ over-allotment option is exercised in full) of AltaGas. We have complied with auditing standards generally accepted in the United States for an auditor’s involvement with offering documents.

We consent to the use in the above-mentioned prospectus of our report to the directors and shareholder of SEMCO Holding Corporation (“**SEMCO**”) on the consolidated statements of financial position and of capitalization of SEMCO at December 31, 2010 and 2009 and the related statements of operations, of changes in equity and comprehensive income and of cash flows for each of the years in the three-year period ended December 31, 2010. Our report is dated April 25, 2011 (except as to notes 12, 13 and 14 which are as of February 1, 2012).

Grand Rapids, Michigan
February 14, 2012

(signed) “*PricewaterhouseCoopers LLP*”

FINANCIAL STATEMENTS

SEMCO Holding Corporation

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SEMCO HOLDING CORPORATION

**Audited financial statement of SEMCO Holding Corporation as at and for the year ended
December 31, 2010 and December 31, 2009**

SEMCO Holding Corporation

Consolidated Financial Statements

As of December 31, 2010, and 2009,
and for the Years Ended December 31, 2010, 2009, and 2008

SEMCO Holding Corporation

Consolidated Financial Statements

As of December 31, 2010, and 2009,
and for the Years Ended December 31, 2010, 2009 and 2008

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All dollar amounts are denominated in U.S. currency.



Report of Independent Auditors

To the Board of Directors and Shareholder of

Semco Holding Corporation

In our opinion, the accompanying consolidated statements of financial position and the related consolidated statements of operations, of capitalization, of changes in equity and comprehensive income and of cash flows present fairly, in all material respects, the financial position of Semco Holding Corporation and its subsidiaries at December 31, 2010 and 2009, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2010 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

A handwritten signature in dark ink that reads "PricewaterhouseCoopers LLP". The signature is written in a cursive, flowing style.

April 25, 2011, except for Notes 12, 13 and 14, as to which the date is February 1, 2012

Semco Holding Corporation
CONSOLIDATED STATEMENTS OF OPERATIONS

	Year Ended December 31,		
	2010	2009	2008
	(in thousands)		
Operating revenues			
Gas sales	\$ 536,433	\$ 675,402	\$ 737,038
Gas transportation	24,175	23,657	24,184
Other	15,821	19,904	22,557
	<u>576,429</u>	<u>718,963</u>	<u>783,779</u>
Operating expenses			
Cost of gas sold	395,793	532,624	590,117
Operations and maintenance	80,136	93,753	97,389
Depreciation and amortization	32,350	31,565	30,889
Property and other taxes	11,905	11,112	10,363
	<u>520,184</u>	<u>669,054</u>	<u>728,758</u>
Operating income	<u>56,245</u>	<u>49,909</u>	<u>55,021</u>
Other income (deductions)			
Interest expense	(23,115)	(21,725)	(30,255)
Debt extinguishment costs	-	(160)	(609)
Other	3,087	2,648	2,950
	<u>(20,028)</u>	<u>(19,237)</u>	<u>(27,914)</u>
Income before income taxes	36,217	30,672	27,107
Income tax expense	<u>(15,022)</u>	<u>(10,302)</u>	<u>(15,814)</u>
Net income	21,195	20,370	11,293
Less: Income attributable to a non-controlling interest	57	-	-
Net income available to common shareholder	<u>\$ 21,138</u>	<u>\$ 20,370</u>	<u>\$ 11,293</u>

The accompanying notes to the consolidated financial statements are an integral part of these statements.

Semco Holding Corporation
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

	December 31,	
	2010	2009
	(in thousands)	
Current Assets		
Cash and cash equivalents	\$ 7,631	\$ 4,258
Restricted cash	441	441
Receivables, less allowances of \$1,370 and \$2,114	40,044	42,180
Accrued revenue	60,701	60,086
Gas in underground storage, at average cost	49,668	51,157
Prepaid expenses	7,213	7,489
Materials and supplies, at average cost	5,393	5,285
Deferred income taxes	4,151	5,519
Regulatory assets	410	1,238
Other	3,276	3,094
	<u>178,928</u>	<u>180,747</u>
Property, Plant and Equipment, Net	664,626	629,235
Deferred Charges and Other Assets		
Goodwill	204,472	204,472
Regulatory assets	73,533	53,133
Investment in unconsolidated affiliate	23,333	23,872
Unamortized debt expense	6,926	9,301
Other	8,148	13,662
	<u>316,412</u>	<u>304,440</u>
Total Assets	<u>\$ 1,159,966</u>	<u>\$ 1,114,422</u>
Current Liabilities		
Current maturities of long-term debt	\$ -	\$ 885
Notes payable	78,000	58,000
Accounts payable	70,794	67,302
Customer advance payments	31,408	30,071
Accrued interest	3,421	1,592
Regulatory liability - amounts payable to customers	2,304	9,171
Other	9,759	15,563
	<u>195,686</u>	<u>182,584</u>
Deferred Credits and Other Liabilities		
Deferred income taxes	52,401	33,341
Regulatory liabilities	69,638	64,775
Pension and other postretirement costs	35,122	40,479
Customer advances for construction	17,273	17,700
Other	19,852	18,334
	<u>194,286</u>	<u>174,629</u>
Commitments and Contingencies		
Capitalization		
Long-term debt	439,834	453,712
Equity		
Common shareholder's equity	325,915	303,497
Non-controlling interest in a consolidated subsidiary	4,245	-
Total equity	<u>330,160</u>	<u>303,497</u>
Total capitalization	<u>769,994</u>	<u>757,209</u>
Total Liabilities and Capitalization	<u>\$ 1,159,966</u>	<u>\$ 1,114,422</u>

The accompanying notes to the consolidated financial statements are an integral part of these statements.

Semco Holding Corporation
CONSOLIDATED STATEMENTS OF CASH FLOW

	Year Ended December 31,		
	2010	2009	2008
		(in thousands)	
Cash flow provided by (used for) operating activities			
Net income	\$ 21,195	\$ 20,370	\$ 11,293
Adjustments to reconcile net income to net cash provided by (used for) operating activities:			
Depreciation and amortization	32,350	31,565	30,889
Amortization of debt costs and debt basis adjustments included in interest expense	2,828	3,040	2,814
Deferred income tax expense	12,977	10,147	13,399
Debt extinguishment costs	-	-	609
Changes in operating assets and liabilities and other			
Receivables, net	2,136	18,693	(8,401)
Accrued revenue	(615)	36,522	(26,911)
Prepaid expenses	199	(762)	1,303
Materials, supplies and gas in underground storage	1,381	47,810	(24,605)
Regulatory asset - gas charges recoverable from customers	828	(1,238)	-
Regulatory liability - amounts payable to customers	(6,867)	(15,925)	7,510
Accounts payable	3,492	(20,139)	13,356
Accrued interest	1,829	(354)	(1,529)
Customer advances and amounts payable to customers	910	508	1,406
Other	(10,083)	(4,082)	10,783
Net cash provided by operating activities	<u>62,560</u>	<u>126,155</u>	<u>31,916</u>
Cash flows provided by (used for) investing activities			
Property additions	(63,617)	(36,670)	(38,999)
Property retirement costs, net of proceeds from property sales	291	134	(1,122)
Changes in restricted cash	-	3,580	(250)
Net cash used for investing activities	<u>(63,326)</u>	<u>(32,956)</u>	<u>(40,371)</u>
Cash flows provided by (used for) financing activities			
Issuance (repayment) of notes payable	20,000	(42,000)	35,000
Issuance of long-term debt, net of related expenses	295,757	114,847	-
Repayment of long-term debt	(314,820)	(154,584)	(28,936)
Contributions received from a non-controlling interest in a consolidated subsidiary	3,202	-	-
Payment of dividends on common stock	-	(13,000)	-
Net cash provided by (used for) financing activities	<u>4,139</u>	<u>(94,737)</u>	<u>6,064</u>
Cash and cash equivalents			
Net increase (decrease)	3,373	(1,538)	(2,391)
Beginning of period	4,258	5,796	8,187
End of period	<u>\$ 7,631</u>	<u>\$ 4,258</u>	<u>\$ 5,796</u>

The accompanying notes to the consolidated financial statements are an integral part of these statements.

Semco Holding Corporation
CONSOLIDATED STATEMENTS OF CAPITALIZATION

	December 31,	
	2010	2009
	(in thousands, except for number of shares and par value)	
Long-term debt		
5.15% senior notes due 2020	\$ 300,000	\$ -
SEMCO RBC Term Loan	45,000	345,000
SHC CES RBC Term Loan	90,000	104,820
7.03% senior notes due 2013	4,834	4,777
Long-Term debt including current maturities	\$ 439,834	\$ 454,597
Less current maturities	-	885
	<u>\$ 439,834</u>	<u>\$ 453,712</u>
Common shareholder's equity		
Common stock - par value \$.01 per share; 100 shares authorized; 10 shares outstanding	\$ -	\$ -
Capital surplus	277,220	277,220
Accumulated other comprehensive (loss)	(72)	(1,352)
Retained earnings (deficit)	48,767	27,629
	<u>\$ 325,915</u>	<u>\$ 303,497</u>
Non-controlling interest in a consolidated subsidiary	<u>\$ 4,245</u>	<u>\$ -</u>
Total capitalization	<u>\$ 769,994</u>	<u>\$ 757,209</u>

The accompanying notes to the consolidated financial statements are an integral part of these statements.

Semco Holding Corporation
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
AND COMPREHENSIVE INCOME

	Year Ended December 31,		
	2010	2009	2008
	(in thousands)		
Changes in Common Shareholder's Equity			
Shares of common stock			
Beginning of period	10	10	10
No activity during period	-	-	-
End of period	10	10	10
Common stock			
Beginning of period	\$ -	\$ -	\$ -
No activity during period	-	-	-
End of period	\$ -	\$ -	\$ -
Capital surplus			
Beginning of period	\$ 277,220	\$ 277,220	\$ 277,220
No activity during period	-	-	-
End of period	\$ 277,220	\$ 277,220	\$ 277,220
Accumulated other comprehensive income (loss)			
Beginning of period	\$ (1,352)	\$ (2,703)	\$ 33
Other comprehensive income (loss) adjustments:			
Valuation adjustment for marketable securities, net of income tax benefit (expense) of \$(49), \$(238), and \$202	80	356	(303)
Unrealized derivative gain (loss) on interest rate hedge, net of income tax benefit (expense) of \$(932), \$(1,012), and \$1,945	1,397	1,525	(2,922)
Annual funded status adjustment associated with benefit plans, net of income tax benefit (expense) of \$131, \$307 and \$(287)	(197)	(530)	489
End of period	\$ (72)	\$ (1,352)	\$ (2,703)
Retained earnings (deficit)			
Beginning of period	\$ 27,629	\$ 20,259	\$ 8,966
Net income available to common shareholder	21,138	20,370	11,293
Cash dividends on common stock	-	(13,000)	-
End of period	\$ 48,767	\$ 27,629	\$ 20,259
Non-controlling interest in a consolidated subsidiary			
Beginning of period	\$ -	\$ -	\$ -
Contributions received from a non-controlling interest	4,188	-	-
Income attributable to a non-controlling interest	57	-	-
End of period	\$ 4,245	\$ -	\$ -
Comprehensive Income			
Net income available to common shareholder	\$ 21,138	\$ 20,370	\$ 11,293
Valuation adjustment for marketable securities, net of income tax benefit (expense) of \$(49), \$(238), and \$202	80	356	(303)
Unrealized derivative gain (loss) on interest rate hedge, net of income tax benefit (expense) of \$(932), \$(1,012), and \$1,945	1,397	1,525	(2,922)
Annual funded status adjustment associated with benefit plans, net of income tax benefit (expense) of \$131, \$307 and \$(287)	(197)	(530)	489
Comprehensive income	\$ 22,418	\$ 21,721	\$ 8,557

The accompanying notes to the consolidated financial statements are an integral part of these statements

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Company Description and Significant Accounting Policies

Company Description. Semco Holding Corporation (“SHC”) is a Delaware corporation headquartered in Port Huron, Michigan. SHC was formed in February 2007. SHC is a wholly-owned subsidiary of Continental Energy Systems L.L.C. (“Continental”). Continental is a Delaware limited liability company headquartered in Troy, Michigan. Continental was formed in November 2005. Continental invests in regulated public utilities. In addition to owning SHC, Continental also owns New Mexico Gas Intermediate, Inc. (“NMGI”). NMGI owns New Mexico Gas Company, a regulated public utility providing gas utility service in New Mexico. Until July 2010, Continental owned CapRock Holding Corporation (“CRHC”). CRHC owned Cap Rock Energy Corporation (“CRE”). CRE was a regulated public utility providing electric utility service in Texas. Continental sold CRHC and CRE on July 13, 2010.

SHC owns SEMCO Energy, Inc. SEMCO Energy, Inc. (“SEMCO”) is a regulated public utility headquartered in Port Huron, Michigan. SEMCO’s primary business is the transmission, distribution, and sale of natural gas in Michigan and Alaska. References to “SHC” mean SHC or SHC and its direct and indirect subsidiaries, including SEMCO, as appropriate in the context of this disclosure. References to “SEMCO” mean SEMCO Energy, Inc. and its subsidiaries, or individual SEMCO subsidiaries, divisions or businesses, as appropriate in the context of the disclosure.

SEMCO’s gas distribution business transports and distributes natural gas to approximately 288,000 customers in Michigan and approximately 132,000 customers in Alaska. The Michigan operation is sometimes referred to as “SEMCO Gas” and the Alaska operation (including the activities of SEMCO’s Alaska Pipeline Company (“APC”) subsidiary) is sometimes referred to as “ENSTAR” or “ENSTAR Natural Gas Company.” These operations are known together as the “Gas Distribution Business.” The Gas Distribution Business is subject to regulation, as discussed in the “Rate Regulation” section below. The Gas Distribution Business accounted for approximately 99% of the SEMCO’s 2010 consolidated operating revenues.

SEMCO’s other businesses primarily include operations and investments in propane distribution, intrastate natural gas pipelines, and natural gas storage facilities. SEMCO’s propane distribution operation typically sells approximately 3 million gallons of propane annually to retail customers in Michigan’s Upper Peninsula and northeast Wisconsin. SEMCO’s pipeline and storage operations own and operate natural gas transmission and storage facilities, respectively, in Michigan. SEMCO is currently developing the Cook Inlet Natural Gas Storage Alaska, LLC (“CINGSA”) in-field storage facility in the Cook Inlet area of Alaska (the “CINGSA Storage Project”).

Basis of Presentation. The financial statements of SHC were prepared in conformity with accounting principles generally accepted in the United States (“US GAAP”). In connection with the preparation of these financial statements, management was required to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates.

Principles of Consolidation. The Consolidated Financial Statements include the accounts of SHC, SEMCO, and SEMCO’s wholly-owned subsidiaries and Alaska Storage Holding Company, LLC (“ASHC”), a subsidiary in which SEMCO has a controlling financial interest. At December 31, 2010, ASHC owned a 70% interest in CINGSA. For additional information about CINGSA, refer to Note 2 in this Annual Report. Investments in unconsolidated companies where SHC has significant influence over, but does not control the entity, are reported using the equity method of accounting.

Rate Regulation. The Gas Distribution Business is subject to regulation. The Michigan Public Service Commission (the “MPSC”) has jurisdiction over the regulatory matters related, directly or indirectly, to SEMCO Gas’s providing services to its Michigan customers. During 2010, SEMCO Gas’s Michigan customers were served under two sets of base rates, including terms and conditions of service, in what were referred to as the “MPSC Division” and “Battle Creek Division.” The MPSC Division consisted of a service territory located in southeastern Michigan, just northeast of the metropolitan Detroit area and in other areas throughout the state. The Battle Creek

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Division consisted of a service territory located in the City of Battle Creek and nearby communities. In January 2011, as part of the resolution of SEMCO Gas's base rate case, the MPSC authorized the combination of MPSC Division and Battle Creek Division rates and terms and conditions of service. This subsequent event is also discussed in Note 14. For additional information about SEMCO Gas's base rate case, refer to Note 2. The Regulatory Commission of Alaska (the "RCA") has jurisdiction over the regulatory matters related, directly or indirectly, to ENSTAR's providing service to its Alaska customers (including the activities of APC). The RCA also has jurisdiction over the regulatory matters related, directly or indirectly, to the CINGSA Storage Project. These regulatory agencies have jurisdiction over, among other things, rates, accounting procedures, and standards of service. The approximate number of customers located in service territories regulated by each of these regulatory agencies is as follows: MPSC — 288,000; and RCA — 132,000. The Gas Distribution Business is subject to current accounting guidance governing the accounting for regulatory matters. Refer to Note 2 for additional information about this accounting guidance.

Cash and Cash Equivalents. Cash and cash equivalents include cash on hand, money market funds and commercial paper. SHC considers all unrestricted highly liquid investments purchased with original maturities of three months or less to be cash equivalents. The carrying amount of cash equivalents approximates market value due to the short-term maturities of these investments.

Restricted Cash. At December 31, 2010, and 2009, SHC had \$0.4 million of restricted cash. Restricted cash consists of the portion of a supplemental retirement trust account expected to be distributed within one year.

Accounts Receivable. Trade accounts receivable are recorded at the billed amount and do not bear interest. The allowance for doubtful accounts is an estimate of the amount of probable credit losses in existing accounts receivable. Allowance for doubtful accounts is based primarily on the aging of receivables, though the historical write-off experience and regional economic data are also taken into consideration. The allowance for doubtful accounts is reviewed monthly. Account balances are charged off against the allowance when it is determined that it is probable that certain individual receivables will not be recovered. Uncollectible accounts, or bad debt expense, was \$1.4 million in 2010 and \$4.3 million in 2009 and in 2008.

Accrued Revenue. Accrued revenue represents revenue earned in the current period but not billed to customers until a future date, usually within one month.

Gas in Underground Storage. The gas inventory of the Gas Distribution Business is reported at average cost. In general, commodity costs and variable transportation costs are capitalized as gas in underground storage. Fixed costs, primarily pipeline demand charges and storage charges, are expensed as incurred through the cost of gas.

Property, Plant, Equipment and Depreciation. At December 31, 2010, SHC's gross property, plant and equipment were \$1,106.9 million and accumulated depreciation was \$442.3 million. At December 31, 2009, SHC's gross property, plant and equipment were \$1,050.9 million and accumulated depreciation was \$421.7 million.

Depreciation is recorded on a straight-line basis over the estimated useful lives of the related property. The lives over which significant classes of regulated and non-regulated depreciable property are depreciated are (in years):

<u>Regulated Property, Plant & Equipment</u>		<u>Non-Regulated Property, Plant & Equipment</u>	
Land	-	Buildings	40
Underground gas storage property	25 - 39	Intrastate gas pipelines	27
Gas transmission property	30 - 57	Propane storage tanks	30
Gas distribution property	18 - 58	Computer & telecommunications equipment	5 - 15
General property	7 - 38	Software	3
		General property	7 - 15

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The ratio of depreciation to the average balance of regulated property was approximately 3.0% for each of 2010, 2009 and 2008. The ratio of depreciation to the average balance of non-regulated property was approximately 4.8% for each of 2010 and 2009 and 5.6% for 2008.

Depreciation rates for regulated utility property are set, on an asset group basis, by the regulatory agencies that have jurisdiction over the property. The depreciation rates are intended to expense, over the expected life of the property, both the original cost of the property and the expected costs to remove or retire the property at the end of its useful life. The portion of depreciation expense related to expensing the original cost of the property is charged to accumulated depreciation. The portion related to the expected costs to remove or retire the property, less expected salvage proceeds, is charged to a regulatory liability. This regulatory liability is known in the utility industry as negative salvage value. When the regulated utility property is ultimately retired or otherwise disposed of in the ordinary course of business, the original cost of the property is charged to accumulated depreciation, and the actual removal costs, less salvage proceeds, are charged to the regulatory liability. With respect to the retirement or disposal of non-regulated property, the resulting gains or losses are recognized in income.

Asset Retirement Obligations. Asset retirement obligations are accounted for under applicable accounting guidance, which requires entities to record the fair value of the cost to remove assets at the end of their useful life, if there is a legal obligation to remove them. The term “conditional asset retirement obligation” used in applicable guidance refers to a legal obligation to perform an asset retirement activity in which the timing and/or method of settlement are conditional on a future event that may or may not be within the control of the entity. The obligation to perform the asset retirement activity is considered unconditional even though uncertainty exists about the timing and/or method of settlement. Accordingly, an entity is required to recognize a liability for the fair value of a conditional asset retirement obligation if the fair value of the liability can be reasonably estimated. The fair value of a liability for the conditional asset retirement obligation should be recognized when incurred. Applicable guidance also clarifies when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation.

SHC has identified certain assets for which asset retirement obligations must be recognized. At December 31, 2010, and December 31, 2009, SHC estimated that the cost of retiring these assets at the date of removal would be \$37.5 million and \$34.3 million, respectively. The present value of these obligations at December 31, 2010, and December 31, 2009, was \$7.2 million and \$5.8 million, respectively, and these amounts are recognized as a liability under the other deferred liabilities section in the Consolidated Statements of Financial Position.

Goodwill. Goodwill represents the excess of a purchase price over the value assigned to the net identifiable assets of businesses acquired. Goodwill is accounted-for under current accounting guidance. Under this accounting guidance, SHC is required to perform impairment tests on its goodwill annually or at any time when events occur which could impact the value of SHC’s goodwill. If an impairment test of goodwill shows that the carrying amount of the goodwill is in excess of the fair value, a corresponding impairment loss would be recorded in the Consolidated Statements of Operations.

The annual impairment tests were performed for SHC’s reporting units for the fiscal years 2010, 2009 and 2008. These tests indicated that there was no impairment of goodwill. There were no changes in the carrying amount of goodwill for the past two years:

	<u>Goodwill</u>
	(in thousands)
Balance as of December 31, 2009 and December 31, 2010	\$ 204,472

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Investment in Unconsolidated Affiliate. The equity method of accounting is used for interests where SHC has significant influence over, but does not control, an entity. SEMCO has a 50% ownership interest in Eaton Rapids Gas Storage System ("ERGSS") for which SHC accounts using the equity method of accounting.

Unamortized Debt Expense. SHC defers expenses incurred in connection with the issuance of debt and amortizes these deferred expenses over the term of the debt. If the underlying debt is retired or refinanced, any unamortized expenses are charged to expense in SHC's Consolidated Statements of Operations, except in situations where the debt is allocated to the Gas Distribution Business. In instances when debt allocated to the Gas Distribution Business is refinanced, any unamortized expenses may, in certain circumstances, be deferred as a regulatory asset and amortized over the term of the new debt.

Customer Advance Payments. SEMCO Gas and ENSTAR receive advance payments from customers who enroll in budget payment programs. These programs are intended to allow customers to pay their estimated annual gas bills in equal monthly payments. As a result, customers make advance payments during the non-heating season, when consumption and charges are generally low, and then utilize these advance payments to pay for a portion of their gas bills during the heating season, when consumption and bills for service are generally high. Customer advance payments also include deposits from customers to cover account credit risk.

Revenue Recognition. The Gas Distribution Business bills customers monthly, on a cycle basis, and follows the utility industry practice of recognizing accrued revenue for services rendered to its customers but not billed at month-end. Gas sales revenue is comprised of three components: (i) monthly customer service fees; (ii) volumetric distribution charges; and (iii) volumetric gas commodity charges. Monthly customer service fees represent fixed fees charged to customers. Distribution charges are charged to customers based on the volume of gas they consume. Gas commodity charges represent the cost of gas consumed by customers and are also based on the volume of gas customers consume. As discussed in more detail in the Cost of Gas section below, SHC does not earn any income on the gas commodity charge portion of rates charged to customers.

SHC's other businesses recognize revenues in the period that services are rendered or products are delivered to customers.

Cost of Gas, Gas Charges Recoverable from Customers, and Amounts Payable to Customers. The rates charged to SEMCO Gas customers include an MPSC-approved gas cost recovery ("GCR") pricing mechanism. ENSTAR has an RCA-approved gas cost adjustment ("GCA") pricing mechanism, which is similar to the GCR pricing mechanism used by SEMCO Gas in Michigan. Both of these pricing mechanisms (referred to together as "GCR pricing mechanisms") are designed so that, in the absence of any cost disallowances, the cost of gas purchased is passed through to SEMCO Gas and ENSTAR customers on a dollar-for-dollar basis and, therefore, no income or loss is recognized on the gas commodity charge portion of rates charged to customers.

The GCR pricing mechanisms allow for the adjustment of rates charged to customers for increases and decreases in the cost of gas purchased for resale to customers. For SEMCO Gas, the recovery of the cost of gas is subject to an MPSC review of its GCR gas purchase plans and actual gas purchases. A GCR gas purchase plan is filed annually with the MPSC by December 31 of each year for the upcoming April 1 to March 31 GCR period. A reconciliation case is filed by June 30 of each year to reconcile actual gas purchases during the previous April 1 to March 31 GCR period to the GCR gas purchase plan for the same period. Both the GCR gas purchase plan cases and reconciliation cases may involve reviews of SEMCO Gas's actions and decisions and potential cost disallowances or other adjustments. From time to time, parties in GCR cases propose disallowances and other adjustments, and those matters are litigated in the proceedings or resolved by settlement. SHC does not recognize potential gas cost disallowances or other adjustments until it determines that the disallowances or adjustments are probable. Disallowed costs and related adjustments are expensed in the cost of gas but are not recovered from customers in rates.

Under the GCR pricing mechanisms covering SEMCO Gas customers in Michigan, the gas commodity charge portion of rates charged to customers (which is also referred to as the "GCR rate"), may not exceed the maximum GCR rate established in the applicable MPSC-approved GCR plan for the 12-month GCR period in question without

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

MPSC approval. On a monthly basis, this GCR rate may be adjusted upward or downward but may not exceed the maximum GCR rate without MPSC approval. The maximum GCR rate may be adjusted upward if actual natural gas prices paid by SEMCO Gas for a specific period of time are significantly different than the prices set in the MPSC-approved GCR plans.

The GCR rate established by the RCA reflects the pricing mechanisms in various ENSTAR gas supply agreements and recovers the cost of natural gas purchased under those contracts, including appropriate prior period adjustments. Prior to 2011, ENSTAR's GCR rate was generally adjusted annually to reflect the estimated cost of gas purchased for the upcoming 12-month GCR period. Effective January 2011, however, ENSTAR's GCR rate is subject to revision quarterly, on a calendar quarter basis. Each quarter's GCR rate reflects the estimated cost of gas purchased for the upcoming 3-month GCR period and other appropriate rate components. This change in the GCR period for ENSTAR is also discussed in Note 14 as a subsequent event. These RCA proceedings may involve reviews of ENSTAR's actions and decisions and potential cost disallowances or other adjustments. From time to time, parties in these cases propose disallowances and other adjustments, and those matters are litigated in the proceedings or resolved by settlement. SHC does not recognize potential gas cost disallowances or other adjustments until it determines that the disallowances or adjustments are probable. Disallowed costs and related adjustments are expensed in the cost of gas but are not recovered from customers in rates.

Any difference between actual allowed cost of gas purchased and the estimate for a particular GCR period and not arising from a cost disallowance or adjustment is deferred as either an over- or under-recovery and typically included in customer GCR rates during the next GCR period. An over-recovery occurs when the actual amount billed for gas costs through the GCR rate exceeds the actual cost of gas purchased and is reflected in Amounts Payable to Customers in the current liabilities section of the Consolidated Statements of Financial Position. An under-recovery occurs when the actual cost of gas purchased exceeds the actual amount billed for gas costs through the GCR rate and is reflected in Gas Charges Recoverable from Customers in the current assets section of the Consolidated Statements of Financial Position. At December 31, 2010, SHC had \$2.3 million recorded in current liabilities for Amounts Payable to Customers and no amounts recorded in current assets for Gas Charges Recoverable from Customers, under various GCR pricing mechanisms.

Income Taxes. SHC uses the liability method in accounting for income taxes. Under the liability method, deferred income taxes are recognized, at currently-enacted income tax rates, to reflect the tax effect of temporary differences between the financial and tax basis of assets and liabilities. Such temporary differences are the result of provisions in the income tax law that either require or permit certain items to be reported on the income tax return in a different period than they are reported in the financial statements. SHC classifies deferred tax assets and liabilities into current and noncurrent amounts based on the classification of the related assets and liabilities.

SHC and its subsidiaries file a consolidated federal income tax return. The consolidated tax liability of SHC is allocated among its subsidiaries and divisions whose results are part of the consolidated federal income tax return based on their separate taxable income. For additional information about SHC's income taxes, refer to Note 3.

Recently-Adopted Accounting Guidance:

Controlling Financial Interest in a Variable Interest Entity. In June 2009, the Financial Accounting Standards Board (the "FASB") issued Statement of Financial Accounting Standards ("SFAS") No 167, *Amendments to FASB Interpretation 46(R)*. This accounting guidance clarifies how to determine whether an enterprise has a controlling financial interest in a variable interest entity. This guidance identifies the primary beneficiary of a variable interest entity as the enterprise that has both the power to direct the activities of a variable interest entity that most significantly impact the entity's economic performance and the obligation to absorb entity-related losses or the right to receive entity-related benefits that could potentially be significant to the variable interest entity. This guidance also requires ongoing assessments of whether an enterprise is the primary beneficiary of a variable interest entity and eliminates the quantitative approach previously required for determining the primary beneficiary. SHC adopted this guidance effective January 1, 2010, and its adoption did not have any impact on SHC's consolidated financial position, cash flow or results of operations.

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fair Value Measurement Disclosures. In January 2010, the FASB issued updated standards containing additional guidance regarding disclosures relating to fair value measurements. Refer to Note 8, Fair Value Measurements, in this Annual Report for a description of the three-tier fair value hierarchy discussed in the accounting guidance. That hierarchy prioritizes the inputs used to measure the fair value of an asset or liability. This updated accounting guidance requires an entity to (i) disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements from one period to the next and describe the reasons for the transfers, and (ii) present separate information about purchases, sales, issuances and settlements in the reconciliation of the beginning and ending balances of fair value measurements using Level 3 inputs. In addition, this guidance clarifies that entities must disclose the valuation techniques and inputs used to measure both recurring and non-recurring fair value measurements.

This guidance became effective for SHC on January 1, 2010, except for disclosures about purchases, sales, issuances and settlements in the reconciliation for fair value measurements using Level 3 inputs. The requirements related to Level 3 inputs are effective with the beginning of the first quarter of 2011. The adoption of this guidance by SHC did not, and is expected not to, have any impact on SHC's consolidated financial position, cash flow or results of operations.

Recently Issued Accounting Guidance Not Yet Adopted:

From time to time, new accounting guidance is issued by the FASB and, if applicable, adopted by SHC as of the specified effective date. Unless otherwise discussed in periodic disclosure documents, SHC believes that recently issued accounting guidance does not apply to SHC.

Statements of Cash Flow. For purposes of the Consolidated Statements of Cash Flow, SHC considers all highly liquid investments purchased with original maturities of three months or less to be cash and cash equivalents.

Additional supplemental cash flow information for the years ended December 31, 2010, 2009, and 2008, is summarized in the following table:

	Year Ended December 31,		
	2010	2009	2008
	(in thousands)		
Cash paid during the year for:			
Interest	\$ 18,482	\$ 18,998	\$ 22,580
Income taxes, net of refunds	\$ 1,000	\$ 1,739	\$ 1,450

Note 2. Regulatory Matters

Regulatory Matters Involving SEMCO Gas. SEMCO Gas is involved in various GCR proceedings before the MPSC, which are described in Note 1 under the caption, "Cost of Gas, Gas Charges Recoverable from Customers, and Amounts Payable to Customers." SEMCO Gas seeks to end its GCR period ending on March 31 of each year with no significant under-recovery or over-recovery of costs incurred to purchase gas for resale to customers. However, if actual gas prices near the end of the GCR period change significantly from prices in the GCR plan, a significant under-recovery or over-recovery could occur.

In October 2008, Public Act 286 of 2008 ("Act 286") and Public Act 295 of 2008 ("Act 295") were enacted by the Michigan legislature. Among other things, Act 295 requires gas and electric utilities (including SEMCO Gas) to establish energy optimization programs (each an "EO Plan") for their customers, to implement and fund various energy efficiency and conservation measures. EO Plans are subject to review and approval by the MPSC.

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In December 2008, SEMCO Gas notified the MPSC of its intent to meet the statutory requirements of Act 295 by using the Independent Energy Optimization Program Administrator (the "Independent Administrator") for the 2009, 2010 and 2011 EO Plan years. In May 2009, the MPSC issued an order approving a settlement agreement entered into in connection with SEMCO Gas's March 2009 EO Plan filing. Under the terms of the settlement, SEMCO Gas made payments to the Independent Administrator of \$4.8 million for 2010 and \$3.2 million for 2009. SEMCO Gas expects to make payments to the Independent Administrator of \$5.8 million for 2011. Those payments, which fund conservation- and energy efficiency-related measures and costs, are being recovered through surcharges imposed on all SEMCO Gas during the period from July 2009 through December 2011. In December 2009, the Independent Administrator implemented and began managing the EO Plan covering SEMCO Gas's customers. At December 31, 2010, SHC had \$0.4 million recorded in current assets for amounts recoverable from customers under the current EO Plan.

Among other things, Act 286 requires prior MPSC approval in connection with the acquisition, transfer of control, or merger of jurisdictional regulated utilities (including SEMCO), and in connection with certain sales, assignments, transfers or encumbrances of jurisdictional regulated utility assets. In accordance with Act 286, in January 2010, the MPSC issued an order defining what types of transactions are subject to Act 286 and thus require prior MPSC approval. Under Act 286, a transfer of control that requires prior approval is presumed to occur if, after the transfer, the transferee owns, controls or holds the right to vote 50% or more of the voting securities of the jurisdictional regulated utility; or after the transfer, the transferee owns, controls or holds the right to vote 20% or more of the voting securities if the transferee is, after the transfer, the largest holder of such securities. Certain financing transactions in the normal course of business and asset sales under a specific dollar threshold (currently \$10 million through 2020 for SEMCO) are excluded from the requirement that the MPSC approve the transactions in advance.

In October 2004, the MPSC initiated a proceeding involving all Michigan gas and electric utilities to review current accounting guidance for asset retirement obligations, Federal Energy Regulatory Commission Order No. 631, "Accounting, Financial Reporting, and Rate Filing Requirements for Asset Retirement Obligations," and related accounting and rate-setting issues. As directed by the MPSC, SEMCO Gas filed responses, in the form of testimony, to various questions raised by the MPSC regarding SEMCO Gas's accounting practices for property retirements, including the cost of removal. Among other things, this proceeding involved an examination of possible changes in accounting for property retirements, for rate-setting purposes. In August 2006, the Administrative Law Judge issued a Proposal for Decision that concluded, among other things, that current accounting guidance governing asset retirement obligations and FERC No. Order 631 be adopted for accounting purposes but not ratemaking purposes, and that the MPSC give due consideration to revising the traditional method of calculating removal costs. In June 2007, the MPSC issued an order that, among other things, found that there should be changes to the way it establishes the cost-of-removal portion of depreciation rates. The MPSC directed certain utilities to file new depreciation cases using the previous year's cost of removal expense as a basis for the filings and to calculate cost of removal depreciation under three different methods described in the order. As required, SEMCO Gas filed a depreciation study in February 2009, using 2007 data, and, in December 2009, the MPSC issued an order approving a settlement in the case. The settlement provided for a decrease depreciation expense of \$0.4 million for the MPSC Division and an increase of \$0.3 million for the Battle Creek Division, using the traditional method of determining removal costs. The new depreciation rates for the MPSC Division and Battle Creek Division were combined and implemented effective January 1, 2011.

In June 2010, SEMCO Gas filed a request with the MPSC seeking authority to increase SEMCO Gas's base rates by approximately \$19.8 million on a normalized annual basis. SEMCO Gas also proposed to combine its MPSC Division and Battle Creek Division so that, among other things, all of its Michigan customers would be served under one set of base rates and one GCR clause. In addition, SEMCO Gas proposed to change various aspects of its rate design, or the way in which the costs of providing service to customers are collected in base rates. SEMCO Gas asked the MPSC to approve, as a three-year pilot program, a single fixed monthly charge for both sales and transportation customers, except for lower-usage residential and commercial customers (who would continue to be billed using a traditional two-part rate design consisting of a fixed customer charge and a volumetric distribution charge). SEMCO Gas also proposed to recover the capital costs associated with the replacement of certain bare steel

Semco Holding Corporation
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mains and the operation and maintenance costs associated with replacing potentially defective service riser valves. Additionally, SEMCO Gas asked that it be allowed to recover from all customers the discounts provided to certain special contract transportation customers who might otherwise bypass SEMCO Gas's transmission and distribution system.

In late-December 2010, the MPSC issued an order authorizing SEMCO Gas to implement an interim and refundable base rate increase of \$8.1 million on a normalized annual basis for service rendered on or after January 1, 2011. Also in late-December 2010, the parties to the proceeding reached a settlement and filed it with the MPSC. Refer to Note 14, for information about the MPSC's approval of this settlement and additional settlement details.

Regulatory Matters Involving ENSTAR and CINGSA. In September 2009, ENSTAR finalized a gas supply agreement with Anchor Point Energy LLC ("APE") (the "APE Contract"), which provides for the purchase of approximately 10 billion cubic feet ("Bcf") of gas to be delivered over approximately eight years (with deliveries now expected to begin in April 2011). ENSTAR asked the RCA, among other things, to approve (i) the APE Contract, and (ii) the construction of a new approximately 20-mile pipeline that would be used to bring gas delivered under the APE Contract into ENSTAR's transmission and distribution system (the "APE Pipeline Project"). The RCA approved the APE Contract in November 2009. The RCA approved the APE Pipeline Project in April 2010. ENSTAR has now obtained all other required regulatory approvals to build the APE Pipeline Project, and construction of the APE Pipeline Project has begun and is expected to be completed in April 2011. Recovery of the investment in the APE Pipeline Project is provided-for in the ENSTAR base rate case settlement recently accepted by the RCA and discussed below. The estimated cost of completing the APE Pipeline Project is approximately \$21.6 million. Refer to Note 14 for information about the completion of the APE Pipeline Project.

Also in 2009, the RCA opened a docket to address ENSTAR's request, consistent with past RCA rulings, to recover through a surcharge approximately \$2.4 million in costs associated with negotiating recent gas supply agreements and submitting those agreements to the RCA for approval. Recovery of these costs is provided-for in the ENSTAR base rate case settlement recently accepted by the RCA and discussed below. At ENSTAR's request, this docket has now been closed.

ENSTAR and APC filed a base rate and rate design case with the RCA in June 2009. In that filing, ENSTAR and APC (which are generally regulated as a single entity by the RCA) sought an initial increase of \$15.4 million in base rate revenue on a normalized annual basis and an additional \$4.8 million increase in base rate revenue on a normalized annual basis to be effective when the APE Pipeline Project was placed in service. A settlement of this matter was negotiated among all of the parties and accepted by the RCA in August 2010. With the new base rates, ENSTAR's base rate revenue is expected to increase by \$7.0 million on a normalized annual basis. Thereafter, ENSTAR's base rate revenue is expected to increase by an additional \$3.8 million on a normalized annual basis when the APE Pipeline Project is completed and gas deliveries to ENSTAR's customers begin (now expected to be in April 2011). ENSTAR and APC are obligated under the settlement to submit another base rate and rate design filing to the RCA on or before August 1, 2014, based on a test year ended December 31, 2013.

In April 2010, ENSTAR finalized a gas supply agreement with Marathon Alaska Production LLC ("MAP") (the "MAP Contract"). The RCA approved the MAP Contract in May 2010. Deliveries under the MAP Contract are expected to supply approximately 90% of the estimated unmet gas supply needs of ENSTAR customers in 2011 and 2012. Gas delivered under the MAP Contract is priced using an average of New York Mercantile Exchange ("NYMEX") natural gas futures, adjusted quarterly, subject to floor and ceiling prices.

In August 2010, ENSTAR finalized a gas supply agreement for "as available" non-firm gas from ConocoPhillips Alaska, Inc. ("COP"), including a commitment by COP to divert gas intended for export from the liquefied natural gas ("LNG") export facility in Kenai, Alaska, for use instead by ENSTAR customers (the "COP Contract"). In October 2010, the RCA approved the COP Contract. Gas delivered under the COP Contract is priced at agreed-upon prices (up to oil parity levels) through the ENSTAR daily bidding system.

Because they will vary depending on the needs of ENSTAR customers, ENSTAR anticipates that, from time to time, the RCA may review the volumes purchased and prices paid under the COP Contract and "as available" non-

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

firm gas purchased under other gas supply agreements. The MAP Contract includes an agreement to supply such “as available” non-firm gas to ENSTAR customers and a commitment by MAP to divert gas intended for export from the LNG export facility for use instead by ENSTAR customers. “As available” non-firm gas delivered under the MAP Contract is priced at agreed-upon prices (up to oil parity levels) through the ENSTAR daily bidding system. In addition, ENSTAR also has “as available” non-firm gas supply arrangements under the gas supply agreement ENSTAR has with Union Oil of California (“Unocal”) (the “Unocal Contract”) and the APE Contract. Purchases of such non-firm gas are made through the ENSTAR daily bidding system.

Refer to Note 14, for information about the effect of the recent announcement by the owners of LNG export plant that they will likely cease exports by mid-2011 on ENSTAR’s contractual right to divert gas intended for liquefaction and eventual export for use by ENSTAR customers under the COP Contract and the MAP Contract.

In July 2010, SEMCO-CINGSA Storage Company (“SCSC”), a SEMCO subsidiary, and an affiliate of MidAmerican Energy Holdings Company (“MEHC”) entered into a joint venture agreement to invest in ASHC, the direct owner of CINGSA. CINGSA was formed to construct, own, and operate the CINGSA Storage Project. As designed, the CINGSA Storage Project would have initial capacity of 11 Bcf of gas and a maximum injection and withdrawal rate of 150 million cubic feet of gas per day. SCSC indirectly owns 70% of CINGSA; MEHC’s affiliate owns the remaining 30% of CINGSA. ENSTAR and three Cook Inlet area electric utilities are expected to be customers of the CINGSA Storage Project. ENSTAR has subscribed for approximately 75% of the CINGSA Storage Project’s initial capacity and approximately 65% of the associated initial gas injection and withdrawal capability, with the remainder of the capacity and injection and withdrawal capability split among the three other investment-grade customers.

In July 2010, CINGSA applied to the RCA for a certificate of public convenience and necessity for the proposed CINGSA Storage Project (a “Storage Certificate”). In December 2010, the RCA approved CINGSA’s Storage Certificate application in part, subject to certain conditions. Refer to Note 14, for additional information about the CINGSA Storage Certificate and related ENSTAR filings with the RCA.

The expected in-service date for the proposed CINGSA Storage Project is April 2012 for injections of gas into storage, with withdrawal capability available to customers of the CINGSA Storage Project in November 2012. It is also reasonably possible that the in-service date for the CINGSA Storage Project will not occur until 2013, delaying anticipated storage injections and withdrawals.

Regulatory Assets and Liabilities. The Gas Distribution Business is comprised of the activities of two regulated utilities and, therefore, SHC must follow accounting guidance that pertains specifically to entities subject to certain types of regulation. SHC refers to this accounting guidance for regulated entities as “regulatory accounting.” Under regulatory accounting, SHC is permitted to defer expenses and income as regulatory liabilities and assets, respectively, in the Consolidated Statements of Financial Position when it is probable that those expenses and income will be allowed in the rate-setting process in a period different from the period in which they would have been reflected in the Consolidated Statements of Operations by an unregulated entity. These deferred regulatory assets and liabilities are then included in the Consolidated Statements of Operations in the periods in which the same amounts are reflected in rates. Management’s assessment of the probability of recovery or pass-through of regulatory assets and liabilities requires judgment and interpretation of laws and regulatory agency orders, rules, and rate-making conventions. If, for any reason, SHC ceases to meet the criteria for application of regulatory accounting for all or part of its operations, the regulatory assets and liabilities related to those portions ceasing to meet such criteria would be eliminated from the Consolidated Statements of Financial Position and included in the Consolidated Statements of Operations for the period in which the discontinuance of regulatory accounting occurs. Such amounts would be classified as extraordinary items. Criteria that give rise to the discontinuance of regulatory accounting include (i) increasing competition that restricts the ability of a utility to charge prices sufficient to recover specific costs, and (ii) a significant change in the manner in which rates are set by regulatory agencies from cost-based regulation to another form of regulation. SHC’s review of these criteria currently supports the continued application of regulatory accounting for the regulated utilities comprising the Gas Distribution Business.

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table summarizes the regulatory assets and liabilities recorded in the Consolidated Statements of Financial Position, as well as the remaining period, as of December 31, 2010, over which the assets or liabilities are expected to be realized or settled:

	December 31,		
	2010	2009	Remaining Period
	(in thousands, except number of years)		
Regulatory assets			
Current			
Energy optimization costs recoverable from customers	\$ 410	\$ 1,238	1 year
Noncurrent			
Unamortized costs related to postretirement benefit plans	\$ 43,328	\$ 41,317	10 - 20 years
Deferred postretirement benefit expense	1,798	2,698	2 years
Deferred loss on reacquired debt	4,538	691	6 - 9 years
Deferred environmental costs	13,367	5,076	1 - 10 years
Other	10,502	3,351	3 - 15 years
	<u>\$ 73,533</u>	<u>\$ 53,133</u>	
Regulatory liabilities			
Current			
Amounts payable to customers (gas cost overrecovery)	\$ 2,304	\$ 9,171	1 year
Noncurrent			
Asset removal costs	\$ 68,158	\$ 64,465	10 - 40 years
Deferred tax benefits	-	310	
Insurance recovery of environmental costs	1,480	-	7 years
	<u>\$ 69,638</u>	<u>\$ 64,775</u>	

Note 3. Income Taxes

Current Accounting Guidance Governing Income Taxes. SHC accounts for income taxes in accordance with current accounting guidance. Current guidance requires an annual measurement of deferred tax assets and deferred tax liabilities based upon the estimated future tax effects of temporary differences and carry-forwards.

	Year Ended December 31,		
	2010	2009	2008
	(in thousands)		
Federal income tax expense:			
Current	\$ 125	\$ 33	\$ 218
Deferred to future periods	11,366	10,414	12,147
State income tax expense (benefit):			
Current	472	616	1,928
Deferred to future periods	3,059	(761)	1,521
Total income tax expense	<u>\$ 15,022</u>	<u>\$ 10,302</u>	<u>\$ 15,814</u>

Reconciliation of Statutory Rate to Effective Rate. The table below provides a reconciliation of the difference between SHC's provision for income taxes and income taxes computed at the statutory rate.

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	Year Ended December 31,		
	2010	2009	2008
		(in thousands)	
Net income (loss) from continuing operations	\$ 21,195	\$ 20,370	\$ 11,293
Add back: Income tax expense	15,022	10,302	15,814
Income attributable to a non-controlling interest	57	-	-
Pre-tax income	36,274	30,672	27,107
Computed federal income tax expense	12,696	10,735	9,487
State income tax expense, net of federal taxes	2,178	(95)	2,242
Nondeductible acquisition related expenses	-	(232)	4,677
Nondeductible termination agreement to sell subsidiary	-	-	-
Other	148	(106)	(592)
Total income tax expense	\$ 15,022	\$ 10,302	\$ 15,814

Deferred Income Taxes. Deferred income taxes arise from temporary differences between the tax basis of assets and liabilities and their reported amounts in SHC's financial statements. SHC also has an estimated net operating loss ("NOL") carry-forward for federal tax purposes of \$90.3 million at December 31, 2010, of which \$6.7 million expires in 2022, \$48.6 million expires in 2023, \$15.6 million expires in 2024, \$0.2 million expires in 2025, \$1.7 million expires in 2026, \$16.9 million expires in 2027, \$0.5 million expires in 2028 and \$0.1 million expires in 2029. SHC's ability to utilize its NOLs is limited by the Internal Revenue Code. SHC currently expects however, that it will realize enough taxable income in future years to utilize its NOLs prior to their expiration.

SHC accounts for uncertainty in income taxes recognized in an entity's financial statements in accordance with guidance governing accounting for income taxes. SHC had approximately \$0.9 million of gross unrecognized tax benefits associated with uncertain tax positions at both December 31, 2010, and December 31, 2009. It is SHC's policy to account for interest and penalties associated with uncertain income tax positions as a component of income tax expense. As of December 31, 2010, no amounts were accrued for interest or penalties associated with uncertain income tax positions.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The table below shows the principal components of SHC's deferred tax assets (liabilities).

	December 31,	
	2010	2009
	(in thousands)	
Property, plant and equipment	\$ (72,929)	\$ (70,491)
Retiree medical benefit regulatory assets	(512)	(827)
Reserve for uncollectible accounts	485	744
Accrued vacation	929	914
Property taxes	(1,469)	(1,421)
Goodwill	(7,893)	(5,385)
Deferred state income tax expense	1,902	2,525
Pensions and other postretirement plans	(1,246)	5,359
Gas in underground storage	(654)	(2,549)
Gas charge over-recovery	806	5,668
Net operating loss carryforward	31,594	35,970
AMT credit carryforward	3,847	3,520
Deferred Michigan business tax expense	(1,696)	(1,080)
Other	(1,414)	(769)
Total deferred taxes	<u>(48,250)</u>	<u>(27,822)</u>
Deferred tax liabilities	\$ (182,778)	\$ (170,342)
Deferred tax assets	134,528	142,520
Total deferred taxes	<u>\$ (48,250)</u>	<u>\$ (27,822)</u>

Note 4. Capitalization

Common Shareholder's Equity.

SHC is a direct wholly-owned subsidiary of Continental.

SHC's common shareholder's equity at December 31, 2010, and 2009, included other comprehensive income of \$1.3 million and \$1.4 million, respectively. The following table provides the components of the accumulated comprehensive income, at December 31, 2010, and 2009, net of income taxes:

	December 31,	
	2010	2009
	(in thousands)	
Funded status adjustment for certain pension plans	\$ (197)	\$ (530)
Unrecognized derivative gains	1,397	1,525
Unrecognized valuation gains on marketable securities	80	356
	<u>\$ 1,280</u>	<u>\$ 1,351</u>

Long-Term Debt. On January 30, 2009, Continental, along with its co-borrowers NMGI, SHC and CRHC, entered into a credit agreement with Royal Bank of Canada ("RBC"), as administrative agent, and a syndicate of lenders (the "CES RBC Credit Agreement"). The CES RBC Credit Agreement consists of a \$300 million secured term loan (the "CES RBC Term Loan") which was drawn at one time and has a maturity date of January 30, 2014. SHC was allocated \$118.0 million of the CES RBC Term loan ("SHC CES RBC Term Loan") and the SHC CES RBC Term Loan has \$90.0 million outstanding at December 31, 2010. The stock of several Continental subsidiaries is pledged as collateral under the CES RBC Credit Agreement.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The SHC CES RBC Term Loan may be incurred and maintained as, or converted into, Alternative Base Rate (“ABR”) loans or LIBOR loans. ABR loans bear interest at a rate per annum of 1.25% plus the higher of (i) prime lending rate announced from time to time by the administrative agent; (ii) the Federal Funds Effective Rate plus ½ of 1%; or (iii) the LIBOR rate for a one month interest period plus 1%. LIBOR loans bear interest at the rate per annum of 2.25% plus the relevant LIBOR rate (for interest periods of one, two, three or six months). Interest on ABR Loans is payable in arrears on the last business day of each March, June, September and December. Interest on LIBOR loans is payable on the last day of each interest period, except in the case of LIBOR loans with an interest period of six months on which interest is to be paid every three months.

SHC has the right to prepay the SHC CES RBC Term Loan, in whole or in part, without premium or penalty. Voluntary prepayments of the SHC CES RBC Term Loan may not be re-borrowed. SHC is also required to make mandatory prepayments of \$0.3 million on the SHC CES RBC Term Loan beginning with the quarter ending June 30, 2009, and each subsequent quarter thereafter until the maturity date. In addition, Continental is required to make mandatory prepayments on the CES RBC Term Loan: (i) if any capital stock is issued pursuant to an initial public offering an amount equal to 50% of the net cash proceeds thereof shall be applied to the CES RBC Term Loan; (ii) if certain indebtedness is incurred, then 100% of the net proceeds thereof must be applied as a prepayment of the CES RBC Term Loan; (iii) if Continental or a subsidiary receives net cash proceeds from any asset sale (as such term is defined by the CES RBC Credit Agreement), then, unless a reinvestment notice is delivered to RBC in respect thereof, 100% of the net cash proceeds thereof must be applied as a prepayment of the CES RBC Term Loan; or (iv) if Continental has any excess cash flow, as defined in the CES RBC Credit Agreement, then a percentage, as dictated by the CES RBC Credit Agreement, of those excess cash flows must be used to prepay the CES RBC Term Loan. Mandatory prepayments of the CES RBC Term Loan may not be re-borrowed. SHC made principal payments on the SHC CES RBC Term Loan in 2010 totaling \$15.7 million and thus satisfied all of its remaining quarterly payment obligations. As a result of these payments, the balance of the SHC CES RBC Term Loan was reduced from \$105.7 million at December 31, 2009, to \$90.0 million at December 31, 2010.

SEMCO also has a credit agreement with RBC, as administrative agent, and a syndicate of lenders (the “SEMCO RBC Credit Agreement”). The SEMCO RBC Credit Agreement consists of a \$130 million secured revolving credit facility (the “SEMCO RBC Revolver”) with a maturity date of November 9, 2012, and a \$345 million secured term loan (the “SEMCO RBC Term Loan”) maturing on November 9, 2014. In the second quarter of 2010, proceeds from the SEMCO’s issuance of its 5.15% Senior Secured Notes (the “Senior Notes”) (discussed below in this note), together with cash on hand, were used to repay \$300 million of the SEMCO RBC Term Loan, resulting in a SEMCO RBC Term Loan balance of \$45 million at December 31, 2010. For information about the RBC Revolver, refer to Note 5.

The SEMCO RBC Term Loan may be incurred and maintained as, or converted into, Alternative Base Rate loans (“SEMCO ABR Loans”) or LIBOR rate loans (“SEMCO LIBOR Loans”). As of December 31, 2010, SEMCO had elected to have the \$45 million of the SEMCO RBC Term Loan as a one-month SEMCO LIBOR Loan with a maturity date of December 31, 2010, and thereafter on a month-to-month basis. Interest on the SEMCO RBC Term Loan is payable at a variable rate and is calculated and paid in the same manner as prescribed for the SEMCO RBC Revolver. For information on how interest is calculated and paid on the SEMCO RBC Term Loan and the SEMCO RBC Revolver, refer to Note 5. SEMCO has the right to prepay the SEMCO RBC Term Loan, in whole or in part. Voluntary prepayments of the SEMCO RBC Term Loan may not be re-borrowed. If certain indebtedness is incurred by SEMCO, then 100% of the net proceeds therefrom must be applied as a prepayment of the SEMCO RBC Term Loan. In addition, if SEMCO or a subsidiary receives net cash proceeds from any asset sale (as such term is defined by the SEMCO RBC Credit Agreement), then, unless a reinvestment notice is delivered to RBC in respect thereof, 100% of the net cash proceeds therefrom must be applied as a prepayment of the SEMCO RBC Term Loan. Mandatory prepayments of the SEMCO RBC Term Loan may not be re-borrowed.

On April 21, 2010, SEMCO completed its issuance of the Senior Notes, in an aggregate principal amount of \$300 million. The Senior Notes were issued at a price of 99.930% and will mature at 100% of their principal amount on April 21, 2020. The Senior Notes have a coupon rate of 5.15%. SEMCO pays the interest on the Senior Notes on a semi-annual basis in arrears on April 21 and October 21 of each year, commencing on October 21, 2010.

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Senior Notes were issued in a private transaction that was not subject to the registration requirements of the Securities Act of 1933. The Senior Notes, the SEMCO RBC Term Loan and the SEMCO RBC Revolver are secured by certain assets of SEMCO. The SEMCO RBC Credit Agreement was amended to permit the issuance of the Senior Notes.

The net proceeds from the Senior Notes were approximately \$295.8 million, after deducting fees and expenses incurred in connection with amending the SEMCO RBC Credit Agreement and issuing the Senior Notes. SEMCO used the net proceeds from the Senior Notes, together with cash on hand, to repay \$300 million of the SEMCO RBC Term Loan and to pay related fees and expenses.

SEMCO's obligations under the Senior Notes are guaranteed on a senior basis by the SEMCO subsidiaries that are guarantors under the SEMCO RBC Credit Agreement. The Senior Notes rank equally and ratably in right of payment with all of the existing and future senior indebtedness of SEMCO and the guarantors (including debt incurred under the SEMCO RBC Credit Agreement). The indenture governing the Senior Notes contains covenants that, among other things, limit SEMCO's ability to create liens, transfer or sell assets, and consolidate, merge or sell substantially all of the SEMCO's assets.

In addition to the SEMCO RBC Term Loan and the Senior Notes, SEMCO had approximately \$5.0 million of other long-term debt outstanding at December 31, 2010, at fixed interest rates.

During 2009, SEMCO redeemed all \$30.0 million of its outstanding 6.49% Senior Notes due 2009 at par. These redemptions were funded from operating cash flows generated during 2009.

During 2008, SEMCO purchased the remaining balances of the 7 1/8% Notes due 2008 and its 7 3/4% Notes due 2013. In addition, SEMCO redeemed \$5.0 million of its 6.40% Senior Notes due 2008 and \$5.0 million of its 7.03% Senior Notes due 2013. These redemptions were funded from the operating cash flows generated during 2008.

At December 31, 2010, there were no annual sinking fund requirements for SHC's existing debt over the next five years. SHC has \$140.0 million of long-term debt maturing over the next five years as follows (in millions):

Maturities of long-term debt	At December 31, 2010	
	Face Amount	Carrying Amount
2011	\$ -	\$ -
2012	-	-
2013	5.0	4.8
2014	135.0	135.0
2015	-	-

Note 5. Short-Term Borrowings

As part of the SEMCO RBC Credit Agreement, SEMCO has \$130 million available to it under the SEMCO RBC Revolver with a maturity date of November 9, 2012. Borrowing under the SEMCO RBC Revolver may be used to refinance existing debt, meet working capital requirements and for general corporate purposes of SEMCO and its subsidiaries and to finance acquisitions permitted under the SEMCO RBC Credit Agreement. At December 31, 2010, SEMCO was utilizing approximately \$78.4 million of the borrowing capacity available under the SEMCO RBC Revolver, leaving approximately \$51.6 million of the borrowing capacity unused. The \$78.4 million of capacity being used consisted of \$78.0 million of borrowings and \$0.4 million of letters of credit. These amounts will change from time to time, reflecting SEMCO's then-current working capital needs and then-current gas supplier credit terms.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Under the terms of the SEMCO RBC Credit Agreement governing the SEMCO RBC Revolver, SEMCO may choose to obtain loans which are SEMCO LIBOR Loans or SEMCO ABR Loans. SEMCO LIBOR Loans bear interest at the LIBOR rate (for one week or a one, two, three or six month period, as elected by SEMCO) plus a margin which ranges from 1.00% to 1.25% and depends on the SEMCO's Ratio of Consolidated Total Debt to Consolidated Total Capitalization (as defined in the SEMCO RBC Credit Agreement). SEMCO's current margin, based on this ratio calculation, is 1.25%. SEMCO must provide three business days' notice to obtain SEMCO LIBOR Loans. SEMCO ABR Loans bear interest at a base rate, which is defined in the SEMCO RBC Credit Agreement as (i) the higher of the prime lending rate announced from time to time by the administrative agent or the Federal Funds Effective Rate, as defined in the SEMCO RBC Credit Agreement, plus 0.25%, plus (ii) a margin which ranges from 0% to 0.25%, also depending on SEMCO's Ratio of Consolidated Total Debt to Consolidated Total Capitalization (as defined in the SEMCO RBC Credit Agreement). SEMCO must provide one business day's notice to obtain SEMCO ABR Loans. Interest is payable on SEMCO LIBOR Loans on the last day of each interest period elected. Interest is payable on SEMCO ABR Loans on the last day of each March, June, September and December.

Under the terms of the SEMCO RBC Credit Agreement, the lenders have committed to provide letters of credit in an aggregate amount of up to \$40 million under the SEMCO RBC Revolver. A portion of the SEMCO RBC Revolver (in an amount not to exceed \$20 million) may be made available for same-day loan requests (the "Swingline Facility"). Interest is calculated on loans outstanding under the Swingline Facility in the same manner as it is calculated for SEMCO ABR Loans.

	Years ended December 31,		
	2010	2009	2008
	(in thousands)		
Notes payable balance at year end	\$ 78,000	\$ 58,000	\$ 100,000
Unused bank credit facilities at year end	\$ 51,600	\$ 71,200	\$ 29,800
Average interest rate at year end	1.7%	2.1%	1.8%
Weighted average interest rate	2.0%	1.8%	4.0%

Covenants in the SEMCO RBC Credit Agreement require that SEMCO not permit its consolidated interest coverage ratio for any test period ending at the end of any calendar quarter to be less than 2.25 to 1. In addition, SEMCO agreed not to permit the ratio of consolidated total debt to consolidated capitalization (as defined in the SEMCO RBC Credit Agreement) as of the last day of any fiscal quarter to be greater than 0.60 to 1. SEMCO's failure to comply with any of its financial covenants may result in an event of default which, if not cured or waived, could result in the acceleration of the debt under the SEMCO RBC Credit Agreement or the indentures governing its outstanding debt issuances that contain cross-acceleration or cross-default provisions. In such a case, there can be no assurance that SEMCO would be able to refinance or otherwise repay such indebtedness, which could result in a material adverse effect on SEMCO's business, results of operation, liquidity and financial condition.

Provisions of the SEMCO RBC Credit Agreement were amended in July 2010, to allow for a planned SEMCO investment in ASHC, which owns the CINGSA Storage Project. The SEMCO RBC Credit Agreement amendments: (i) allow SEMCO to incur additional indebtedness (including guarantees) of up to \$120 million to fund this joint venture; (ii) permit SEMCO to provide an unsecured guarantee for indemnity obligations relating to this joint venture of up to \$80 million; and (iii) permit an investment by SEMCO in this joint venture of up to \$160 million. For additional information about the CINGSA Storage Project, refer to Note 2.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 6. Financial Instruments

The following methods and assumptions were used to estimate the fair value of each significant class of financial instruments:

Cash, Cash Equivalents, Accounts Receivable, Accounts Payable and Notes Payable. The carrying amount approximates fair value because of the short maturity of those instruments.

Long-Term Debt. The fair values of SHC's long-term debt are estimated based on quoted market prices for the same or similar issues. The table below shows the estimated fair values of SHC's long-term debt, excluding current interest payable, as of December 31, 2010, and 2009:

	December 31,	
	2010	2009
	(in thousands)	
Long-term debt, including current maturities		
Carrying amount	\$ 439,834	\$ 454,597
Fair value	453,088	455,460

Note 7. Risk Management Activities and Derivative Transactions

The business activities of SHC and its direct and indirect subsidiaries expose SHC to a variety of risks, including commodity price risk and interest rate risks. Management identifies risks associated with SHC's business and determines which risks it wishes to manage with financial instruments and which types of instruments it should use to manage those risks.

SHC records all derivative instruments into which it enters based on current accounting guidance on this subject. The applicable guidance requires that every derivative instrument (including certain derivative instruments embedded in other contracts), except for those which qualify for the normal purchases and sales exception, be recorded in the statement of financial position, as either an asset or liability, measured at fair value. Derivative instruments that qualify for the purchase and sales exception are not recognized at fair value in the statement of financial position. The applicable accounting guidance also requires that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. Special accounting for qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the statement of operations, and requires that an entity must document, designate, and assess the effectiveness of transactions that receive hedge accounting. For derivatives designated as cash flow hedges, changes in fair value are recorded in other comprehensive income for the portion of the change in value of the derivative that is an effective hedge. Any ineffective portion of the change in fair value would be recorded as a gain or loss in the income statement.

SHC and SEMCO may, from time to time, enter into fixed-to-floating interest rate swaps in order to maintain the desired mix of fixed-rate and floating-rate debt. These swaps would be designated as fair value hedges under accounting guidance, and the difference between the amounts paid and received under these swaps would be recorded as an adjustment to interest expense over the term of the swap agreement. If the swaps were terminated, any unrealized gains or losses would be recognized pro-rata over the remaining term of the hedged item as an increase or decrease in interest expense.

SHC and SEMCO may also, from time to time, enter into floating-to-fixed interest rate swaps in order to maintain the desired mix of fixed-rate and floating-rate debt. These swaps would be designated as cash flow hedges under the applicable accounting guidance, and the difference between the amounts paid and received under these swaps would be recorded as an adjustment to interest expense over the term of the swap agreement. For cash flow hedges, the effective portion of gains and losses on derivative transactions would be reported as a component of

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

other comprehensive income. Gains and losses related to hedge ineffectiveness for outstanding derivatives would be computed on a quarterly basis and included in interest expense.

In January 2008, SEMCO entered into two floating-to-fixed interest rate swap agreements with a financial institution in order to hedge the variable component of the interest payments on a portion of the SEMCO RBC Term Loan. The first interest rate swap agreement hedged the variable component of the interest payments on \$100 million of the SEMCO RBC Term Loan for the period from February 15, 2008, through February 15, 2010 (the "February 2010 Swap"). The February 2010 Swap expired in accordance with its terms on February 15, 2010. The second interest rate swap agreement hedged the variable component of the interest payments on an additional \$100 million of the SEMCO RBC Term Loan for the period from February 15, 2008, through August 15, 2010 (the "August 2010 Swap"). The August 2010 Swap effectively converted the variable or floating interest rate on a portion of the SEMCO RBC Term Loan to a fixed interest rate and was being accounted-for as a cash flow hedge. On a quarterly basis, SEMCO paid the counterparty a fixed interest rate of 3.09% on the principal amount covered by the August 2010 Swap and received payments based on a floating interest rate based on LIBOR.

During the second quarter of 2010, SEMCO issued \$300 million in Senior Notes. Proceeds from this issuance, together with cash on hand, were used to repay \$300 million of the SEMCO RBC Term Loan. As a result of this repayment, the August 2010 Swap became ineffective to the extent that it no longer qualified for hedge accounting under the applicable accounting guidance. Consequently, SEMCO ceased hedge accounting for the August 2010 Swap effective April 21, 2010. The fair value of the August 2010 Swap at April 21, 2010, represented a loss of \$1.4 million. Based on accounting guidance, this amount was reclassified from other comprehensive income to earnings (interest expense) in the second quarter of 2010. After discontinuation of hedge accounting, the fair value of the August 2010 Swap was marked to market and the resulting adjustment was recorded in earnings. The August 2010 Swap expired in accordance with its terms on August 15, 2010.

See Note 4, in this report for information about SEMCO's RBC Term Loan and SEMCO's issuance of the Senior Notes in April 2010.

Note 8. Fair Value Measurements

Accounting guidance governing fair value measurements and disclosures provides that fair value represents the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that is determined based upon assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, accounting guidance also establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

- Level 1: Observable inputs, such as quoted prices in active markets;
- Level 2: Inputs, other than quoted prices in active markets, that are observable either directly or indirectly; and
- Level 3: Unobservable inputs for which there is little or no market data, requiring the reporting entity to develop its own assumptions.

Assets and liabilities measured at fair value are based on one or more of the following three valuation techniques noted under accounting guidance:

- (A) Market approach: Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities;
- (B) Cost approach: Amount that would be required to replace the service capacity of an asset (replacement cost); and
- (C) Income approach: Techniques to convert future amounts to a single present amount based upon market expectations (including present value techniques, option-pricing and excess earnings models).

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Financial assets measured at fair value as of December 31, 2010, are set forth in the table below:

Description	Frequency	Asset / (Liability)	Level 1 (In thousands)	Level 2	Level 3	Valuation Technique
Marketable Securities	Recurring	\$ 1,288	\$ 1,288	\$ -	\$ -	A

SEMCO's marketable securities represent deferred compensation payments invested in both equity and debt securities and held in two trusts. The fair values of these marketable securities are obtained from quoted market prices and are provided by the bank administering the trusts.

Note 9. Pension Plans and Other Postretirement Benefits

Pensions. SEMCO has defined-benefit pension plans for eligible employees ("Pension Plans"). Benefits under the Pension Plans are generally based upon years of service or a combination of years of service and compensation during the final years of employment. SEMCO's funding policy is to contribute amounts annually to fund the Pension Plans based upon actuarial and economic assumptions intended to achieve adequate funding of projected benefit obligations. SEMCO also has a Supplemental Executive Retirement Plan, or SERP, which is an unfunded defined-benefit pension plan. Effective in March 2008, the SERP was closed to additional participants and SERP benefit accruals for participants ceased.

In 2010, 2009 and 2008, SEMCO expensed pension costs of \$6.3 million, \$7.7 million and \$3.6 million, respectively. The pension expense for 2010, 2009 and 2008 includes \$1.7 million, \$1.7 million and \$1.8 million, respectively, for the amortization of regulatory assets related to pension costs. The pension expense for 2008 also includes a curtailment gain of \$0.5 million due to the closing of the SERP to new participants and the end to SERP accruals.

SEMCO contributed \$9.1 million to fund its Pension Plans during 2010. SEMCO estimates it will contribute approximately \$6.0 million to fund its Pension Plans in 2011.

Other Postretirement Benefits. SEMCO has postretirement benefit plans ("Postretirement Plans") that provide certain medical and prescription drug benefits to eligible retired employees, their spouses and covered dependents. Benefits are based on a combination of the retiree's age and years of service at retirement. SEMCO accounts for retiree medical benefits in accordance with current accounting guidance. This guidance requires the full accrual of such costs during the years that the employee renders service until the date of full eligibility.

In 2010, 2009 and 2008, SEMCO expensed retiree medical costs of \$1.7 million, \$2.4 million and \$1.8 million, respectively. Retiree medical expense for 2010, 2009 and 2008 includes \$1.3 million, \$1.3 million, \$1.3 million, respectively, for the amortization of regulatory assets related to retiree medical costs.

SEMCO contributed \$1.5 million to fund its Postretirement Plans or to cover retiree medical costs during 2010. SEMCO estimates it will make contributions of \$1.4 million to fund its Postretirement Plans or to cover retiree medical costs in 2011.

The Patient Protection and Affordable Care Act and the related Health Care and Education Reconciliation Act (the "Health Care Acts") were enacted in March 2010. For tax years beginning after December 31, 2012, the Health Care Acts repeal the tax deduction for the portion of health care costs that are reimbursed by the Medicare Part D subsidy. To reflect this change in the law, SEMCO decreased its deferred tax asset balance by \$4.8 million and increased its regulatory assets by \$4.8 million, as the rate-setting process generally allows for the SEMCO's recovery of income tax expense (which was effectively increased by the repeal of this tax deduction in the Health

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Care Acts). As a result, the Health Care Acts had no effect on the net income of SHC or SEMCO for the year ended December 31, 2010.

SEMCO uses a measurement date of December 31 for the Pension Plans and Postretirement Plans. The following tables provide information about the Pension Plans and Postretirement Plans:

Pension Benefits

	<u>2010</u>	<u>2009</u>	<u>2008</u>
		(in thousands)	
Components of net periodic benefit cost			
Service cost	\$ 3,788	\$ 3,288	\$ 3,082
Interest cost	6,703	6,580	6,074
Expected return on plan assets	(6,948)	(5,299)	(6,799)
Curtailment gain	-	-	(490)
Amortization of net loss	1,046	1,505	-
Amortization of regulatory asset	1,668	1,668	1,752
Net periodic benefit cost	<u>\$ 6,257</u>	<u>\$ 7,742</u>	<u>\$ 3,619</u>

Other Postretirement Benefits

	<u>2010</u>	<u>2009</u>	<u>2008</u>
		(in thousands)	
Components of net periodic benefit cost			
Service cost	\$ 717	\$ 637	\$ 654
Interest cost	2,241	2,325	2,403
Expected return on plan assets	(2,544)	(2,058)	(2,604)
Amortization of net (gain) or loss	(31)	83	(13)
Early retirement capped rights	-	151	-
Amortization of regulatory asset	1,311	1,311	1,331
Net periodic benefit cost	<u>\$ 1,694</u>	<u>\$ 2,449</u>	<u>\$ 1,771</u>

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	Pension Benefits		Other Postretirement Benefits	
	December 31,		December 31,	
	2010	2009	2010	2009
	(in thousands)			
Projected benefit obligation (PBO) / Accumulated postretirement benefit obligation (APBO) at current measurement date	\$ 129,598	\$ 118,370	\$ 41,430	\$ 38,735
Less: Fair value of assets at current measurement date	<u>100,599</u>	<u>84,934</u>	<u>36,234</u>	<u>31,954</u>
Funded status	\$ (28,999)	\$ (33,436)	\$ (5,196)	\$ (6,781)
Accumulated benefit obligation for pension benefit plans	\$ 115,596	\$ 104,606	N/A	N/A
Contributions and benefits paid				
Company contributions	9,077	8,096	1,537	1,715
Benefits paid	(4,878)	(3,616)	(1,492)	(1,290)
Items not yet recognized as a component of net periodic benefit costs				
Net transition obligation	\$ -	\$ -	\$ -	\$ -
Net prior service cost (credit)	227	-	-	-
Net loss (gain)	<u>23,100</u>	<u>23,275</u>	<u>(480)</u>	<u>(49)</u>
	\$ 23,327	\$ 23,275	\$ (480)	\$ (49)
The above amounts are reflected in the consolidated statements of financial position as follows:				
Regulatory assets / liabilities	\$ 23,077	\$ 23,354	\$ (480)	\$ (49)
Accumulated comprehensive income	<u>250</u>	<u>(79)</u>	<u>-</u>	<u>-</u>
	\$ 23,327	\$ 23,275	\$ (480)	\$ (49)

The estimated net loss and prior service cost for the defined-benefit pension plans that will be amortized into net periodic benefit cost in 2011 from regulatory assets and/or liabilities is \$1.0 million. The estimated net loss and prior service cost for the other postretirement benefit plans that will be amortized into net periodic benefit cost in 2011 from the regulatory assets and/or liabilities is zero. There are no net loss or prior service costs for either the defined-benefit pension plans or the other postretirement benefit plans that are estimated to be amortized into net periodic benefit cost in 2011 from accumulated comprehensive income.

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NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Assumptions. The following tables provide the assumptions used to determine the benefit obligations and the net periodic benefit costs for Pension Plans and Postretirement Plans for 2010 and 2009:

	Pension Benefits		Other Postretirement Benefits	
	2010	2009	2010	2009
	(in thousands, except for percentages)			
Assumptions and dates used at disclosure				
Discount rate	5.60% (1)	5.90% (2)	5.60%	5.90%
Compensation increase rate	4.00%	4.00%	N/A	N/A
Current year trend - medical	N/A	N/A	8.20%	8.60%
Ultimate year trend	N/A	N/A	5.00%	5.00%
Year of Ultimate trend rate	N/A	N/A	2019	2019
Measurement date	12/31/2010	12/31/2009	12/31/2010	12/31/2009
Census date	1/01/2010	1/01/2009	1/01/2010	1/01/2009
Assumptions used to determine expense				
Discount rate	5.90% (2)	6.50% (3)	5.90%	6.50%
Long-term rate of return on assets	8.00%	8.00%	8.00%	8.00%
Compensation increase rate	4.00%	4.00%	N/A	N/A
Current year trend - medical	N/A	N/A	8.60%	9.00%
Ultimate year trend	N/A	N/A	5.00%	5.00%
Year of Ultimate trend rate	N/A	N/A	2019	2019

(1) 2010 Discount rate for the SERP was 4.3%. All other plans assumed a 5.6% discount rate.

(2) 2009 Discount rate for the SERP was 4.90%. All other plans assumed a 5.90% discount rate.

(3) 2009 Discount rate for the SERP was 7.00%. All other plans assumed a 6.50% discount rate.

The discount rate used is determined by reference to the Towers Watson U.S. Rate: Link Yield Curve, other long-term corporate bond measures and the expected cash flows of the plans. The duration of the securities underlying those indexes reasonably matches the expected timing of anticipated future benefit payments.

The expected long-term rate of return on plan assets is established based on expectations of asset returns for the investment mix in its plans (with some reliance on historical asset returns for the plans). The expected returns of various asset categories are blended to derive an appropriate long-term assumption.

Plan Assets. The weighted-average asset allocations of the Pension Plans and Postretirement Plans at December 31, 2010, and 2009, are presented in the following table:

December 31,	Percentage Allocation			
	Pension Benefits		Other Postretirement Benefits	
	2010	2009	2010	2009
Asset Category				
Equity securities	66.9%	67.9%	67.1%	67.8%
Debt securities	32.8%	31.8%	32.9%	32.1%
Other	0.3%	0.3%	0.0%	0.1%
Total	100.0%	100.0%	100.0%	100.0%

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SEMCO has a target asset allocation of 67% equities and 33% debt instruments for funding its Pension Plans and Postretirement Plans. Year-end pension contributions and cash held for retiree pension payments also impact the actual asset allocation compared to the target asset allocation.

The primary goal of the funding approach is to ensure that pension and other postretirement liabilities are met. Emphasis is placed on the long-term characteristics of individual asset classes and the benefits of diversification across multiple asset classes. The approach incorporates an assessment of the proper long-term level of risk for the plans, considering factors such as the long-term nature of the related liabilities, the current funded status of the plans, and the impact of asset allocation on the volatility and magnitude of contributions and expense.

The table below provides the fair values of pension and post retirement benefits trust plan assets as of December 31, 2010. The table also identifies the level of inputs used to determine the fair value of assets in each category (see Note 8 for the definition of these levels). All of the plan assets are identified as Level 1 inputs as the fair market values are based on the quoted market prices or are cash equivalents which are equal to fair market value.

Description	Level 1	Level 2	Level 3	Total
		(in thousands)		
Domestic equities	\$ 76,047	\$ -	\$ -	\$ 76,047
International equities	15,622	-	-	15,622
Fixed income securities	44,909	-	-	44,909
Cash & cash equivalents (a)	256	-	-	256
Total	\$ 136,834	\$ -	\$ -	\$ 136,834

(a) Cash and cash equivalents are predominantly held in money market funds.

At December 31, 2010, the fair value of the plan assets of \$136.8 million in the table above consisted of \$100.6 million in assets for pension benefits and \$36.2 million in assets for postretirement benefits.

Estimated Future Benefit Payments. The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

	Pension Benefits	Other Postretirement Benefits		
		Gross Benefits	Less Medicare Part D Subsidy	Net Benefits
		(in thousands)		
2011	\$ 4,695	\$ 1,786	\$ 197	\$ 1,589
2012	5,846	1,862	220	1,642
2013	5,796	1,943	246	1,697
2014	6,467	2,050	271	1,779
2015	6,180	2,229	288	1,941
Years 2016 - 2020	38,822	13,458	1,780	11,678

401(k) Plans and Profit-Sharing Plans. SEMCO has defined contribution plans, commonly referred to as 401(k) plans, covering eligible employees. Certain of the 401(k) plans contain provisions for SEMCO matching contributions. The amount expensed for SEMCO matching contributions was \$1.6 million for each of the years 2010, 2009 and 2008.

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SEMCO also has profit-sharing plans covering ENSTAR union-represented employees. Annual contributions are generally discretionary or determined by a formula, which includes minimum contribution requirements. Profit-sharing expense was \$0.2 million for each of the years 2010, 2009 and 2008.

Note 10. Transactions with Related Parties

Management services are provided to SEMCO by the same company that manages the group of investment funds that together are the majority owner of Continental. Fees for these services amounted to \$1.2 million for the years 2010, 2009 and 2008. These fees are included in Operations and Maintenance expense in the Consolidated Statements of Operations.

ERGSS provides natural gas storage services to SEMCO Gas. The cost of these services was \$3.5 million for each of the years 2010 and 2009, and \$3.1 million for 2008. These costs are included in cost of gas sold in the Consolidated Statements of Operations.

SHC had receivables from affiliates of \$0.1 million and \$0.6 million as of December 31, 2010, and December 31, 2009, respectively. These receivables are included in Other Current Assets in the Consolidated Statements of Financial Position.

Note 11. Commitments and Contingencies

Lease Commitments. SEMCO leases buildings, vehicles and equipment. These leases are classified as operating leases in accordance with the applicable accounting guidance. A significant portion of the SEMCO's vehicles are leased. Leases on the majority of SEMCO's new vehicles are for a minimum of twelve months. SEMCO has the right to extend each vehicle lease annually and to cancel an extended lease at any time.

SEMCO's future minimum lease payments that have initial or remaining non-cancelable lease terms in excess of one year at December 31, 2010, totaled \$11.8 million consisting of (in millions):

2011	\$	2.2
2012	\$	1.8
2013	\$	1.8
2014	\$	1.7
2015	\$	1.7
Thereafter	\$	2.6

Total lease payments were approximately \$3.5 million, \$3.3 million and \$3.1 million in 2010, 2009 and 2008, respectively. The annual future minimum lease payments are less than the lease payments incurred in 2008 through 2010, because most of the vehicle leases at December 31, 2010, were on a month-to-month basis and therefore were subject to cancellation at any time. However, management expects to renew or replace substantially all of these leases.

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Commitments for Natural Gas Supplies, Transmission and Storage. SEMCO enters into contracts to purchase natural gas and natural gas transportation and storage services from various suppliers for its Gas Distribution Business. These contracts, which have expiration dates that range from 2011 to 2019, are used to assure that there is an adequate supply of natural gas to meet the needs of customers of SEMCO Gas and ENSTAR and to minimize exposure to market price fluctuations. SEMCO's estimated gas purchase contractual obligations as of December 31, 2010, total \$223.5 million, consisting of (in millions):

2011	\$	86.3
2012	\$	43.8
2013	\$	29.7
2014	\$	20.9
2015	\$	11.3
Thereafter	\$	31.5

Guarantees. SEMCO has issued letters of credit through financial institutions for the benefit of third parties that have extended credit or have financial exposure to SEMCO. At December 31, 2010, the outstanding letters of credit amounted to \$0.4 million. Under the terms of these letters of credit, if SEMCO does not pay amounts when due under the covered contracts, the beneficiary of the letter of credit may present its claim for payment to the financial institution, which will, in turn, request payment from SEMCO. If SEMCO does not make the requested payment, the financial institution will make the payment, effectively guaranteeing SEMCO's payment. The letters of credit are entered into on a short-term basis, normally every six-to-twelve months, and are then renewed for another short-term period. At December 31, 2010, the scheduled expiration dates for these letters of credit range from March 1, 2011 to November 9, 2011.

Environmental Issues. Prior to the construction of major interstate natural gas pipelines, gas for heating and other uses was manufactured from processes involving coal, coke or oil. Residual byproducts of these processes may have caused environmental conditions that require investigation and remediation. SEMCO owns seven sites in Michigan where such manufactured gas plants ("MGP") were formerly located. Even though SEMCO never operated MGP facilities at four of the sites, and did so at a fifth site for only a brief period of time, SEMCO is subject to federal, state and local laws and regulations that require, among other things, the investigation and, if necessary, the remediation of contamination associated with these sites, irrespective of fault, legality of initial activity, or ownership, and which may impose liability for damage to natural resources. SEMCO has complied with the applicable Michigan Department of Environmental Quality ("MDEQ") requirements, which require current landowners to mitigate unacceptable risks to human health from the byproducts of MGP operations and to notify the MDEQ and adjacent property owners of potential contaminant migration. SEMCO is currently investigating these sites and anticipates conducting any necessary additional investigatory and remediation activities as appropriate. SEMCO has already investigated, remediated and closed a site related to one of the seven MGP sites, with the MDEQ's approval.

In connection with these investigatory and remediation activities SEMCO has attempted to identify other potentially responsible parties to bear some or all of the costs and liabilities associated with those activities at several of these sites. SEMCO also is pursuing recovery of the costs of these activities from insurance carriers. In 2008, SEMCO received approximately \$1.9 million from an insurer in exchange for a release of the insurer from liability for claims related to all of SEMCO's MGP sites. In accordance with an MPSC accounting order, the payment was initially recorded as a deferred asset. That payment was subsequently reclassified as a deferred liability as a result of the recent SEMCO Gas base rate case settlement. The payment under the settlement will continue to be amortized over ten years. For additional information about the SEMCO Gas base rate case settlement, refer to Notes 2 and 14. SEMCO is continuing to pursue the recovery of investigatory and remediation costs from another insurer. SEMCO is unable to predict, however, whether and to what extent it will be successful in involving other potentially responsible parties in MGP-related investigatory or remediation activities, or in bearing some or all of the costs and liabilities thereof, or in securing additional insurance recoveries for costs and liabilities associated with these sites.

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SEMCO accrues for costs associated with environmental investigation and remediation obligations when such costs are probable and reasonably estimable. Accruals for estimated costs for environmental remediation obligations are generally recognized no later than the completion of a Remedial Action Plan ("RAP") for a site. Such accruals are adjusted as further information becomes available or circumstances change. At three of the MGP sites, SEMCO has begun efforts to determine the extent of remediation, if any, that must be performed, with the expectation of completing and submitting a RAP for each of the sites to the MDEQ. From time to time, however, pre-RAP remediation activities are undertaken during the investigatory process. As a result of investigational work performed to date, SHC's Consolidated Statements of Financial Position include an accrual and a corresponding regulatory asset in the amount of \$5.3 million at December 31, 2010, for estimated environmental investigation and remediation costs that SHC believes are probable at these three sites. SHC has not discounted this accrual to its present value. The accrued costs are expected to be paid out over the next three years.

The accrual of \$5.3 million represents what SHC believes is probable and reasonably estimable. However, SHC also believes that it is reasonably possible that there could be up to an additional \$5.9 million of environmental investigation and remediation costs for these three sites. It is also reasonably possible that the amount accrued or the estimated range of costs may change in the future as SEMCO's investigation of these sites continues and any remediation activities are undertaken. These cost estimates have been developed using probabilistic modeling, advice from outside consultants, and judgment by management. The estimated liabilities are based on a current understanding of the costs of investigation and remediation. Actual costs, which may differ materially from these estimates, may vary depending on, among other factors, the actual environmental conditions at each site, the level and actual cost of any remediation required, and changes in applicable environmental laws.

SEMCO has done less investigational and remedial work at the remaining four MGP sites but continues to meet all applicable MDEQ requirements. SEMCO believes that further investigation and any remediation of environmental conditions at these sites may be the obligation of other potentially responsible parties and is presently considering whether to file a lawsuit against prior owners of these MGP sites to establish, among other things, their responsibilities with respect to the investigation and remediation of these sites. See Note 14 for information about a settlement in principle reached with respect to these four MGP sites. Similarly, environmental investigation and remediation costs at a fifth MGP site also may be the responsibility, in whole or in part, of another potentially responsible party.

In accordance with an MPSC accounting order, SEMCO's environmental investigation and remediation costs associated with these MGP sites are deferred and amortized over ten years. Rate recognition of the related amortization expense does not begin until the costs are subject to review by the MPSC in a SEMCO Gas base rate case.

Self-Insurance. SEMCO is self-insured for health care costs up to \$100,000 per subscriber annually. Insurance coverage is carried for risks in excess of this amount. Effective September 1, 2009, an additional 153 union-represented employees were covered under this self-insured plan. SEMCO incurred self-insured health care expense of approximately \$5.9 million, \$4.5 million and \$3.5 million for the years ended December 31, 2010, 2009 and 2008, respectively. SEMCO's estimated claims incurred but not reported were \$0.8 million and \$0.7 million as of December 31, 2010, and 2009, respectively, and are included in Other Current Liabilities in the Consolidated Statements of Financial Position.

Other Contingencies. In the normal course of business, SHC and SEMCO may be a party to lawsuits and administrative proceedings before various courts and government agencies. Both also may be involved in private dispute resolution proceedings. These lawsuits and proceedings may involve personal injury, property damage, contractual issues and other matters (including alleged violations of federal, state and local laws, rules, regulations and orders). Management cannot predict the outcome or timing of any pending or threatened litigation or of actual or possible claims. Except as otherwise stated, management believes resulting liabilities, if any, will not have a material adverse impact upon SHC's consolidated financial position, cash flow, or results of operations.

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In December 2008, Aurora Power Resources, Inc. ("Aurora Power") filed a lawsuit against SEMCO in Alaska state court, claiming that the use of an incorrect meter constant by ENSTAR caused Aurora Power to deliver more gas to ENSTAR's pipeline system on behalf of the U.S. Department of Defense's Ft. Richardson laundry ("Ft. Richardson") than was consumed by Ft. Richardson over an extended period of time, resulting in substantial overcharges. SEMCO has determined that, in 2002, ENSTAR replaced a gas meter for Ft. Richardson. The new meter measured deliveries on a Ccf (hundred cubic feet) basis. Deliveries and bills were calculated, however, as if the meter was recording deliveries on a Mcf (thousand cubic feet) basis. As a result of this billing error, Aurora Power overpaid ENSTAR for transportation service, and the U.S. Department of Defense overpaid Aurora Power for natural gas. ENSTAR sales customers actually consumed the gas ENSTAR believed was being consumed by Ft. Richardson. Negotiations with Aurora Power were unsuccessful, and Aurora Power commenced this litigation.

Aurora Power asserts that it is entitled to "gas in kind" under the applicable special transportation contract and tariff to compensate it for the over-deliveries of gas on behalf of Ft. Richardson. ENSTAR disagrees with this contention and believes instead that reimbursement of actual amounts paid is appropriate. ENSTAR filed a motion to refer Aurora Power's complaint to the RCA on the grounds that the RCA has primary jurisdiction over the special contract and tariff issues that will be a factor in determining the measure of Aurora Power's damages. The court granted ENSTAR's motion. Evidentiary hearings were held by the RCA on this matter, and in March 2011, the RCA held that the special contract and tariff provisions that might have required reimbursement "in kind" did not apply to Aurora Power's claim. See Note 14 for information about Aurora Power's appeal of this RCA ruling.

In April 2009, ENSTAR entered into a settlement agreement with the U.S. Department of Defense to remedy the billing error for the period of time where Aurora Power was the U.S. Department of Defense's third-party supplier at Ft. Richardson (October 1, 2004, through October 31, 2006). ENSTAR made a payment to the U.S. Department of Defense and obtained a general release. Because gas sales customers actually consumed the gas and had not yet paid for it, ENSTAR proposed to include amounts paid to the U.S. Department of Defense and to another third-party supplier to Ft. Richardson for the commodity portion of bills for over-deliveries of gas to ENSTAR's pipeline system on behalf of Ft. Richardson in its 2009 Gas Cost Adjustment rate. (The Gas Cost Adjustment rate is the GCR rate charged to ENSTAR customers for the gas they consume.) In March 2010, the RCA rejected ENSTAR's request that these amounts be included in the Gas Cost Adjustment rate and ordered that refunds be made. ENSTAR did not appeal the RCA's ruling. The costs disallowed by this RCA order totaled approximately \$6.7 million, including interest. In compliance with the RCA order, ENSTAR filed a refund plan with the RCA in April 2010. The RCA issued an order requiring that direct refunds be made to qualified customers. The bulk of the refunds were made in November 2010.

Aside from Aurora Power, two other third-party suppliers to the U.S. Department of Defense at Ft. Richardson were affected by this billing error. ENSTAR has resolved the claims of both third-party suppliers.

In March 2009, an explosion and fire occurred at an ENSTAR customer's residence in Anchorage, Alaska. There was extensive damage to a garage and minor damage to the residence. The owner of the residence suffered burns. A lawsuit was filed against ENSTAR in March 2011. The insurance deductible for this type of claim is \$1 million.

An investigation into a 2004 house fire in the SEMCO Gas's service territory in Michigan revealed that a service riser valve (later identified as a Rockford-Eclipse Series 125 valve) malfunctioned when it was actuated by the customer, resulting in an uncontrolled flow of gas. The gas ignited, and the resulting fire caused damage to the customer's residence. During the following four years, seven other riser valve-related gas leaks occurred without any associated property damage or personal injuries. SEMCO Gas has taken a variety of precautionary measures, including labeling each valve with a "Do Not Operate" tag. In mid-2009, an expert engaged by SEMCO determined that a design defect had caused these valve failures. Additional riser valve failures have occurred recently, again without any associated property damage or personal injuries. There are approximately 38,000 valves of this design in the SEMCO Gas system.

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In May 2010, SEMCO filed a lawsuit in Michigan state court against defendants SEMCO believes are responsible for a valve design defect and resulting valve failures. All defendants have filed responsive pleadings and asserted various defenses to SEMCO's claims. SEMCO Gas also has initiated a valve replacement program estimated to cost as much as \$10 million over a five-year period. Refer to Note 14, for information about the MPSC's approval of SEMCO Gas's use of deferral accounting for valve replacement- and valve litigation-related expenditures.

In July 2010, the Municipality of Anchorage sent ENSTAR assessment notices increasing the personal property tax on ENSTAR's pipelines by approximately \$0.6 million annually. ENSTAR requested an informal settlement of the assessment directly with the Municipal Assessor but was notified in August 2010 that this request had been rejected. ENSTAR filed an appeal of the assessment with the Municipality of Anchorage's Board of Equalization in September 2010. An adverse Board of Equalization ruling may be appealed to Alaska state court.

Note 12. Business Segments

SEMCO's primary business is the transmission, distribution and sale of natural gas to its customers, otherwise referred to as its Gas Distribution Business. SEMCO's Gas Distribution Business is structured geographically into two segments:

- The "SEMCO Gas" segment, which is subject to regulation by the MPSC, provides natural gas service to approximately 285,000 customers in Michigan's Upper and Lower Peninsulas.
- The "ENSTAR" segment (including the activities of SEMCO's APC and CINGSA subsidiaries), which is subject to regulation by the RCA, provides natural gas service to approximately 132,000 customers in Anchorage, Alaska and the surrounding areas.

SEMCO has operations and investments in other businesses, including propane distribution, intrastate natural gas pipelines and natural gas storage facilities in Michigan. Under current accounting guidance on segment reporting, these businesses do not meet the quantitative thresholds required to be reportable business segments and are combined and included with SEMCO's corporate division in a category the Company refers to as "Corporate and Other".

SEMCO's corporate division is a cost center rather than a business segment. Any corporate operating expenses that do not relate to the ongoing operations of SEMCO's business segments or are not allocable to them under various regulatory rules are not allocated to those segments. Instead, these unallocated expenses remain on the books of the SEMCO's corporate division. SEMCO's corporate division is included in Corporate and Other.

SEMCO Holding files a consolidated federal income tax return which is allocated among its subsidiaries and divisions whose results are part of the consolidated federal income tax return based on their separate taxable income.

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The following table provides business segment information as well as a reconciliation of the segment information to the applicable line in the Consolidated Financial Statements:

	Operating Revenue (b)	Depreciation and Amortization	Interest Income	Interest Expense	Income Taxes	Net Income Attributable to SHC (b)
	(in thousands)					
2010						
SEMCO Gas	\$ 299,641	\$ 18,464	\$ 143	\$ (9,250)	\$ (10,272)	\$ 17,761
ENSTAR	270,366	12,397	748	(6,751)	(5,980)	8,493
Corporate and other	6,700	1,489	14,571	(21,526)	1,230	(5,116)
Intercompany eliminations (a)	(278)	-	(14,412)	14,412	-	-
Total	<u>\$ 576,429</u>	<u>\$ 32,350</u>	<u>\$ 1,050</u>	<u>\$ (23,115)</u>	<u>\$ (15,022)</u>	<u>\$ 21,138</u>
2009						
SEMCO Gas	\$ 382,474	\$ 18,097	\$ 160	\$ (7,856)	\$ (11,049)	\$ 18,102
ENSTAR	328,774	11,995	322	(4,879)	(3,868)	5,762
Corporate and other	7,976	1,473	11,740	(20,500)	4,615	(3,494)
Intercompany eliminations (a)	(261)	-	(11,510)	11,510	-	-
Total	<u>\$ 718,963</u>	<u>\$ 31,565</u>	<u>\$ 712</u>	<u>\$ (21,725)</u>	<u>\$ (10,302)</u>	<u>\$ 20,370</u>
2008						
SEMCO Gas	\$ 478,455	\$ 17,503	\$ 396	\$ (10,294)	\$ (12,005)	\$ 20,043
ENSTAR	293,638	11,652	797	(7,589)	(7,515)	10,588
Corporate and other	20,037	1,734	(17,510)	(30,291)	3,706	(19,338)
Intercompany eliminations (a)	(8,351)	-	17,919	17,919	-	-
Total	<u>\$ 783,779</u>	<u>\$ 30,889</u>	<u>\$ 1,602</u>	<u>\$ (30,255)</u>	<u>\$ (15,814)</u>	<u>\$ 11,293</u>
	Total Assets (b)	Goodwill	Capital Expenditures			
		(in thousands)				
2010						
SEMCO Gas	\$ 679,669	\$ 65,446	\$ 21,915			
ENSTAR	430,603	130,474	41,462			
Corporate and other	49,694	8,552	240			
Total	<u>\$ 1,159,966</u>	<u>\$ 204,472</u>	<u>\$ 63,617</u>			
2009						
SEMCO Gas	\$ 645,957	\$ 65,446	\$ 22,405			
ENSTAR	414,332	130,474	13,903			
Corporate and other	54,133	8,552	362			
Total	<u>\$ 1,114,422</u>	<u>\$ 204,472</u>	<u>\$ 36,670</u>			

- (a) Represents the elimination of intercompany gas distribution revenue and intercompany interest.
(b) The Company has no international assets, international operating revenues or international net income.

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 13. Reconciliation to Canadian Generally Accepted Accounting Principles

These historical financials statements are presented in accordance with US GAAP. The following tables provide a reconciliation of the historical financial information to Canadian generally accepted accounting principles ("C-GAAP").

Semco Holding Corporation
CONSOLIDATED STATEMENT OF OPERATIONS

	Explanatory Notes Below	Year ended December 31, 2010		
		US GAAP	Effect of Transition to C-GAAP (in thousands)	C-GAAP
Operating revenues				
Gas sales		\$ 536,433	\$ -	\$ 536,433
Gas transportation		24,175	-	24,175
Other	1	15,821	3,665	19,486
		<u>576,429</u>	<u>3,665</u>	<u>580,094</u>
Operating expenses				
Cost of gas sold		395,793	-	395,793
Operations and maintenance	1	80,136	388	80,524
Depreciation and amortization	1	32,350	643	32,993
Property and other taxes	1	11,905	139	12,044
		<u>520,184</u>	<u>1,170</u>	<u>521,354</u>
Operating income		<u>56,245</u>	<u>2,495</u>	<u>58,740</u>
Other income (deductions)				
Interest expense		(23,115)	-	(23,115)
Other	1	3,087	(2,309)	778
		<u>(20,028)</u>	<u>(2,309)</u>	<u>(22,337)</u>
Income before income taxes		<u>36,217</u>	<u>186</u>	<u>36,403</u>
Income tax expense	1	<u>(15,022)</u>	<u>(186)</u>	<u>(15,208)</u>
Net income		<u>21,195</u>	<u>-</u>	<u>21,195</u>
Less: Income attributable to a non-controlling interest		<u>57</u>	<u>-</u>	<u>57</u>
Net income available to common shareholder		<u>\$ 21,138</u>	<u>\$ -</u>	<u>\$ 21,138</u>

Explanatory Notes:

- 1) *Accounting for Joint Ventures.* US GAAP requires the Company's investments in joint ventures to be accounted for using the equity method. Canadian GAAP requires that investments in joint ventures are proportionally consolidated. The different accounting treatment affects only the presentation and the classification and not earnings or shareholder's equity.

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Semco Holding Corporation
CONSOLIDATED STATEMENT OF FINANCIAL POSITION

		At December 31, 2010		
	Explanatory Notes Below	US GAAP	Effect of Transition to C-GAAP (in thousands)	C-GAAP
Current Assets				
Cash and cash equivalents	1	\$ 7,631	\$ 510	\$ 8,141
Restricted cash		441	-	441
Receivables, less allowances	1	40,044	509	40,553
Accrued revenue		60,701	-	60,701
Gas in underground storage, at average cost		49,668	-	49,668
Prepaid expenses		7,213	-	7,213
Materials and supplies, at average cost	1	5,393	97	5,490
Deferred income taxes		4,151	-	4,151
Regulatory assets		410	-	410
Other		3,276	-	3,276
		<u>178,928</u>	<u>1,116</u>	<u>180,044</u>
Property, Plant and Equipment, Net	1	664,626	22,676	687,302
Deferred Charges and Other Assets				
Goodwill		204,472	-	204,472
Regulatory assets	3	73,533	(22,597)	50,936
Investment in unconsolidated affiliate	1	23,333	(23,333)	-
Unamortized debt expense	2	6,926	(6,926)	-
Other		8,148	(1,368)	6,780
		<u>316,412</u>	<u>(54,224)</u>	<u>262,188</u>
Total Assets		<u>\$ 1,159,966</u>	<u>\$ (30,432)</u>	<u>\$ 1,129,534</u>
Current Liabilities				
Notes payable	1	\$ 78,000	\$ 522	\$ 78,522
Accounts payable		70,794	-	70,794
Customer advance payments		31,408	-	31,408
Accrued interest		3,421	-	3,421
Regulatory liability - amounts payable to customers		2,304	-	2,304
Other	1	9,759	13	9,772
		<u>195,686</u>	<u>535</u>	<u>196,221</u>
Deferred Credits and Other Liabilities				
Deferred income taxes	1 & 3	52,401	24	52,425
Regulatory liabilities		69,638	-	69,638
Pension and other postretirement costs	3	35,122	(24,215)	10,907
Customer advances for construction		17,273	-	17,273
Other		19,852	-	19,852
		<u>194,286</u>	<u>(24,191)</u>	<u>170,095</u>
Commitments and Contingencies				
Non-Controlling Interest in a Consolidated Subsidiary	4	-	4,245	4,245
Capitalization				
Long-term debt	2	439,834	(6,926)	432,908
Common shareholder's equity				
Capital surplus		277,220	-	277,220
Accumulated other comprehensive income (loss)	3	(72)	150	78
Retained earnings		48,767	-	48,767
		<u>325,915</u>	<u>150</u>	<u>326,065</u>
Non-controlling interest in a consolidated subsidiary	4	4,245	(4,245)	-
Total equity		<u>330,160</u>	<u>(4,095)</u>	<u>326,065</u>
Total capitalization		<u>769,994</u>	<u>(11,021)</u>	<u>758,973</u>
Total Liabilities and Capitalization		<u>\$ 1,159,966</u>	<u>\$ (30,432)</u>	<u>\$ 1,129,534</u>

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Explanatory Notes:

- 1) *Accounting for Joint Ventures.* US GAAP requires the Company's investments in joint ventures to be accounted for using the equity method. Canadian GAAP requires that investments in joint ventures are proportionally consolidated. The different accounting treatment affects only the presentation and the classification and not earnings or shareholder's equity.
- 2) *Transaction Costs.* Under US GAAP, transaction costs arising from the issuance of debt are recorded as a non-current asset. For Canadian GAAP, these costs are classified in long-term debt.
- 3) *Pension Funding Status.* US GAAP requires an employer to recognize the overfunded or underfunded status of a defined benefit pension and other post-retirement plans as an asset or liability, while Canadian GAAP does not require the recognition of the defined benefit pension and other post-retirement plan funding status.
- 4) *Non-Controlling Interest in a Consolidated Subsidiary.* US GAAP includes non-controlling interests as part of equity. For Canadian GAAP, non-controlling interest is reported in the mezzanine.

The following additional disclosures are requirements of Canadian GAAP and not US GAAP.

Accounts Receivable and Allowance for Doubtful Accounts. The Company had the following past due and uncollectible receivables at December 31, 2010:

			Receivables by period not impaired			
	Total	Receivables Impaired	Less than 30 days	31-60 days	61-90 days	Over 90 days
			(in thousands)			
Accounts receivable at December 31, 2010						
Trade receivables	\$ 38,431	\$ 1,328	\$ 32,646	\$ 3,677	\$ 319	\$ 461
Other receivables	2,983	42	1,642	70	238	991
Allowance for doubtful accounts	(1,370)	(1,370)	-	-	-	-
	<u>\$ 40,044</u>	<u>\$ -</u>	<u>\$ 34,288</u>	<u>\$ 3,747</u>	<u>\$ 557</u>	<u>\$ 1,452</u>
Allowance for doubtful accounts						
Balance at January 1, 2010						\$ (2,114)
New allowance						(1,352)
Allowance applied to uncollectible customer accounts						2,096
Balance at December 31, 2010						<u>\$ (1,370)</u>

Shareholder's Capital. As of December 31, 2010, the Company is authorized to issue 100 shares of voting common stock and 10 shares have been issued. These shares do not have any special attributes attached to them.

Common Stock:	
Par Value	\$0.01
Shares Authorized	100
Shares Outstanding	10

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Joint Ventures. The Company's proportionate interests in its joint venture arrangements are summarized in the table below:

	2010			2009 (a)
	ERGSS 50%	ASHC 70%	Total	ERGSS 50%
(in thousands)				
Proportionate share of operating income for the year ended December 31				
Revenues	\$ 3,665	-	\$ 3,665	\$ 3,507
Expenses	(1,170)	-	(1,170)	(1,160)
	<u>\$ 2,495</u>	<u>\$ -</u>	<u>\$ 2,495</u>	<u>\$ 2,347</u>
Proportionate share of net assets at December 31				
Current assets	\$ 1,116	\$ 2,598	\$ 3,714	\$ 1,508
Property, plant and equipment, net	6,183	8,417	14,600	6,723
Other long-term assets	-	62	62	-
Current liabilities	(535)	(1,172)	(1,707)	(899)
Long-term liabilities	76	-	76	48
	<u>\$ 6,840</u>	<u>\$ 9,905</u>	<u>\$ 16,745</u>	<u>\$ 7,380</u>
Proportionate share of cash flows for the year ended December 31				
Operating activities	\$ 2,812	\$ 637	\$ 3,449	\$ 2,989
Investing activities	(22)	(8,280)	(8,302)	(5)
Financing activities	(2,850)	9,551	6,701	(2,950)
	<u>\$ (60)</u>	<u>\$ 1,908</u>	<u>\$ 1,848</u>	<u>\$ 34</u>

(a) During 2009, the Company was only involved in the ERGSS joint venture. The ASHC joint venture was formed in 2010.

Note 14. Subsequent Events

Under current accounting guidance, SHC is required to disclose events that occur after the balance sheet date but before financial statements are issued or are available to be issued. These are known as subsequent events. Subsequent events have been reviewed through February 1, 2012, the issuance date of these financial statements.

Prior to 2011, ENSTAR's GCR rate was generally adjusted annually to reflect the estimated cost of gas purchased for the upcoming 12-month GCR period. Effective January 2011, ENSTAR's GCR rate is subject to adjustment quarterly, on a calendar quarter basis. Each quarter GCR rate reflects the estimated cost of gas purchased for the upcoming 3-month GCR period and other appropriate rate components. For additional information concerning ENSTAR's GCR rate, refer to Note 1 under the section captioned "*Cost of Gas, Gas Charges Recoverable from Customers and Amounts Payable to Customers.*"

On January 6, 2011, the MPSC approved the settlement of the SEMCO Gas base rate and rate design case, and issued an order for the implementation of the new base rates for service rendered on and after January 7, 2011. The primary provisions of the MPSC-approved settlement include: (i) an estimated \$8.1 million increase in base rate revenue on a normalized annual basis; (ii) an authorized return on equity of 10.35% and an overall rate of return of 7.19%; (iii) allocation of the entire increase, on a combined divisional basis, to SEMCO Gas sales customers and not transportation or special contract customers; and (iv) no change in the current SEMCO Gas rate design. The MPSC also authorized SEMCO Gas to combine its MPSC Division and Battle Creek Division rates and terms and conditions of service. The GCR clauses of the MPSC Division and Battle Creek Division will be combined on and after April 1, 2011. SEMCO Gas has agreed not to file its next base rate case with the MPSC until SEMCO Gas is able to submit audited historical financial data for the 12-month period ending December 31, 2011, or later.

In addition, under the settlement, SEMCO Gas will initiate a Main Replacement Program ("MRP") during 2011. Under the MRP, SEMCO Gas will maintain its current main renewal program and, in addition, will spend at

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

least an average of \$4.4 million a year to replace an additional 13 miles of main and related structures and equipment annually, with a carrying cost rate of 11.66% on those additional expenditures. SEMCO Gas will begin imposing the MRP surcharge in June 2012, and the surcharge is expected to generate approximately \$1.5 million in additional annual revenue. SEMCO Gas also is permitted to defer the costs associated with replacing certain defective service valves. Recovery of the deferred amounts is not guaranteed. Rather, recovery of any amounts, including carrying charges, will be subject to an MPSC review of the actions taken by SEMCO Gas to address the valve issue and all associated expenditures. For additional information regarding the lawsuit filed by SEMCO regarding defective valves and SEMCO Gas's valve replacement program, refer to Note 11. For additional information concerning the SEMCO Gas base rate case, refer to Note 2.

The MAP Contract and the COP Contract includes a commitment by MAP and COP, respectively, to divert gas intended for export from the LNG export facility in Kenai, Alaska, for use instead by ENSTAR customers. In February 2011, the owners of the LNG export plant announced that they would likely cease exports by mid-2011, thus eliminating ENSTAR's diversion rights. In addition, with the expected closure of the LNG export facility in mid-2011, maximum daily deliveries under the MAP Contract may be reduced, if MAP shuts-in wells during summer production and such production cannot later be restored.

In December 2010, the RCA granted CINGSA's Storage Certificate application in part, subject to certain conditions. The RCA subsequently granted CINGSA's request for reconsideration of this order, and, in January 2011, issued an order establishing the service territory for the proposed CINGSA Storage Project. Later in January 2011, the RCA issued another order accepting stipulations reached among parties to the case, approving CINGSA's inception rates and tariff, and explaining the basis for its decision to grant the Storage Certificate to CINGSA. A petition for reconsideration of the RCA's decision on the issuance of the Storage Certificate to CINGSA and the resolution of various ratemaking issues was filed with the RCA. The RCA denied the petition in mid-March 2011.

As provided in the stipulations accepted by the RCA, CINGSA will make a filing in 2012 updating the rates for services from the CINGSA Storage Project to reflect updated estimates of construction costs and debt costs. CINGSA will make another filing with the RCA in 2014 that will further update its rates to reflect actual construction costs and operating costs. CINGSA is also obligated to file a base rate case with the RCA in mid-2017 based upon a test year ending December 31, 2016.

In addition to a Storage Certificate, CINGSA must obtain various property rights, orders, permits, and other authorizations for the CINGSA Storage Project. These include a storage injection order from the Alaska Oil and Gas Conservation Commission (the "AOGCC") and conditional use permits from the Kenai Planning and Zoning Commission (the "KPZC"). The AOGCC has issued the required storage injection order, and the KPZC has issued conditional use permits for the CINGSA Storage Project. Affiliated opponents of the CINGSA Storage Project have appealed these actions to Alaska state court. Since no stay of either decision has been obtained, work on the project may continue. The appeals are pending.

In addition, CINGSA filed an eminent domain action in mid-March 2011, to acquire some of the surface and subsurface property and mineral rights necessary for the operation of the CINGSA Storage Project that CINGSA was unable to obtain through negotiation. Negotiations with a producer and the State of Alaska to acquire necessary property rights have been successfully concluded, and negotiations with a native corporation to secure subsurface property rights needed for the CINGSA Storage Project continue.

ENSTAR filed a petition in January 2011, seeking RCA approval to recover amounts charged to ENSTAR by CINGSA for various storage-related services from ENSTAR's customers. The method of recovery was not specified. The Alaska Attorney General did not oppose ENSTAR's request. The RCA subsequently issued an order approving ENSTAR's recovery of RCA-approved CINGSA charges for various storage-related services in ENSTAR's rates. At a later date, ENSTAR will propose the specific mechanism for recovering these CINGSA charges in rates charged to ENSTAR customers. The RCA is expected to consider that proposal in a proceeding following that filing.

Semco Holding Corporation
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Aurora Power asserts that it is entitled to “gas in kind” from ENSTAR under the applicable special transportation contract and tariff to compensate it for the over-deliveries of gas on behalf of Ft. Richardson. ENSTAR disagrees with this contention and believes instead that reimbursement of actual amounts paid is appropriate. ENSTAR filed a motion to refer Aurora Power’s complaint to the RCA on the grounds that the RCA has primary jurisdiction over the special contract and tariff issues that will be a factor in determining the measure of Aurora Power’s damages. The court granted the motion. Evidentiary hearings were held by the RCA on this matter, and, in March 2011, the RCA held that the special contract and tariff provisions that might have required reimbursement in kind did not apply to Aurora Power’s claim. Aurora Power appealed the RCA ruling on April 8, 2011, and asked that its appeal of various RCA rulings be consolidated with the lawsuit it filed against SEMCO. For additional information regarding this matter and the lawsuit filed by Aurora Power against SEMCO, refer to Note 11.

On March 31, 2011, the APE Pipeline Project was placed in service and new base rates went into effect. With these new base rates, ENSTAR’s base rate revenue is expected to increase by an additional \$3.8 million on a normalized annual basis.

In March 2009, an explosion and fire occurred at an ENSTAR customer’s residence in Anchorage, Alaska. There was extensive damage to a garage and minor damage to the residence. The owner of the residence suffered burns. A lawsuit was filed against ENSTAR in March 2011. The insurance deductible for this type of claim is \$1 million.

On April 7, 2011, SEMCO reached a settlement in principle with respect to the investigation and remediation of four MGP sites. A potentially responsible party SEMCO believed was responsible for the further investigation and any remediation of environmental conditions at these sites and against whom SEMCO planned to file a lawsuit has agreed, among other things, (i) for SEMCO to convey the four sites to it, and (ii) to bear all future environmental investigation and remediation costs for these sites except for a payment by SEMCO of \$2.5 million towards these costs. Upon completion of the settlement, in accordance with an MPSC accounting order, SEMCO will defer this payment and amortize it over ten years. Rate recognition of the related amortization expense does not begin until the costs are subject to review by the MPSC in a SEMCO Gas base rate case.

In September 2011, two additional investors, CIRI-CINGSA Holding and First Alaska Capital Partners, contributed an aggregate of \$7.7 million to ASHC in exchange for an aggregate ownership interest of 8.5% in ASHC. As a result, SCSC now has a 65% ownership interest in ASHC, with MEHC, CIRI-CINGSA Holding and First Alaska Capital Partners holding ownership interests in ASHC of 26.5%, 4.25% and 4.25%, respectively.

In November 2011, CINGSA completed the terms of a \$90 million secured Construction and Term Loan Facility (the “CINGSA Facility”) with RBC Capital Markets LLC as the lead arranger and administrative agent and two additional lenders. The CINGSA Facility is non-recourse to the joint venture partners and will have a four-year maturity. Loans under the CINGSA Facility, from the closing until the third anniversary date of the CINGSA Facility, may either be at LIBOR plus a margin of 2.25% or an Alternative Base Rate, as defined in the CINGSA Facility plus a margin of 1.25%. Commencing on the third anniversary date of the CINGSA Facility, the margin on LIBOR and the Alternative Base Rate loans will increase to 2.50% and 1.50%, respectively. The proceeds from the CINGSA Facility will be used to fund 50% of the anticipated \$180 million CINGSA Storage Project costs.

There were no other subsequent events requiring an adjustment to or disclosure in SHC’s Consolidated Financial Statements.

**Unaudited financial statements of SEMCO Holding Corporation as at and for the three and
nine month periods ended September 30, 2011 and 2010**

SEMCO Holding Corporation

Unaudited Consolidated Financial Statements

**As of September 30, 2011, and September 30, 2010,
and for the three- and nine-month periods ended September 30, 2011, and September 30, 2010**

SEMCO Holding Corporation

Unaudited Consolidated Financial Statements

As of September 30, 2011, and September 30, 2010,
and for the three- and nine-month periods ended September 30, 2011, and September 30, 2010

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All dollar amounts are denominated in U.S. currency.

Semco Holding Corporation
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
	(in thousands)			
Operating revenues				
Gas sales	\$ 60,912	\$ 61,358	\$ 393,552	\$ 360,693
Gas transportation	4,608	4,455	18,101	17,487
Other	3,244	2,988	12,460	11,435
	<u>68,764</u>	<u>68,801</u>	<u>424,113</u>	<u>389,615</u>
Operating expenses				
Cost of gas sold	36,027	38,324	279,812	263,769
Operations and maintenance	19,953	19,736	62,622	57,784
Depreciation and amortization	8,681	8,065	26,033	24,381
Property and other taxes	2,933	3,240	9,219	8,965
	<u>67,594</u>	<u>69,365</u>	<u>377,686</u>	<u>354,899</u>
Operating income	<u>1,170</u>	<u>(564)</u>	<u>46,427</u>	<u>34,716</u>
Other income (deductions)				
Interest expense	(5,718)	(6,389)	(17,276)	(17,240)
Other	1,274	329	3,211	1,884
	<u>(4,444)</u>	<u>(6,060)</u>	<u>(14,065)</u>	<u>(15,356)</u>
Income before income taxes	<u>(3,274)</u>	<u>(6,624)</u>	<u>32,362</u>	<u>19,360</u>
Income tax (expense)	<u>1,352</u>	<u>2,654</u>	<u>(15,048)</u>	<u>(8,057)</u>
Net income	<u>\$ (1,922)</u>	<u>\$ (3,970)</u>	<u>\$ 17,314</u>	<u>\$ 11,303</u>
Less: Income attributable to a non-controlling interest	<u>231</u>	<u>-</u>	<u>393</u>	<u>-</u>
Net income available to common shareholder	<u>\$ (2,153)</u>	<u>\$ (3,970)</u>	<u>\$ 16,921</u>	<u>\$ 11,303</u>
Comprehensive Income				
Net income available to common shareholder	\$ (2,153)	\$ (3,970)	\$ 16,921	\$ 11,303
Other comprehensive income (loss)				
Valuation adjustment for marketable securities, net of income tax benefit (expense) of \$66, \$(43), \$55 and \$(22)	(100)	72	(83)	40
Unrealized derivative gain on interest rate hedge, net of income tax expense of \$0, \$0, \$0 and \$932	-	-	-	1,397
Total comprehensive income	<u>\$ (2,253)</u>	<u>\$ (3,898)</u>	<u>\$ 16,838</u>	<u>\$ 12,740</u>

The accompanying condensed notes to the unaudited consolidated financials statements are an integral part of these statements.

Semco Holding Corporation
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
(Unaudited)

	At September 30,	
	2011	2010
	(in thousands)	
Current Assets		
Cash and cash equivalents	\$ 13,697	\$ 2,386
Restricted cash	7,157	441
Receivables, less allowances of \$1,936 and \$2,260	17,773	17,958
Accrued revenue	14,005	13,518
Gas in underground storage, at average cost	57,196	59,822
Prepaid expenses	7,268	6,554
Deferred income taxes	5,395	1,827
Materials and supplies, at average cost	6,044	5,951
Regulatory assets	2,395	590
Other	1,367	1,364
	<u>132,297</u>	<u>110,411</u>
Property, Plant and Equipment, Net	722,299	644,852
Deferred Charges and Other Assets		
Goodwill	204,472	204,472
Regulatory assets	86,311	61,638
Investment in unconsolidated affiliate	22,762	23,445
Unamortized debt expense	5,765	7,309
Other	7,389	12,660
	<u>326,699</u>	<u>309,524</u>
Total Assets	<u>\$ 1,181,295</u>	<u>\$ 1,064,787</u>
Current Liabilities		
Current maturities of long-term debt and capital lease	\$ 4	\$ -
Notes payable	73,000	45,000
Accounts payable	38,190	28,891
Customer deposits and advance payments	25,158	29,503
Regulatory liabilities	3,602	4,246
Accrued interest	7,138	7,196
Other	548	13,700
	<u>147,640</u>	<u>128,536</u>
Deferred Credits and Other Liabilities		
Regulatory liabilities	73,539	68,152
Deferred income taxes	82,465	43,063
Pension and other postretirement costs	32,567	35,667
Customer advances for construction	17,277	17,435
Other	21,630	15,876
	<u>227,478</u>	<u>180,193</u>
Long-Term Debt and Capital Lease	440,324	439,820
Equity		
Common Shareholder's Equity		
Capital Surplus	277,220	277,220
Accumulated comprehensive income (loss)	(155)	85
Retained earnings	65,688	38,933
	<u>342,753</u>	<u>316,238</u>
Non-controlling interest in a consolidated subsidiary	23,100	-
Total Equity	<u>365,853</u>	<u>316,238</u>
Total Liabilities and Equity	<u>\$ 1,181,295</u>	<u>\$ 1,064,787</u>

The accompanying condensed notes to the unaudited consolidated financials statements are an integral part of these statements

Semco Holding Corporation
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30,	
	2011	2010
	(in thousands)	
Cash flow provided by (used for) operating activities		
Net income (loss)	\$ 17,314	\$ 11,303
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	26,033	24,381
Amortization of debt costs and debt basis adjustments included in interest expense	1,583	2,301
Deferred income tax expense	4,554	10,702
Non-cash share-based compensation	471	579
Changes in operating assets and liabilities and other:		
Receivables and accrued revenue	68,966	70,789
Materials, supplies and gas in underground storage	(8,180)	(9,332)
Current regulatory assets and liabilities	(688)	(4,277)
Accounts payable	(32,604)	(38,411)
Accrued interest	3,717	5,606
Customer advances	(6,246)	(833)
Other	(539)	(6,346)
Net cash provided by (used for) operating activities	74,381	66,462
Cash flows provided by (used for) investing activities		
Property additions	(74,807)	(36,831)
Proceeds from property sales, net of expenses	(1,200)	557
Changes in restricted cash	(6,716)	-
Net cash used for investing activities	(82,723)	(36,274)
Cash flows provided by (used for) financing activities		
Contributions received from non-controlling interest	19,448	-
Issuance (repayment) of short-term bank debt	(5,000)	(13,000)
Issuance of long-term debt, net of expenses	-	295,760
Repayment of long-term debt and capital lease payments	(40)	(314,820)
Net cash provided by (used for) financing activities	14,408	(32,060)
Cash and cash equivalents		
Net increase (decrease)	6,066	(1,872)
Beginning of period	7,631	4,258
End of period	\$ 13,697	\$ 2,386

The accompanying condensed notes to the unaudited consolidated financials statements are an integral part of these statements.

Semco Holding Corporation
CONDENSED NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

As of September 30, 2011, and September 30, 2010,
and for the three- and nine-month periods ended September 30, 2011, and September 30, 2010

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

Semco Holding Corporation (“SHC” or the “Company”) is a Delaware corporation headquartered in Port Huron, Michigan. SHC was formed in December 2007. SHC is a wholly-owned subsidiary of Continental Energy Systems L.L.C. (“Continental”). Continental is a Delaware limited liability company headquartered in Troy, Michigan. Continental was formed in November 2005. Continental invests in regulated public utilities. In addition to owning SHC, Continental also owns New Mexico Gas Intermediate, Inc. (“NMGI”). NMGI owns New Mexico Gas Company, a regulated public utility providing gas utility service in New Mexico. Until July 2010, Continental owned CapRock Holding Corporation (“CRHC”). CRHC owned Cap Rock Energy Corporation (“CRE”). CRE was a regulated public utility providing electric utility service in Texas. Continental sold CRHC and CRE on July 13, 2010.

SHC owns all of the outstanding common stock of SEMCO Energy, Inc. (“SEMCO”). SEMCO is a regulated public utility headquartered in Port Huron, Michigan, and its primary business is the transmission, distribution and sale of natural gas to its customers in Michigan and Alaska. References to “SHC” mean SHC or SHC and its direct and indirect subsidiaries, including SEMCO, as appropriate in the context of this disclosure. References to “SEMCO” mean SEMCO Energy, Inc. and its subsidiaries, or individual SEMCO subsidiaries, divisions or businesses, as appropriate in the context of the disclosure.

SEMCO’s gas distribution business transports and distributes natural gas to approximately 285,000 customers in Michigan and approximately 132,000 customers in Alaska. The Michigan operation is sometimes referred to as “SEMCO Gas” and the Alaska operation (including the activities of SEMCO’s Alaska Pipeline Company (“APC”) subsidiary) is sometimes referred to as “ENSTAR” or “ENSTAR Natural Gas Company.” SEMCO Gas and ENSTAR are divisions of SEMCO. These operations are known together as the “Gas Distribution Business.” The Gas Distribution Business is subject to regulation by the Michigan Public Service Commission (“MPSC”) in Michigan and the Regulatory Commission of Alaska (“RCA”) in Alaska.

SEMCO’s other businesses primarily include operations and investments in propane distribution, intrastate natural gas pipelines, and natural gas storage facilities. In addition, SEMCO is currently developing the Cook Inlet Natural Gas Storage Alaska, LLC (“CINGSA”) in-field storage facility in the Cook Inlet area of Alaska (the “CINGSA Storage Project”).

The accompanying financial statements were prepared by the Company and should be read in conjunction with the financial statements and notes thereto in the Company's 2010 Annual Report. The information in the accompanying financial statements reflects, in the opinion of the Company's management, all adjustments (which are comprised of only normal recurring adjustments) necessary for a fair statement of the information shown, subject to year-end and other adjustments, as later information may require or warrant.

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NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Basis of Presentation. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("US GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates.

Principles of Consolidation. The Consolidated Financial Statements include the accounts of SHC, SEMCO, and SEMCO's wholly-owned subsidiaries, and Alaska Storage Holding Company, LLC ("ASHC"), a subsidiary in which SEMCO has a controlling financial interest. ASHC is the direct owner of CINGSA. For additional information about CINGSA, refer to Note 2 of the Notes to the Consolidated Financial Statements in the Company's 2010 Annual Report. Prior to September 30, 2011, SEMCO-CINGSA Storage Company ("SCSC"), SEMCO's subsidiary, and an affiliate of MidAmerican Energy Holdings Company ("MEHC") had 70% and 30% ownership interests, respectively, in ASHC. On September 30, 2011, two additional investors, CIRI-CINGSA Holding and First Alaska Capital Partners, contributed an aggregate of \$7.7 million to ASHC in exchange for an aggregate ownership interest of 8.5% in ASHC. As a result, SCSC now has a 65% ownership interest in ASHC, with MEHC, CIRI-CINGSA Holding and First Alaska Capital Partners holding ownership interests in ASHC of 26.5%, 4.25% and 4.25%, respectively. Investments in unconsolidated entities, where the Company has significant influence over but does not control the entity, are reported using the equity method of accounting.

Goodwill and Goodwill Impairments. Goodwill represents the excess of a purchase price over the value assigned to the net identifiable assets of businesses acquired. The Company accounts for goodwill under current accounting guidance. Under this guidance, the Company is required to perform impairment tests on its goodwill annually or at any other time when events occur that could impact the value of the Company's goodwill. If an impairment test of goodwill shows that the carrying amount of the goodwill is in excess of the fair value, a corresponding impairment loss would be recorded in the Consolidated Statements of Operations.

The annual impairment tests for the Company's business units will be conducted during the fourth quarter of 2011. There were no changes in the carrying amount of goodwill for the nine-month period ended September 30, 2011.

	<u>Goodwill</u>
	(in thousands)
Balance as of December 31, 2010, and September 30, 2011	\$ 204,472

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NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes. The Company's effective tax rate for the three months ended September 30, 2011, was 39% as compared to 40% for the three months ended September 30, 2010. The Company's effective tax rate for the nine months ended September 30, 2011, was 47% as compared to 42% for the nine months ended September 30, 2010. The increase in the effective tax rate for the nine months ended September 30, 2011, is due primarily to the recognition of a one-time non-cash \$2.0 million income tax charge resulting from a change in Michigan tax law.

In May 2011, Michigan enacted the Michigan Corporate Income Tax ("MCIT"), effective January 1, 2012. The MCIT, a simplified 6% corporate income tax, is replacing the Michigan Business Tax ("MBT"), which was a complex multi-part business tax. Both the MBT and the MCIT are income taxes for financial reporting purposes, for which deferred income tax assets and liabilities are recorded. The Company re-measured its Michigan deferred income tax assets and liabilities at June 30, 2011, to reflect this change in the law. The MCIT does not allow future tax deductions to offset the book-tax difference that existed under the MBT. Due primarily to the elimination of these future tax deductions, the Company eliminated \$11.9 million of net deferred tax assets associated with its Michigan utility (SEMCO Gas) book-tax temporary differences and recognized an \$11.9 million regulatory asset. In addition to the amounts related to SEMCO Gas, the Company eliminated \$2.0 million of net deferred tax assets associated with its non-utility book-tax temporary differences and recognized a \$2.0 million deferred income tax expense.

Recently Issued Accounting Guidance:

From time to time, new accounting pronouncements are issued by the Financial Accounting Standards Board and are adopted by the Company as of the specified effective date. Unless otherwise discussed in periodic disclosure documents, the Company believes that such accounting pronouncements do not apply to the Company.

In May 2011, new accounting guidance was issued that will be included in Accounting Standards Codification ("ASC") Topic 820, "Fair Value Measurement." This guidance clarifies concepts applicable to fair value measurements of non-financial assets and requires the disclosure of quantitative information about unobservable inputs used in such fair value measurements. This guidance will be effective for reporting periods beginning after December 15, 2011, and will be applied prospectively. The Company does not expect this guidance, when it becomes effective, to have a material impact on its consolidated financial position, cash flows or results of operations.

In September 2011, new accounting guidance was issued that will be included in ASC Topic 350, "Intangibles – Goodwill and Other." This new guidance simplifies how entities test goodwill for impairment. It permits an entity first to assess qualitative factors to determine whether it is more likely than not (that is, a likelihood of more than 50%) that the fair value of a reporting unit is less than its carrying amount. If it is more likely than not that the fair value of a reporting unit is less than its carrying amount, entities must perform a more detailed two-step goodwill impairment test. That test is used to identify potential goodwill impairments and to measure the amount of goodwill impairment losses, if any, to be recognized in the entities' financial statements. This new guidance is effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, with

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NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

early adoption permitted. The Company expects to adopt this new guidance in 2012 and does not believe adoption of this new guidance will have a material impact on its consolidated financial position, cash flows or results of operations.

In September 2011, new accounting guidance was issued that will be included in ASC Topic 715, "Compensation – Retirement Benefits." This new guidance requires all nongovernmental entities that participate in multiemployer pension or postretirement benefit plans to provide additional qualitative and quantitative disclosures about financial obligations, risks and commitments, as well as to describe the level of participation in such multiemployer plans. This new guidance requires employers to disclose detailed information about significant multiemployer plans in which they participate, including contributions made to the plans, the financial health and funded status of the plans, and the expiration dates of collective-bargaining agreements that require contributions to the plans. The provisions of this new guidance will be applied retrospectively for annual periods ending after December 15, 2011. Early adoption of this new guidance is permitted. The Company is currently evaluating the impact of this new guidance.

Recently Adopted Accounting Guidance:

In June 2011, new accounting guidance was issued that will be included in ASC Topic 220, "Presentation of Comprehensive Income." This guidance requires entities to present the components of net income and other comprehensive income either as one continuous statement or as two consecutive statements. It eliminates the option of presenting components of other comprehensive income as part of the statement of changes in stockholders' equity. The guidance does not change the items that must be reported in other comprehensive income, how such items are measured or when they must be classified to net income. This guidance is effective for interim and annual periods beginning after December 15, 2011. The Company adopted this guidance effective with the second quarter of 2011 and is now presenting the Consolidated Statement of Comprehensive Income immediately after the Consolidated Statement of Operations. Because this guidance only affects how information is presented, it did not have any effect on the Company's consolidated financial position, cash flows or results of operations.

NOTE 2 - SHORT-TERM AND LONG-TERM DEBT

On January 30, 2009, Continental, along with its co-borrowers NMGI, SHC and CRHC, entered into a credit agreement with Royal Bank of Canada ("RBC"), as administrative agent, and a syndicate of lenders (the "CES RBC Credit Agreement"). The CES RBC Credit Agreement consists of a \$300 million secured term loan (the "CES RBC Term Loan") which was drawn at one time and has a maturity date of January 30, 2014. SHC was initially allocated \$118.0 million of the CES RBC Term loan ("SHC CES RBC Term Loan"). As of September 30, 2011, the outstanding balance on the SHC CES RBC Term Loan was \$90.0 million. The stock of several Continental subsidiaries is pledged as collateral under the CES RBC Credit Agreement.

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NOTE 2 - SHORT-TERM AND LONG-TERM DEBT (Continued)

The SHC RBC Term Loan may be incurred and maintained as, or converted into, Alternative Base Rate (“ABR”) loans or LIBOR loans. ABR loans bear interest at a rate per annum of 1.25% plus the higher of (i) prime lending rate announced from time to time by the administrative agent; (ii) the Federal Funds Effective Rate plus $\frac{1}{2}$ of 1%; or (iii) the LIBOR rate for a one month interest period plus 1%. LIBOR loans bear interest at the rate per annum of 2.25% plus the relevant LIBOR rate (for interest periods of one, two, three or six months). Interest on ABR Loans is payable in arrears on the last business day of each March, June, September and December. Interest on LIBOR loans is payable on the last day of each interest period, except in the case of LIBOR loans with an interest period of six months on which interest is to be paid every three months.

SEMCO also has a credit agreement with RBC, as administrative agent, and a syndicate of lenders (the “SEMCO RBC Credit Agreement”). The SEMCO RBC Credit Agreement consists of a \$130 million secured revolving credit facility (the “SEMCO RBC Revolver”), with a maturity date of November 9, 2012, and a \$345 million secured term loan (the “SEMCO RBC Term Loan”), with a maturity date of November 9, 2014. The balance on the SEMCO RBC Term Loan at September 30, 2011, was \$45 million. For further information on the SEMCO RBC Term Loan, including the repayment of \$300 million of the Term Loan in the second quarter of 2010, refer to Note 4 of the Notes to the Consolidated Financial Statements in the Company’s 2010 Annual Report.

Interest on the SEMCO RBC Revolver and SEMCO RBC Term Loan is at variable rates, which are based on LIBOR or an alternative base rate. For additional information on the interest rates used to calculate interest due under the SEMCO RBC Credit Agreement, refer to Note 5 of the Notes to the Consolidated Financial Statements in the Company’s 2010 Annual Report.

At September 30, 2011, SEMCO was utilizing \$73.5 million of the borrowing capacity available under the SEMCO RBC Revolver, leaving approximately \$56.5 million of the borrowing capacity unused. The \$73.5 million of capacity being used represented \$73.0 million of borrowings and approximately \$0.5 million of letters of credit. These amounts will change from time to time reflecting SEMCO’s then-current working capital needs and then-current gas supplier credit terms.

SEMCO also has issued senior secured notes (“Senior Notes”) in an aggregate principal amount of \$300 million with a fixed interest rate of 5.15%. The Senior Notes will mature at 100% of their principal amount on April 21, 2020. SEMCO pays the interest on the Senior Notes on a semi-annual basis in arrears on April 21 and October 21 of each year. For additional information on the Senior Notes, refer to Note 4 of the Notes to the Consolidated Financial Statements in the Company’s 2010 Annual Report.

In addition to the SEMCO RBC Term Loan and the Senior Notes, SEMCO has approximately \$5.0 million of other long-term debt outstanding at September 30, 2011, at fixed interest rates.

The SEMCO RBC Credit Agreement and the indentures governing certain of SEMCO’s other debt contain various financial covenants. At September 30, 2011, SEMCO was in compliance with these financial covenants. Failure to comply with any of the financial covenants may result in an event of default which, if not cured or waived, could result in the acceleration of the debt under the SEMCO RBC Credit Agreement or the indentures governing SEMCO’s other outstanding debt that contain cross-acceleration or cross-default provisions.

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NOTE 2 - SHORT-TERM AND LONG-TERM DEBT (Continued)

In April 2011, CINGSA entered into an agreement to lease land containing an underground reservoir (the "CINGSA Reservoir Lease") for the purpose of developing the CINGSA Storage Project. The CINGSA Reservoir Lease is being recorded as a capitalized lease. The assets and related obligations for the CINGSA Reservoir Lease have been recorded at the present value of the minimum lease payments, or approximately \$0.5 million. The capitalized cost of the CINGSA Reservoir Lease is being reported as part of Property, Plant and Equipment, Net and the discounted balance due on the CINGSA Reservoir Lease is being reported as part of Current Maturities of Long-Term Debt and Capital Lease and Long-Term Debt and Capital Lease within the Consolidated Statements of Financial Position. The capitalized cost recorded for the CINGSA Reservoir Lease did not involve the exchange of cash and therefore is not reflected in the Company's Consolidated Statements of Cash Flows.

NOTE 3 - RISK MANAGEMENT ACTIVITIES AND DERIVATIVE TRANSACTIONS

The Company's business activities expose it to a variety of risks, including commodity price risk and interest rate risk. Management identifies risks associated with the Company's business and determines which risks, if any, it wishes to manage with financial instruments and which type of instruments it should use to manage those risks. If used by the Company, such instruments may be subject to regulation under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 and, when finalized, implementing regulations of the Securities Exchange Commission, the Commodity Futures Trading Commission, and other federal agencies.

The Company records all derivative instruments into which it enters based on current accounting guidance on this subject. The applicable guidance requires that every derivative instrument (including certain derivative instruments embedded in other contracts), except for those that qualify for the normal purchases and sales exception, be recorded in the statement of financial position, as either an asset or liability, and measured at fair value. Derivative instruments that qualify for the purchase and sales exception are not recognized at fair value in the statement of financial position. The guidance on this subject also requires that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. Special accounting for qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the statement of operations and requires that an entity document, designate, and assess the effectiveness of transactions that receive hedge accounting. For derivatives designated as cash flow hedges, changes in fair value are recorded in other comprehensive income for the portion of the change in value of the derivative that is an effective hedge. Any ineffective portion of the change in fair value would be recorded as a gain or loss in the income statement.

As of September 30, 2011, the Company did not have any financial instruments used to manage its commodity price risks or interest rate risks.

NOTE 4 – FAIR VALUE MEASUREMENTS

Accounting guidance governing fair value measurements and related disclosures provides that fair value represents the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that is determined based upon assumptions that market participants would use in pricing an asset or liability. As a basis for making such assumptions, accounting guidance also establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

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NOTE 4 – FAIR VALUE MEASUREMENTS (Continued)

- Level 1: Observable inputs, such as quoted prices in active markets;
- Level 2: Inputs, other than quoted prices in active markets, that are observable either directly or indirectly; and
- Level 3: Unobservable inputs for which there is little or no market data, requiring the reporting entity to develop its own assumptions.

Assets and liabilities measured at fair value are based on one or more of the following three valuation techniques identified under accounting guidance:

- (A) Market approach: Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities;
- (B) Cost approach: Amount that would be required to replace the service capacity of an asset (replacement cost); and
- (C) Income approach: Techniques to convert future amounts to a single present value based upon market expectations (including present value techniques, option-pricing and excess earnings models).

Financial assets and liabilities measured at fair value as of September 30, 2011, are set forth in the table below:

Description	Frequency	Asset / (Liability)	Level 1 (In thousands)	Level 2	Level 3	Valuation Technique
Marketable Securities	Recurring	\$ 894	\$ 894	\$ -	\$ -	A

SEMCO's marketable securities represent future deferred compensation payments invested in both equity and debt securities and held in two trusts. The fair values of these marketable securities are obtained from quoted market prices and are provided to SEMCO by the bank administering the trusts.

NOTE 5 - TRANSACTIONS WITH RELATED PARTIES

Management services are provided to the Company by an affiliate of the Company that manages the group of investment funds that together are the indirect majority owner of the Company. Fees for these services amounted to \$0.3 million and \$0.9 million for each of the three- and nine-month periods ended September 30, 2011, and September 30, 2010, respectively. These fees are included in Operations and Maintenance ("O&M") expense in the Consolidated Statements of Operations.

Eaton Rapids Gas Storage System ("ERGSS") provides natural gas storage services to SEMCO Gas. SEMCO Gas Storage Company, a subsidiary of SEMCO, is a 50% owner of ERGSS. The cost of these storage services provided to SEMCO Gas was \$0.9 million and \$2.6 million for each of the three- and nine-month periods ended September 30, 2011, and September 30, 2010, respectively. These costs are included in Cost of Gas Sold in the Consolidated Statements of Operations.

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NOTE 5 - TRANSACTIONS WITH RELATED PARTIES (Continued)

The Company's Consolidated Statements of Financial Position include a \$0.5 million receivable from affiliates as of September 30, 2011. The receivable is included in Other Current Assets in the Consolidated Statements of Financial Position.

NOTE 6 – PENSION PLANS AND OTHER POSTRETIREMENT BENEFITS

The following tables summarize the components of SEMCO's net pension benefit and net other postretirement benefit costs:

	Pension Benefits			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
	(in thousands)			
Components of net benefit cost				
Service cost	\$ 1,032	\$ 916	\$ 3,095	\$ 2,841
Interest cost	1,759	1,660	5,277	5,027
Expected return on plan assets	(2,018)	(1,737)	(6,055)	(5,211)
Amortization of prior service costs	5	-	15	-
Amortization of net loss	239	232	718	784
Income from settlement	-	4	-	-
Amortization of regulatory asset	417	417	1,252	1,251
Net benefit cost	<u>\$ 1,434</u>	<u>\$ 1,492</u>	<u>\$ 4,302</u>	<u>\$ 4,692</u>

	Other Postretirement Benefits			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
	(in thousands)			
Components of net benefit cost				
Service cost	\$ 238	\$ 186	\$ 713	\$ 537
Interest cost	569	560	1,708	1,681
Expected return on plan assets	(722)	(645)	(2,167)	(1,908)
Amortization of net (gain) loss	-	(9)	-	(23)
Amortization of regulatory asset	328	328	983	983
Net benefit cost	<u>\$ 413</u>	<u>\$ 420</u>	<u>\$ 1,237</u>	<u>\$ 1,270</u>

SHC's expected long-term rate of return on pension plan assets is 8%. For the twelve months ended September 30, 2011, the actual return on pension plan assets was 0%, and for the twelve months ended September 30, 2010, the actual return was 14.7%. The expected rate of return is an assumption about long-term asset performance that SHC reviews annually for reasonableness and appropriateness.

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NOTE 7 - COMMITMENTS AND CONTINGENCIES

Environmental Issues. Prior to the construction of major interstate natural gas pipelines, gas for heating and other uses was manufactured from processes involving coal, coke or oil. Residual byproducts of these processes may have caused environmental conditions that require investigation and remediation. As of September 30, 2011, SEMCO Gas owned seven sites in Michigan where such manufactured gas plants ("MGP") were formerly located. (As noted below, SEMCO Gas has conveyed four of those MGP sites to a prior owner of the sites. Refer to Note 11, Subsequent Events, for additional information about the transfer of these four sites.) Even though SEMCO Gas never operated MGP facilities at four of the sites and did so at a fifth site for only a brief period of time, SEMCO Gas is subject to federal, state and local laws and regulations that require, among other things, the investigation and, if necessary, the remediation of contamination associated with these sites, irrespective of fault, legality of initial activity, or ownership, and which may impose liability for damage to natural resources. SEMCO Gas has complied with the applicable Michigan Department of Environmental Quality ("MDEQ") requirements, which mandate that current landowners mitigate unacceptable risks to human health from the byproducts of MGP operations and notify the MDEQ and adjacent property owners of potential contaminant migration. As discussed in more detail below, SEMCO Gas is currently investigating several of these MGP sites and anticipates conducting any necessary additional investigatory and remediation activities as appropriate. SEMCO Gas has already investigated, remediated and closed a site related to one of the MGP sites, with the MDEQ's approval.

In connection with these activities, SEMCO Gas is attempting to identify other potentially responsible persons to bear some or all of the costs and liabilities associated with activities at several of these sites. SEMCO Gas also is pursuing recovery of the costs of these activities from insurance carriers. In 2008, SEMCO Gas received approximately \$1.9 million from an insurer in exchange for a release of the insurer from liability for claims related to all of SEMCO Gas's MGP sites. In accordance with an MPSC accounting order, the payment was initially recorded as a deferred asset. This payment was subsequently reclassified as a deferred liability as a result of a 2011 SEMCO Gas base rate case settlement. The payment made by the insurer under the settlement will continue to be amortized over ten years. SEMCO Gas is continuing to pursue the recovery of investigation and remediation costs from another insurer. SEMCO Gas is unable to predict, however, whether and to what extent it will be successful in involving other potentially responsible persons in MGP-related investigatory or remediation activities, or in bearing some or all of the costs and liabilities thereof, or in securing additional insurance recoveries for costs and liabilities associated with these sites.

SEMCO Gas accrues for costs associated with environmental investigation and remediation obligations when such costs are probable and reasonably estimable. Accruals for estimated costs for environmental remediation obligations are generally recognized no later than the completion of SEMCO Gas's Remedial Action Plan ("RAP") for a site. Such accruals are adjusted as further information becomes available or circumstances change. At three of the MGP sites, SEMCO Gas has begun efforts to determine the extent of remediation, if any, that must be performed, with the expectation of completing and submitting a RAP for each of the sites to the MDEQ. From time to time, moreover, pre-RAP remediation activities are undertaken during the investigatory process. As a result of investigational work performed to date, the Company's Consolidated Statements of Financial Position include an accrual and a corresponding regulatory asset in the amount of \$5.3 million at September 30, 2011, for estimated environmental investigation and remediation costs that SEMCO Gas believes are probable at these three sites. The Company has not discounted this accrual to its present value. The accrued costs are expected to be paid out over the next three years.

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NOTE 7 - COMMITMENTS AND CONTINGENCIES (Continued)

The accrual of \$5.3 million represents what the Company believes is probable and reasonably estimable. However, the Company also believes that it is reasonably possible that there could be up to an additional \$5.9 million of environmental investigation and remediation costs associated with these three sites. It is also reasonably possible that the amount accrued or the estimated range of additional costs may change in the future as SEMCO Gas's investigation of these sites continues and any remediation activities are undertaken. SEMCO Gas's cost estimates have been developed using probabilistic modeling, advice from outside consultants, and judgment by management. The liabilities estimated are based on a current understanding of the costs of investigation and remediation at these three sites. Actual costs, which may differ materially from these estimates, may vary depending on, among other factors, the actual environmental conditions at each site, the actual costs of any required remediation, and changes in applicable environmental laws.

SEMCO Gas has done relatively less investigational and remedial work at the remaining four MGP sites but continues to meet all applicable MDEQ requirements. SEMCO Gas believed that further investigation and any remediation of environmental conditions at these sites could be the obligation of other potentially responsible persons and had been considering whether to file a lawsuit against prior owners of these four MGP sites to establish, among other things, their responsibilities with respect to the investigation and remediation of these sites. In July 2011, SEMCO Gas entered into a settlement with respect to the investigation and remediation of these four MGP sites. Under the settlement, (i) the four MGP sites will be transferred to a prior owner of the sites, (ii) SEMCO Gas will pay \$2.5 million towards the investigation and remediation of environmental conditions at the sites, and (iii) SEMCO Gas will be indemnified against any additional investigation, remediation, and other site-related costs. SEMCO Gas has made the payment required by the settlement and has conveyed the four MGP sites to the prior owner. Refer to Note 11, Subsequent Events, for additional information about the transfer of these four sites. Similarly, SEMCO Gas believes that the environmental investigation and remediation costs at a fifth MGP site also may be the responsibility, in whole or in part, of another potentially responsible person. It is actively considering ways in which to pursue that matter.

In accordance with an MPSC accounting order, SEMCO Gas's environmental investigation and remediation costs associated with these MGP sites (including the \$2.5 million paid in connection with the settlement involving the four MGP sites) are deferred and amortized over ten years. Rate recognition of the related amortization expense does not begin until the costs are subject to review by the MPSC in a base rate case.

Other Contingencies. In the normal course of business, the Company may be a party to lawsuits and administrative proceedings before various courts and governmental agencies. The Company also may be involved in private dispute resolution proceedings. These lawsuits and other kinds of proceedings may involve personal injuries, property damage, contractual issues and other matters (including alleged violations of federal, state and local laws, rules, regulations and orders). Management cannot predict the outcome or timing of any pending or threatened litigation or of actual or possible claims. Except as otherwise stated, management believes that resulting liabilities, if any, will not have a material adverse impact upon the Company's consolidated financial position, cash flow, or results of operations.

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NOTE 7 - COMMITMENTS AND CONTINGENCIES (Continued)

In December 2008, Aurora Power Resources, Inc. ("Aurora Power") filed a lawsuit against SEMCO in Alaska state court, claiming that the use of an incorrect meter constant by ENSTAR caused Aurora Power to deliver more gas to ENSTAR's pipeline system on behalf of the U.S. Department of Defense's Ft. Richardson laundry ("Ft. Richardson") than was consumed by Ft. Richardson over an extended period of time, resulting in substantial overcharges. SEMCO has determined that, in 2002, ENSTAR replaced a gas meter for Ft. Richardson. The new meter measured deliveries on a Ccf (hundred cubic feet) basis. Deliveries and bills were calculated, however, as if the meter was recording deliveries on a Mcf (thousand cubic feet) basis. As a result of this billing error, Aurora Power overpaid ENSTAR for transportation service, and the U.S. Department of Defense overpaid Aurora Power for natural gas. ENSTAR sales customers actually consumed the gas ENSTAR believed was being consumed by Ft. Richardson.

Aurora Power asserts that it is entitled to "gas in kind" under the applicable special transportation contract and tariff to compensate it for the over-deliveries of gas on behalf of Ft. Richardson. ENSTAR disagrees with this contention and believes instead that reimbursement of actual amounts paid is appropriate. ENSTAR filed a motion to refer Aurora Power's complaint to the RCA on the grounds that the RCA has primary jurisdiction over the special contract and tariff issues that will be a factor in determining the measure of Aurora Power's damages. The court granted ENSTAR's motion. Evidentiary hearings were held by the RCA in this matter, and, in March 2011, the RCA held that the special contract and tariff provisions that might have required reimbursement of "gas in kind" did not apply to Aurora Power's claim. Aurora Power has appealed the RCA's decision to Alaska state court and sought to consolidate the appeal with the underlying lawsuit. In April 2011, Aurora Power's appeal and underlying lawsuit were consolidated by the court. ENSTAR has filed various motions in the case, and a schedule has been established by the court for the submission of motion responses and replies by Aurora Power and ENSTAR.

In April 2009, ENSTAR entered into a settlement agreement with the U.S. Department of Defense to remedy the billing error for the period of time where Aurora Power was the U.S. Department of Defense's third-party supplier at Ft. Richardson (October 1, 2004, through October 31, 2006). ENSTAR made a payment to the U.S. Department of Defense and obtained a general release. Because gas sales customers actually consumed the gas and had not yet paid for it, ENSTAR proposed to include amounts paid to the U.S. Department of Defense and to another third-party supplier to Ft. Richardson for the commodity portion of bills for over-deliveries of gas to ENSTAR's pipeline system on behalf of Ft. Richardson in its 2009 Gas Cost Adjustment, or GCA, rate. (The GCA rate is also referred to as a "Gas Cost Recovery" or "GCR" rate.) In March 2010, the RCA rejected ENSTAR's request that these amounts be included in the GCA rate and ordered that refunds be made. ENSTAR did not appeal the RCA's ruling. The costs disallowed by this RCA order totaled approximately \$6.7 million, including interest. In compliance with the RCA order, ENSTAR filed a refund plan with the RCA in April 2010. The RCA issued an order requiring that direct refunds be made to qualified customers. The refunds will be completed in 2011, with the last credits appearing on the January 2012 bills of customers.

Aside from Aurora Power, two other third-party suppliers to the U.S. Department of Defense at Ft. Richardson were affected by this billing error. ENSTAR has resolved the claims of both third-party suppliers.

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NOTE 7 - COMMITMENTS AND CONTINGENCIES (Continued)

In March 2009, an explosion and fire occurred at an ENSTAR customer's residence in Anchorage, Alaska. There was extensive damage to a garage and minor damage to the residence. The owner of the residence suffered burns. A lawsuit was filed against ENSTAR in March 2011. The Company's insurance deductible for this type of claim is \$1 million.

An investigation into a 2004 house fire in SEMCO Gas's Michigan service territory revealed that a service riser valve (later identified as a Rockford-Eclipse Series 125 valve) malfunctioned when it was actuated by the customer, resulting in an uncontrolled flow of gas. The gas ignited, and the resulting fire caused damage to the customer's residence. During the following seven years, thirteen other riser valve-related gas leaks occurred without any associated property damage or personal injuries. In response, SEMCO Gas has taken a variety of precautionary measures, including labeling each valve with a "Do Not Operate" tag. In mid-2009, an expert engaged by SEMCO Gas determined that a design defect had caused these valve failures. Additional riser valve failures have occurred recently, again without any associated property damage or personal injuries. There are approximately 44,000 valves of this design in the SEMCO Gas system, and SEMCO Gas has replaced approximately 15,000 of these valves as of September 2011, under a valve replacement program SEMCO Gas initiated.

In May 2010, SEMCO Gas filed a lawsuit in Michigan state court against defendants SEMCO Gas believes are responsible for a valve design defect and resulting valve failures. All defendants have filed responsive pleadings and asserted various defenses to SEMCO Gas's claims. In September 2011, the court granted the motions for summary judgment filed by the defendants, on the grounds that the Uniform Commercial Code's four year statute of limitations barred SEMCO Gas's claims. SEMCO Gas has appealed this decision. As noted earlier, SEMCO Gas also has initiated a valve replacement program. That program is estimated to cost as much as \$10 million over a five-year period. Refer to Note 14 of the Notes to the Consolidated Financial Statements in the Company's 2010 Annual Report for information about the MPSC's approval of the SEMCO Gas's use of deferral accounting for valve replacement- and valve litigation-related expenditures.

In July 2010, the Municipality of Anchorage sent ENSTAR assessment notices increasing the personal property tax on ENSTAR's pipelines by approximately \$0.6 million annually. ENSTAR filed an appeal of the assessment with the Municipality of Anchorage's Board of Equalization in September 2010. A hearing on the appeal was held in May 2011, and the Board of Equalization upheld the assessor's valuation of ENSTAR's pipelines. In June 2011, ENSTAR filed a motion for reconsideration of this decision. In August 2011, the Board of Equalization granted ENSTAR's request for reconsideration, and another hearing was held to consider the Company's appeal. Following this hearing, the Board of Equalization again upheld the assessor's valuation of ENSTAR's pipelines. ENSTAR has filed an appeal of this decision in Alaska state court. Additionally, in September 2011, ENSTAR filed an appeal of the 2011 pipeline property tax assessment with the Board of Equalization. Adverse final Board of Equalization rulings on the 2011 appeal may also be appealed to Alaska state court.

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NOTE 8 - REGULATORY MATTERS

SEMCO Gas

In early January 2011, the MPSC approved a settlement of the SEMCO Gas base rate and rate design case, and issued an order for the implementation of the new base rates for service rendered on and after January 7, 2011. The primary provisions of the MPSC-approved settlement included: (i) an estimated \$8.1 million increase in base rate revenue on a normalized annual basis; (ii) an authorized return on equity of 10.35% and an overall rate of return of 7.19%; (iii) allocation of the entire increase, on a combined divisional basis, to SEMCO Gas sales customers and not transportation or special contract customers; and (iv) no change in the current SEMCO Gas rate design. The MPSC also authorized SEMCO Gas to combine its MPSC Division and Battle Creek Division rates and terms and conditions of service. The Gas Cost Recovery ("GCR") clauses of the MPSC Division and Battle Creek Division were combined on April 1, 2011. SEMCO Gas has agreed not to file its next base rate case with the MPSC until SEMCO Gas is able to submit audited historical financial data for the 12-month period ending December 31, 2011, or later.

In addition, under the settlement, SEMCO Gas will initiate a Main Replacement Program ("MRP") during 2011. Under the MRP, SEMCO Gas will maintain its current main renewal program and, in addition, will spend at least an average of \$4.4 million a year to replace an additional 13 miles of main and related structures and equipment annually, with a carrying cost rate of 11.66% on those additional expenditures. SEMCO Gas will begin imposing the MRP surcharge in June 2012, and the surcharge is expected to generate approximately \$1.5 million in additional annual revenue on a normalized annual basis. SEMCO Gas also is permitted to defer the costs associated with replacing certain defective service valves. Recovery of the deferred amounts is not guaranteed. Rather, recovery of any amounts, including carrying charges, will be subject to an MPSC review of the actions taken by SEMCO Gas to address the valve issue and all associated expenditures. For additional information about the lawsuit filed by SEMCO Gas regarding defective valves, refer to Note 7. For additional information about the SEMCO Gas base rate case, refer to Note 2 of the Notes to the Consolidated Financial Statements in the Company's 2010 Annual Report.

ENSTAR & CINGSA

Prior to 2011, ENSTAR's GCR rate was generally adjusted annually to reflect the estimated cost of gas purchased for the upcoming 12-month GCR period. Effective January 2011, ENSTAR's GCR rate is subject to adjustment quarterly, on a calendar quarter basis. Each quarterly GCR rate reflects the estimated cost of gas purchased for the upcoming 3-month GCR period and other appropriate rate components. For additional information concerning ENSTAR's GCR rate, refer to Note 1 of the Notes to the Consolidated Financial Statements in the Company's 2010 Annual Report, under the section captioned "Cost of Gas, Gas Charges Recoverable from Customers and Amounts Payable to Customers."

Based on ENSTAR's base rate case settlement accepted by the RCA in August 2010, ENSTAR's base rate revenue was expected to increase by an additional \$3.8 million on a normalized annual basis when a project to connect the ENSTAR system to a new source of gas (the "APE Pipeline Project") is completed and gas deliveries to ENSTAR's customers begin. In early April 2011, the APE Pipeline Project was completed and went into service. The related change in base rates was made in customer billings beginning in April 2011, after notice was given to the RCA.

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NOTE 8 - REGULATORY MATTERS (Continued)

In December 2010, the RCA granted CINGSA a certificate of public convenience and necessity (a "Storage Certificate") for the CINGSA Storage Project, in part, subject to certain conditions. The RCA subsequently granted CINGSA's request for reconsideration of this order, and, in January 2011, issued an order establishing the service territory for the proposed CINGSA Storage Project. Later in January 2011, the RCA issued another order accepting stipulations reached among parties to the case, approving CINGSA's inception rates and tariff, and explaining the basis for its decision to grant the Storage Certificate to CINGSA. A petition for reconsideration of the RCA's decision on the issuance of the Storage Certificate to CINGSA and the resolution of various ratemaking issues was filed with the RCA. The RCA denied the petition in mid-March 2011.

As provided in the stipulations accepted by the RCA, CINGSA will make a filing in 2012 updating the rates for services from the CINGSA Storage Project to reflect then-current estimates of construction costs and debt costs. CINGSA will make another filing with the RCA in 2014 that will further update rates for services from the CINGSA Storage Project to reflect actual construction costs and operating costs. CINGSA is also obligated to file a base rate case with the RCA in mid-2017 based on a test year ending December 31, 2016.

In addition to a Storage Certificate, CINGSA must obtain various property rights, orders, permits, and other authorizations for the CINGSA Storage Project. These include a storage injection order from the Alaska Oil and Gas Conservation Commission (the "AOGCC") and conditional use permits from the Kenai Planning and Zoning Commission (the "KPZC"). The AOGCC has issued the required storage injection order, and the KPZC has issued conditional use permits for the CINGSA Storage Project. Affiliated opponents of the CINGSA Storage Project have appealed these actions to Alaska state court. Since no stay of either decision has been obtained, work on the project may continue. The appeals are pending.

ENSTAR filed a petition in January 2011, seeking RCA approval to recover amounts charged to ENSTAR by CINGSA for various storage-related services from ENSTAR's customers. The method of recovery was not specified. The Alaska Attorney General did not oppose ENSTAR's request. The RCA subsequently issued an order approving ENSTAR's recovery of RCA-approved CINGSA charges for various storage-related services in ENSTAR's rates. In a filing made in August 2011, ENSTAR asked the RCA to approve the recovery of storage-related costs in the GCR rate charged to ENSTAR's Alaska customers. As part of this filing and in compliance with a prior RCA order, ENSTAR also filed its contract with CINGSA with the RCA for approval. This filing describes in detail the cost recovery methodology that ENSTAR proposes be used to recoup these expenses, including various proposed revisions to the relevant tariff provisions. For additional information on the approval of this filing in October 2011, refer to Note 11, Subsequent Events.

In March 2011, CINGSA brought a condemnation action in Alaska state court to obtain title to property necessary to construct and operate the CINGSA Storage Project. This lawsuit has been filed against property owners that have not already sold their property or granted easements to CINGSA. The complaint requests that the court grant CINGSA rights to the property and also award just compensation to the property owners for these interests. In July 2011, the court granted CINGSA immediate possession of the condemned property interests. CINGSA deposited with the court an amount equal to the estimated just compensation value for the condemned property interests. If one or more of the property owners

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dispute the value proposed by CINGSA and approved for deposit by the court, they may request further proceedings before a special master and the court.

NOTE 8 - REGULATORY MATTERS (Continued)

Effective August 1, 2011, CINGSA completed the purchase of mineral and property interests in the Cannery Loop Unit from Marathon Alaska Production Company ("MAP") for \$5.5 million. These mineral and property rights are needed for the construction and operation of the CINGSA Storage Project. Because CINGSA's operations are surrounded by land from which MAP continues to produce gas, the parties have indemnified each other against interference with their respective business operations.

In August 2011, ENSTAR entered into additional gas supply agreements with Buccaneer Energy, LLC ("Buccaneer"), Cook Inlet Energy, LLC ("Cook Inlet Energy"), and Aurora Gas, LLC ("Aurora Gas"). The gas supply agreement with Buccaneer is for up to 31.5 billion cubic feet ("Bcf") of firm gas supply, with deliveries to start when the CINGSA Storage Project goes into service and extend until 2018. The pricing under this contract varies by season and is adjusted quarterly, subject to ceiling and floor prices. The other two contracts are for non-firm variable-priced bid gas offered for sale and purchased through the ENSTAR daily bidding system, subject to a ceiling price. Deliveries under these two contracts are expected to begin in the winter of 2011-2012. The Buccaneer, Cook Inlet Energy and Aurora Gas contracts were approved by the RCA in September 2011. As a result, the cost of gas purchased under these contracts is includable for recovery under ENSTAR's GCR mechanism.

In August 2011, ENSTAR sought RCA approval of an amendment to the November 2000 gas supply agreement with Union Oil Company of California ("Union Oil") (the "November 2000 Unocal Contract"). If approved, the amendment would permit Union Oil to deliver gas to ENSTAR at a new delivery point. ENSTAR is seeking RCA approval to recover the transportation costs associated with gas being delivered at this new delivery point in the GCR rate charged to customers. For additional information on the approval of this amendment by the RCA, refer to Note 11, Subsequent Events.

NOTE 9 – BUSINESS SEGMENTS

SEMCO's primary business is the transmission, distribution and sale of natural gas to its customers, otherwise referred to as its Gas Distribution Business. SEMCO's Gas Distribution Business is structured geographically into two segments:

- The "SEMCO Gas" segment, which is subject to regulation by the MPSC, provides natural gas service to approximately 285,000 customers in Michigan's Upper and Lower Peninsulas.
- The "ENSTAR" segment (including the activities of SEMCO's APC and CINGSA subsidiaries), which is subject to regulation by the RCA, provides natural gas service to approximately 132,000 customers in Anchorage, Alaska and the surrounding areas.

SEMCO has operations and investments in other businesses, including propane distribution, intrastate natural gas pipelines and natural gas storage facilities in Michigan. Under current accounting guidance on segment reporting, these businesses do not meet the quantitative thresholds required to be reportable business segments and are combined and included with SEMCO's corporate division in a category the Company refers to as "Corporate and Other".

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NOTE 9 – BUSINESS SEGMENTS (Continued)

SEMCO's corporate division is a cost center rather than a business segment. Any corporate operating expenses that do not relate to the ongoing operations of SEMCO's business segments or are not allocable to them under various regulatory rules are not allocated to those segments. Instead, these unallocated expenses remain on the books of the SEMCO's corporate division. SEMCO's corporate division is included in Corporate and Other.

SEMCO Holding files a consolidated federal income tax return which is allocated among its subsidiaries and divisions whose results are part of the consolidated federal income tax return based on their separate taxable income.

The following table provides business segment information as well as a reconciliation of the segment information to the applicable line in the Consolidated Financial Statements:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
	(in thousands)			
Operating Revenues (b)				
SEMCO Gas	\$ 33,315	\$ 32,597	\$ 224,080	\$ 207,065
ENSTAR	34,327	35,209	194,930	178,442
Corporate and other	1,198	1,066	5,325	4,315
Corporate - intercompany eliminations (a)	(76)	(71)	(222)	(207)
Total Operating Revenue	<u>\$ 68,764</u>	<u>\$ 68,801</u>	<u>\$ 424,113</u>	<u>\$ 389,615</u>
Net Income (Loss) Attributable to Semco Holding Corporation (b)				
SEMCO Gas	\$ (1,844)	\$ (1,419)	\$ 14,347	\$ 9,903
ENSTAR	524	(1,532)	7,749	4,342
Corporate and other (a)	(602)	(1,019)	(4,782)	(2,942)
Total Operating Income (Loss)	<u>\$ (1,922)</u>	<u>\$ (3,970)</u>	<u>\$ 17,314</u>	<u>\$ 11,303</u>

(a) Represents the elimination of intercompany gas distribution revenue.

(b) The Company has no international operating revenues or net income.

Semco Holding Corporation
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NOTE 10 – RECONCILIATION OF FINANCIAL INFORMATION

These historical financials statements are presented in accordance with US GAAP. The following tables provide a reconciliation of the historical condensed financial information to Canadian generally accepted accounting principles (“C-GAAP”).

Semco Holding Corporation
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
(Unaudited)

		At September 30, 2011		
	Explanatory Notes Below	US GAAP	Effect of Transition	C-GAAP
			to C-GAAP	
(in thousands)				
Current Assets				
Cash and cash equivalents	1	\$ 13,697	\$ 550	\$ 14,247
Restricted cash		7,157	-	7,157
Receivables, less allowances	1	17,773	311	18,084
Accrued revenue		14,005	-	14,005
Gas in underground storage, at average cost		57,196	-	57,196
Prepaid expenses		7,268	-	7,268
Deferred income taxes		5,395	-	5,395
Materials and supplies, at average cost	1	6,044	97	6,141
Regulatory assets		2,395	-	2,395
Other		1,367	-	1,367
		<u>132,297</u>	<u>958</u>	<u>133,255</u>
Property, Plant and Equipment, Net	1	722,299	22,426	744,725
Deferred Charges and Other Assets				
Goodwill		204,472	-	204,472
Regulatory assets	3	86,311	(22,597)	63,714
Investment in unconsolidated affiliate	1	22,762	(22,762)	-
Unamortized debt expense	2	5,765	(5,765)	-
Other	3	7,389	(1,368)	6,021
		<u>326,699</u>	<u>(52,492)</u>	<u>274,207</u>
Total Assets		<u>\$ 1,181,295</u>	<u>\$ (29,108)</u>	<u>\$ 1,152,187</u>

NOTE 10 – RECONCILIATION OF FINANCIAL INFORMATION (Continued)

		At September 30, 2011		
			Effect of	
	Explanatory	US GAAP	Transition	C-GAAP
	Notes Below		to C-GAAP	
			(in thousands)	
Current Liabilities				
Current maturities of long-term debt and capital lease		\$ 4	\$ -	\$ 4
Notes payable		73,000	-	73,000
Accounts payable	1	38,190	437	38,627
Customer deposits and advance payments		25,158	-	25,158
Regulatory liabilities		3,602	-	3,602
Accrued interest		7,138	-	7,138
Other	1	548	39	587
		<u>147,640</u>	<u>476</u>	<u>148,116</u>
Deferred Credits and Other Liabilities				
Regulatory liabilities	3	73,539	(24,215)	49,324
Deferred income taxes	3	82,465	100	82,565
Pension and other postretirement costs		32,567	-	32,567
Customer advances for construction		17,277	-	17,277
Other	1	21,630	146	21,776
		<u>227,478</u>	<u>(23,969)</u>	<u>203,509</u>
Long-Term Debt and Capital Lease	2	440,324	(5,765)	434,559
Equity				
Common shareholder's equity				
Capital Surplus		277,220	-	277,220
Accumulated comprehensive income (loss)	3	(155)	150	(5)
Retained earnings		65,688	-	65,688
		<u>342,753</u>	<u>150</u>	<u>342,903</u>
Non-controlling interest in a consolidated subsidiary		23,100		23,100
Total Equity		<u>365,853</u>	<u>150</u>	<u>366,003</u>
Total Liabilities and Equity		<u>\$ 1,181,295</u>	<u>\$ (29,108)</u>	<u>\$ 1,152,187</u>

Explanatory Notes:

- 1) *Accounting for Joint Ventures.* US GAAP requires the Company's investments in joint ventures to be accounted for using the equity method. Canadian GAAP requires that investments in joint ventures are proportionally consolidated. The different accounting treatment affects only the presentation and the classification and not earnings or shareholder's equity.
- 2) *Transaction Costs.* Under US GAAP, transaction costs arising from the issuance of debt are recorded as a non-current asset. For Canadian GAAP, these costs are classified in long-term debt.
- 3) *Pension Funding Status.* US GAAP requires an employer to recognize the overfunded or underfunded status of a defined benefit pension and other post-retirement plans as an asset or liability, while Canadian GAAP does not require the recognition of the defined benefit pension and other post-retirement plan funding status.

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NOTE 10 – RECONCILIATION OF FINANCIAL INFORMATION (Continued)

Semco Holding Corporation
CONSOLIDATED STATEMENT OF OPERATIONS
(Unaudited)

Explanatory Notes Below	Three months ended September 30, 2011			Nine months ended September 30, 2011		
	US GAAP	Effect of Transition to C-GAAP (in thousands)	C-GAAP	US GAAP	Effect of Transition to C-GAAP (in thousands)	C-GAAP
Operating revenues						
Gas sales	\$ 60,912	\$ -	\$ 60,912	\$ 393,552	\$ -	\$ 393,552
Gas transportation	4,608	-	4,608	18,101	-	18,101
Other	3,244	860	4,104	12,460	2,678	15,138
	<u>68,764</u>	<u>860</u>	<u>69,624</u>	<u>424,113</u>	<u>2,678</u>	<u>426,791</u>
Operating expenses						
Cost of gas sold	36,027	-	36,027	279,812	-	279,812
Operations and maintenance	19,953	98	20,051	62,622	323	62,945
Depreciation and amortization	8,681	161	8,842	26,033	483	26,516
Property and other taxes	2,933	35	2,968	9,219	104	9,323
	<u>67,594</u>	<u>294</u>	<u>67,888</u>	<u>377,686</u>	<u>910</u>	<u>378,596</u>
Operating income	<u>1,170</u>	<u>566</u>	<u>1,736</u>	<u>46,427</u>	<u>1,768</u>	<u>48,195</u>
Other income (deductions)						
Interest expense	(5,718)	-	(5,718)	(17,276)	-	(17,276)
Other	1,274	(516)	758	3,211	(1,536)	1,675
	<u>(4,444)</u>	<u>(516)</u>	<u>(4,960)</u>	<u>(14,065)</u>	<u>(1,536)</u>	<u>(15,601)</u>
Income before income taxes	<u>(3,274)</u>	<u>50</u>	<u>(3,224)</u>	<u>32,362</u>	<u>232</u>	<u>32,594</u>
Income tax (expense)	<u>1,352</u>	<u>(50)</u>	<u>1,302</u>	<u>(15,048)</u>	<u>(232)</u>	<u>(15,280)</u>
Net income	<u>\$ (1,922)</u>	<u>\$ -</u>	<u>\$ (1,922)</u>	<u>\$ 17,314</u>	<u>\$ -</u>	<u>\$ 17,314</u>
Less: Income attributable to a non-controlling interest	<u>231</u>	<u>-</u>	<u>231</u>	<u>393</u>	<u>-</u>	<u>393</u>
Net income available to common shareholder	<u>\$ (2,153)</u>	<u>\$ -</u>	<u>\$ (2,153)</u>	<u>\$ 16,921</u>	<u>\$ -</u>	<u>\$ 16,921</u>

Explanatory Notes:

- 1) *Accounting for Joint Ventures.* US GAAP requires the Company's investments in joint ventures to be accounted for using the equity method. Canadian GAAP requires that investments in joint ventures are proportionally consolidated. The different accounting treatment affects only the presentation and the classification and not earnings or shareholder's equity.

The following additional disclosure is a requirement of Canadian GAAP and not US GAAP.

Shareholder's Capital. As of September 30, 2011, the Company is authorized to issue 100 shares of voting common stock and 10 shares have been issued. These shares do not have any special attributes attached to them.

Common Stock:	
Par Value	\$0.01
Shares Authorized	100
Shares Outstanding	10

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NOTE 11 - SUBSEQUENT EVENTS

Under current accounting guidance, the Company is required to disclose events that occur after the balance sheet date but before financial statements are issued or are available to be issued. These are known as subsequent events. Subsequent events have been reviewed through February 1, 2012, the issuance date of these financial statements.

On October 15, 2011, the SEMCO Gas conveyed four MGP sites to a prior owner of the sites, pursuant to a settlement entered into in July 2011. SEMCO Gas continues to own three MGP sites where it is engaged in environmental investigation and, if necessary, remediation activities. Investigatory and remediation activities at one of the three sites may be the responsibility, in whole or in part, of another potentially responsible person.

In August 2011, ENSTAR sought RCA approval of an amendment to the November 2000 Unocal Contract. If approved, the amendment would permit Union Oil to deliver gas to ENSTAR at a new delivery point. ENSTAR is seeking RCA approval to recover the transportation costs associated with gas being delivered at this new delivery point in the GCR rate charged to customers. The RCA approved the amendment and GCR recovery of the transportation costs in an order dated October 26, 2011.

In a filing made in August 2011, ENSTAR asked the RCA to approve the recovery of storage-related costs in the GCR rate charged to ENSTAR's Alaska customers. As part of this filing and in compliance with a prior RCA order, ENSTAR also filed its contract with CINGSA with the RCA for approval. On October 26, 2011, the RCA approved the GCR cost recovery methodology proposed by ENSTAR and the CINGSA contract.

In November 2011, ENSTAR entered into an additional short term gas supply agreement with Union Oil (the "November 2011 Unocal Contract") for non-firm variable priced gas similar to the Cook Inlet Energy and Aurora Gas contracts. Deliveries under the November 2011 Unocal Contract are expected to begin in the winter of 2011-2012. Under an October 2011 ruling by the RCA, gas supply agreements with a term of less than a year for gas that will be purchased under ENSTAR's daily bidding system need not be filed for approval by the RCA. As a result, the cost of gas purchased under the November 2011 Unocal Contract is includable for recovery under ENSTAR's GCR mechanism.

In November 2011, CINGSA completed the terms of a \$90 million secured Construction and Term Loan Facility (the "CINGSA Facility") with RBC Capital Markets LLC as the lead arranger and administrative agent and two additional lenders. The CINGSA Facility is non-recourse to the joint venture partners and will have a four-year maturity. Loans under the CINGSA Facility, from the closing until the third anniversary date of the CINGSA Facility, may either be at LIBOR plus a margin of 2.25% or an Alternative Base Rate, as defined in the CINGSA Facility plus a margin of 1.25%. Commencing on the third anniversary date of the CINGSA Facility, the margin on LIBOR and the Alternative Base Rate loans will increase to 2.50% and 1.50%, respectively. The proceeds from the CINGSA Facility will be used to fund 50% of the anticipated \$180 million CINGSA Storage Project costs.

There were no other subsequent events requiring an adjustment to or disclosure in the Company's Consolidated Financial Statements.

ALTAGAS LTD. PRO FORMA FINANCIAL STATEMENTS

ALTAGAS LTD

Unaudited pro forma consolidated balance sheet As at September 30, 2011

(\$000s CAD)	AltaGas	SEMCO (1)	Pro forma Adjustments	Notes to the Pro forma Statements	Pro forma Consolidated
ASSETS					
Current Assets					
Cash and cash equivalents	2,946	14,934	(14,934)	3.a	2,946
Accounts receivable	221,831	18,956			240,787
Inventory	7,873	66,390			74,263
Restricted cash	19,470	7,502			26,972
Regulatory assets	682	2,510			3,192
Risk management	45,576				45,576
Prepaid expense and other current assets	6,248	23,731			29,979
	304,626	134,023	(14,934)		423,715
Capital assets					
Energy arrangements, contracts and relationships	2,157,707	780,621	102,807	3.b	3,041,135
Goodwill	204,505				204,505
Regulatory assets	199,497	214,327	231,307	3.c	645,131
Risk management	87,119	66,785			153,904
Risk management	19,093				19,093
Long-term investments and other assets	15,080	6,311			21,391
	2,987,627	1,202,067	319,180		4,508,874
LIABILITIES & SHAREHOLDERS' EQUITY					
Current Liabilities					
Accounts payable and accrued liabilities	270,286	40,489	6,289	3.d	317,064
Dividends payable	9,222				9,222
Short-term debt	2,662	76,519	(76,519)	3.e	2,662
Current portion of long-term debt	101,593	4	(4)	3.e	101,593
Customer deposits	23,057	26,371			49,428
Regulatory liabilities	1,785	3,776			5,561
Risk management	54,352				54,352
Other current liabilities	8,681	8,098			16,779
	471,638	155,256	(70,234)		556,660
Long-term debt					
Asset retirement obligations	948,028	455,505	424,707	3.f	1,828,240
Future income taxes	41,145	7,493			48,638
Regulatory liabilities	242,308	80,890	(1,572)	3.d	321,626
Risk management	20,059	51,701			71,760
Risk management	19,155				19,155
Other long-term liabilities	28,821	33,442			62,263
Future employee obligations	12,598	34,136			46,734
	1,783,752	818,424	352,902		2,955,078
Common shares					
Preferred shares	1,052,880	290,582	36,541	3.g	1,380,003
Contributed surplus	194,126				194,126
Accumulated other comprehensive income (loss)	4,955				4,955
Accumulated other comprehensive income (loss)	(10,320)	(5)	5	3.h	(10,320)
Accumulated earnings	(37,766)	68,854	(73,571)	3.d & 3.h	(42,483)
	1,203,875	359,430	(37,024)		1,526,281
Non controlling interest in a consolidated subsidiary					
		24,213	3,302	3.i	27,515
	2,987,627	1,202,067	319,180		4,508,874

- (1) Amounts have been translated from US dollars to Canadian dollars at the closing rate of exchange at September 30, 2011, which was 1.0482.

ALTAGAS LTD

Unaudited pro forma consolidated statement of income For the year ended December 31, 2010

(\$000s CAD except for share amounts)	AltaGas (2)	SEMCO (1 & 3)	Pro forma Adjustments	Notes to the Pro forma Statements	Pro forma Consolidated
REVENUE					
Operating	1,352,427	597,439			1,949,866
Unrealized loss on risk management	(1,337)				(1,337)
Other revenue	2,962	801			3,763
	<u>1,354,052</u>	<u>598,240</u>			<u>1,952,292</u>
EXPENSES					
Cost of sales	868,554	407,627			1,276,181
Operating and administrative	241,540	95,336			336,876
Accretion of asset retirement obligations	2,880				2,880
Amortization: capital assets	79,216	33,979			113,195
Amortization: energy arrangements, contracts and relationships	9,964				9,964
	<u>1,202,154</u>	<u>536,942</u>			<u>1,739,096</u>
Foreign exchange loss	67				67
Interest expense					
Short-term debt	1,533	1,253	(1,253)	3.j	1,533
Long-term debt	47,309	22,553	10,534	3.k	80,396
Income before income taxes	102,989	37,491	(9,281)		131,200
Income tax (expense) recovery					
Current income tax	222	(3,723)	2,320	3.l	(1,181)
Future income tax	(1,949)	(11,940)			(13,889)
NET INCOME	<u>101,262</u>	<u>21,829</u>	<u>(6,961)</u>		<u>116,130</u>
Non controlling interest		59			59
Preferred shares dividends (net of tax)	4,038				4,038
NET INCOME APPLICABLE TO COMMON SHARES	<u>97,224</u>	<u>21,770</u>	<u>(6,961)</u>		<u>112,033</u>
Weighted average number of shares (thousands)					
basic	81,512		12,100		93,612
diluted	81,891		12,100		93,991
Net income per share					
basic	1.19				1.20
diluted	1.19				1.19

- (1) Amounts have been translated from US dollars to Canadian dollars using average rate of exchange for the year, which was 1.0299.
- (2) This statement of income does not reflect any earnings from the Pacific Natural Gas (PNG) assets, which were acquired in a separate business acquisition by AltaGas on December 20, 2011.
- (3) This statement of income does not reflect any earnings from the CINGSA assets (see note 3.b).

ALTAGAS LTD

Unaudited pro forma consolidated statement of income For the nine months ended September 30, 2011

(\$000s CAD except for share amounts)	AltaGas (2)	SEMCO (1 & 3)	Pro forma Adjustments	Notes to the Pro forma Statements	Pro forma Consolidated
REVENUE					
Operating	1,164,673	417,530			1,582,203
Unrealized loss on risk management	(15,514)				(15,514)
Other revenue	(8,039)	1,639			(6,400)
	<u>1,141,120</u>	<u>419,168</u>			<u>1,560,288</u>
EXPENSES					
Cost of sales	771,797	273,740			1,045,537
Operating and administrative	191,140	70,700			261,840
Accretion of asset retirement obligations	1,824				1,824
Amortization: capital assets	58,137	25,941			84,078
Amortization: energy arrangements, contracts and relationships	7,606				7,606
	<u>1,030,504</u>	<u>370,380</u>			<u>1,400,884</u>
Foreign exchange loss	77				77
Interest expense					
Short-term debt	4,360	772	(772)	3.m	4,360
Long-term debt	35,027	16,129	6,523	3.n	57,679
Income before income taxes	71,152	31,887	(5,751)		97,288
Income tax (expense) recovery					
Current income tax	(797)	(10,266)	1,438	3.o	(9,626)
Future income tax	(8,406)	(4,682)			(13,088)
NET INCOME	<u>61,949</u>	<u>16,938</u>	<u>(4,313)</u>		<u>74,574</u>
Non controlling interest		<u>384</u>			<u>384</u>
Preferred share dividends (net of tax)	8,250				8,250
NET INCOME APPLICABLE TO COMMON SHARES	<u>53,699</u>	<u>16,554</u>	<u>(4,313)</u>		<u>65,940</u>
 Weighted average number of shares (thousands)					
basic	83,188		12,100		95,288
diluted	84,242		12,100		96,342
 Net income per share					
basic	0.65				0.69
diluted	0.64				0.68

- (1) Amounts have been translated from US dollars to Canadian dollars using average rate of exchange for the period, which was 0.9783.
- (2) This statement of income does not reflect any earnings from the Pacific Natural Gas (PNG) assets, which were acquired in a separate business acquisition by AltaGas on December 20, 2011.
- (3) This statement of income does not reflect any earnings from the CINGSA assets (see note 3.b).
- (4) This statement of income does not reflect contributions of a fourth quarter which is typically strong as operating income in the Utility business is highly seasonal. Revenues are primarily based on the demand for space heating in the winter months, mainly from November to March. Costs, on the other hand, are generally incurred more uniformly over the year. This results in stronger first and fourth quarters and weaker second and third quarters.

ALTAGAS LTD

NOTES TO THE UNAUDITED PRO FORMA CONSOLIDATED FINANCIAL STATEMENTS

**As at and for the nine months ended September 30, 2011
and for the year ended December 31, 2010
(In thousands of Canadian Dollars unless otherwise indicated)**

1. Acquisition of SEMCO Holding Corporation

AltaGas Ltd. ("AltaGas" or the "Corporation") and a wholly-owned subsidiary of AltaGas have entered into a definitive agreement (the "Agreement") with Continental Energy Systems LLC ("Continental") and SEMCO Holding Corporation ("SEMCO") to acquire 100% of SEMCO for approximately US \$1,135 million, including approximately US \$355 million in assumed debt (the "Acquisition"). SEMCO is the sole shareholder of SEMCO Energy, Inc. a privately held regulated public utility company headquartered in Port Huron, Michigan with natural gas distribution operations in Alaska and Michigan. SEMCO is currently developing the Cook Inlet Natural Gas Storage Alaska, in-field storage facility in the Cook Inlet area of Alaska ("CINGSA" or "CINGSA assets").

The transaction is subject to customary approvals including regulatory approvals from the Michigan Public Service Commission, the Regulatory Commission of Alaska and the United States Federal Trade Commission and Department of Justice under the Hart-Scott-Rodino Antitrust Improvements Act of 1976. The regulatory approval process is expected to take approximately six months and AltaGas expects the Acquisition to close in the third quarter, 2012.

Funding for the Acquisition is expected to be provided from a combination of equity and debt, specifically:

- (i) the net proceeds from the \$350 million subscription receipt offering;
- (ii) and expected draws of approximately \$488 million on existing credit facilities available to the Corporation.

2. Basis of presentation

The accompanying unaudited pro forma consolidated balance sheet at September 30, 2011, and unaudited pro forma consolidated statements of income for the nine months ended September 30, 2011 and the year ended December 31, 2010 (the "Pro forma Statements") have been prepared by management of AltaGas for inclusion in the short-form prospectus as described in note 1.

The Pro forma Statements have been prepared in accordance with Part V Pre-changeover accounting standards (Canadian GAAP) of the Canadian Institute of Chartered Accountants Handbook ("CICA"). The accounting policies used in the preparation of the Pro forma Statements are consistent with those described in the audited consolidated financial statements of AltaGas as at and for the year ended December 31, 2010. The Corporation is engaged in rate-regulated activities and, as permitted by the CICA Accounting Standards Board and Section 5.4 of National Instrument 52-107 "Acceptable Accounting Principles and Auditing Standards" has elected to defer the adoption of International Financial Reporting Standards for 2011. Accordingly, the accounting standards in Part V of the CICA Handbook have been applied in the preparation of the unaudited consolidated financial statements as at and for the nine months ended September 30, 2011 and for the year ended December 31, 2010.

The unaudited pro forma consolidated statements of income give effect to the Acquisition as if it had occurred on January 1, 2010. The unaudited pro forma consolidated balance sheet gives effect to the Acquisition as if it had occurred on September 30, 2011.

The Pro forma Statements have been prepared using the following information:

- a) Audited consolidated financial statements of AltaGas Ltd. as at and for the year ended December 31, 2010;
- b) Audited consolidated financial statements of SEMCO Holding Corporation as at and for the year ended December 31, 2010;
- c) Unaudited consolidated financial statements of AltaGas Ltd. as at and for the nine months ended September 30, 2011;
- d) Unaudited consolidated financial statements of SEMCO Holding Corporation as at and for the nine months ended September 30, 2011;
- e) Such other supplementary information as was considered necessary to reflect the SEMCO Acquisition and related financing in the Pro forma Statements.

The financial statements of SEMCO identified in b) and d) above are prepared in accordance with accounting principles generally accepted in the United States ("US GAAP"). However, note 13 to the audited financial statements of SEMCO for the year ended December 31, 2010 and note 10 to the unaudited financial statements of SEMCO as at and for the nine months ended September 30, 2011 provide reconciliations to Canadian GAAP and these Canadian GAAP amounts have been reflected in the Pro forma Statements.

SEMCO unaudited consolidated financial statements are presented in US dollars. The financial information of SEMCO within the Pro forma Statements are reported in Canadian dollars. SEMCO assets and liabilities were translated to Canadian dollars at the rate of exchange at September 30, 2011. Revenue and expenses were translated to Canadian dollars at the average rate of exchange for the period. Exchange gains and losses have been included in accumulated other comprehensive income.

The Pro forma Statements do not include the anticipated financial benefits from such items as potential cost savings or synergies arising from the Acquisition, nor are they necessarily indicative of the results of operations or financial position that would have occurred had the Acquisition been effected on the dates indicated, or the results that may be obtained in the future.

The Pro forma Statements have been prepared for illustrative purpose only. Actual amounts recorded once the purchase price allocation is finalized will depend on a number of factors and may differ materially from those recorded in these Pro forma Statements.

3. Pro forma adjustments

The Acquisition will be accounted for using the purchase method of accounting. Accordingly, the acquired business' identifiable assets and liabilities are recorded at their fair values.

Management's preliminary assessment of the net assets acquired and liabilities assumed and the preliminary purchase price allocation are subject to change due to changes in the fair values of the respective assets and liabilities at the closing date of the Acquisition. These changes will be not known until after the closing date of the Acquisition and may differ materially from the amounts recorded in the Pro forma Statements.

The Pro forma Statements reflect the following adjustments:

Pro forma consolidated balance sheet at September 30, 2011:

- a) Cash and cash equivalents of SEMCO in the amount of \$14,934 were not acquired as they will be retained by the vendor prior to the closing;
- b) Capital assets have been increased by \$102,807 to reflect the estimated fair value of the CINGSA assets;
- c) Goodwill has been increased by \$231,307 to reflect the net replacement of SEMCO goodwill with the goodwill resulting from the Acquisition;
- d) Recognition of estimated Acquisition-related pre-tax costs for \$6,289 and the related deferred income tax adjustment for \$1,571 to reflect the tax effect at the statutory rate of 25%;
- e) Current portion of long-term debt of \$4 and short-term debt for \$76,519 were not acquired as they will be retired by the vendor prior to the closing of the Acquisition;
- f) The net increase in long-term debt of \$424,707 is a reflection of:
 - i. \$141,612 SEMCO long-term debt not assumed;
 - ii. The assumption of \$78,615 of incremental debt expected to be assumed by the date of Acquisition related to the construction of the CINGSA assets; and
 - iii. Borrowings under AltaGas' senior unsecured credit facilities in the amount of \$487,704.
- g) Common shares have been increased by \$327,123 to reflect the net proceeds from the issuance of new common shares upon exchange of subscription receipts, as described in note 1, and reduced by \$290,582 to cancel the outstanding SEMCO common shares;
- h) SEMCO accumulated other comprehensive loss of \$5 and accumulated earnings of \$68,854 have been eliminated;
- i) Non-controlling interest in a SEMCO subsidiary has been increased by \$3,302 to reflect the estimated fair value of non-controlling interest in CINGSA.

Pro forma consolidated statement of income for the year ended December 31, 2010:

- j) Interest expense has been decreased by \$1,253 to reflect the interest related to the SEMCO short-term debt not assumed as outlined in note 3.e.
- k) Interest expense has been increased by \$13,769 to reflect the interest related to long-term debt outlined in note f.(ii) and f.(iii) with a weighted average interest rate estimated to be 2.37% and reduced by \$3,235 to reflect the interest related to the SEMCO debt not assumed;
- l) Income tax recovery of \$2,320 to reflect the tax effect on the pro forma adjustments at the statutory rate of 25%.

Pro forma consolidated statement of income for the nine months ended September 30, 2011

- m) Interest expense has been decreased by \$772 to reflect the interest related to the SEMCO short-term debt not assumed as outlined in note 3.e.
- n) Interest expense has been increased by \$8,796 to reflect the interest related to long-term debt outlined in note f.(ii) and f.(iii) with a weighted average interest rate estimated to be 2.37% and decreased by \$2,273 to reflect the interest related to the SEMCO debt not assumed;
- o) Income tax recovery of \$1,438 to reflect the tax effect on the pro forma adjustments at the statutory rate of 25%.

CERTIFICATE OF THE CORPORATION

Dated: February 14, 2012

This short form prospectus, together with the documents incorporated by reference, constitutes full, true and plain disclosure of all material facts relating to the securities offered by this short form prospectus as required by the securities legislation of each of the provinces of Canada.

ALTAGAS LTD.

(signed) David W. Cornhill
Chief Executive Officer

(signed) Deborah S. Stein
Chief Financial Officer

ON BEHALF OF THE BOARD OF DIRECTORS

(signed) M. Neil McCrank
Director

(signed) Robert B. Hodgins
Director

CERTIFICATE OF THE UNDERWRITERS

Dated: February 14, 2012

To the best of our knowledge, information and belief, this short form prospectus, together with the documents incorporated by reference, constitutes full, true and plain disclosure of all material facts relating to the securities offered by this short form prospectus as required by the securities legislation of each of the provinces of Canada.

BMO NESBITT BURNS INC.

RBC DOMINION SECURITIES
INC.

TD SECURITIES INC.

By: (signed) Sean M. Brown

By: (signed) Trevor Gardner

By: (signed) Alec W.G. Clark

CIBC WORLD MARKETS INC.

NATIONAL BANK
FINANCIAL INC.

SCOTIA CAPITAL INC.

By: (signed) Kelsen Vallee

By: (signed) Iain Watson

By: (signed) Cameron Goldade

HSBC SECURITIES (CANADA) INC.

MACQUARIE CAPITAL MARKETS
CANADA LTD.

By: (signed) Greg Gannett

By: (signed) Paul Huebener

BEACON SECURITIES
LIMITED

FIRSTENERGY CAPITAL
CORP.

PETERS & CO. LIMITED

By: (signed) Daniel Holland

By: (signed) Erik B. Bakke

By: (signed) Blair Ward

Press Release Dated April 13, 2012

Exhibit DSS - 3

ALTAGAS LTD. CLOSSES \$200 MILLION MEDIUM-TERM NOTE OFFERING

Calgary, Alberta (April 13, 2012)

AltaGas Ltd. (AltaGas) (TSX: ALA, ALA.PR.A, ALA.R) today announced that it has completed its \$200 million issue of senior unsecured medium-term notes (the Offering). The notes carry a coupon rate of 4.07 percent and mature on June 1, 2020.

The net proceeds resulting from the issuance of the notes will be used by AltaGas to reduce outstanding indebtedness and for general corporate purposes. The unsecured medium-term notes are rated BBB by both Standard & Poor's Rating Services and DBRS Limited.

The offering is being made through a syndicate of investment dealers co-led by BMO Capital Markets and National Bank Financial Inc. under AltaGas' Short Form Base Shelf Prospectus dated December 7, 2011 and Prospectus Supplement dated April 9, 2012.

AltaGas is an energy infrastructure business with a focus on natural gas, power and regulated utilities. AltaGas creates value by acquiring, growing and optimizing its energy infrastructure, including a focus on renewable energy sources. For more information visit: www.altagas.ca.

Investment Community
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investor.relations@altagas.ca

Media
(403) 691-9873
media.relations@altagas.ca

This news release contains forward-looking statements. When used in this news release, the words "may", "would", "could", "will", "intend", "plan", "anticipate", "believe", "seek", "propose", "estimate", "expect", and similar expressions, as they relate to AltaGas or an affiliate of AltaGas, are intended to identify forward-looking statements. In particular, this news release contains forward-looking statements with respect to, among other things, the use of proceeds from the Offering. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. Such statements reflect AltaGas' current views with respect to future events based on certain material factors and assumptions and are subject to certain risks and uncertainties, including without limitation, changes in market, competition, governmental or regulatory developments, general economic conditions and other factors set out in AltaGas' public disclosure documents. Many factors could cause AltaGas' actual results, performance or achievements to vary from those described in this news release, including without limitation those listed above. These factors should not be construed as exhaustive. Should one or more of these risks or uncertainties materialize, or should assumptions underlying forward-looking statements prove incorrect, actual results may vary materially from those described in this news release as intended, planned, anticipated, believed, sought, proposed, estimated or expected, and such forward-looking statements included in this news release, should not be unduly relied upon. Such statements speak only as of the date of this news release. AltaGas does not intend, and does not assume any obligation, to update these forward-looking statements except as required by law. The forward-looking statements contained in this news release are expressly qualified by this cautionary statement.