EL PASO NATURAL GAS COMPANY, L.L.C.

CONSOLIDATED FINANCIAL STATEMENTS
With Independent Auditor's Reports

As of December 31, 2012 and 2011,
for the periods of January 1, 2012 to May 24, 2012,
May 25, 2012 to December 31, 2012 and
the year ended December 31, 2011

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EL PASO NATURAL GAS COMPANY, L.L.C.

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Report of Independent Auditors

To the Member and Management of El Paso Natural Gas Company, L.L.C.

In our opinion, the accompanying consolidated statements of income and comprehensive income, of member's equity and of cash flows for the period from January 1, 2012 to May 24, 2012, present fairly, in all material respects, the results of operations and cash flows of El Paso Natural Gas Company, L.L.C. and its subsidiaries (the "Predecessor Company") for the period from January 1, 2012 to May 24, 2012, in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Predecessor Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit 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 audit provide a reasonable basis for our opinion. The financial statements of the Predecessor Company as of December 31, 2011 and for the year then ended were audited by other auditors whose report dated February 27, 2012 expressed an unqualified opinion on those statements.

As discussed in Note 2 to the consolidated financial statements, in connection with the acquisition of El Paso Corporation by Kinder Morgan, Inc., a new basis of accounting was established as of May 25, 2012.

PricewaterhouseCoopers LLP

April 26, 2013

Independent Auditor's Report

To the Member and Management of El Paso Natural Gas Company, L.L.C.

We have audited the accompanying consolidated financial statements of El Paso Natural Gas Company, L.L.C. and its subsidiaries (the "Successor Company"), which comprise the consolidated balance sheet as of December 31, 2012 and the related consolidated statements of income and comprehensive income, of member's equity and of cash flows for the period from May 25, 2012 to December 31, 2012.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on the consolidated financial statements based on our audit. We conducted our audit 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Successor Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Successor Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of El Paso Natural Gas Company, L.L.C. and its subsidiaries at December 31, 2012 and the results of their operations and their cash flows for the period from May 25, 2012 to December 31, 2012 in accordance with accounting principles generally accepted in the United States of America.

PricewaterhouseCoopers LLP, 1201 Louisiana, Suite 2900, Houston, TX 77002
T: (713) 356 4000, F: (713) 356 4717, www.pwc.com/us

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Emphasis of Matter

As discussed in Note 2 to the **c**onsolidated financial statements, in connection with the acquisition of El Paso Corporation by Kinder Morgan, Inc., a new basis of accounting was established as of May 25, 2012. Our opinion is not modified with respect to this matter.

PricewaterhouseCoopers LLP

April 26, 2013

EL PASO NATURAL GAS COMPANY, L.L.C.

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(In Millions)

	Successor	Predecessor	
	Period from Acquisition May 25, 2012 to December 31, 2012	Period from January 1, 2012 to May 24, 2012	Year Ended December 31, 2011
Revenues	$ 301	$ 190	$ 509
Operating Costs and Expenses			
Operation and maintenance	113	80	206
Depreciation and amortization	54	33	92
Taxes, other than income taxes	17	13	31
Total Operating Costs and Expenses	184	126	329
Operating Income	117	64	180
Other Income (Expense)			
Other income, net	2	1	2
Interest expense	(53)	(35)	(88)
Affiliated interest income, net	7	9	17
Total Other Expense	(44)	(25)	(69)
Income Before Income Taxes	73	39	111
Income Tax Expense	(1)	(15)	(42)
Net Income	72	24	69
Other Comprehensive Income			
Adjustments to postretirement benefit plan liabilities (net of income tax expense of $0 during January 1 to May 24, 2012, $0 during May 25 to December 31, 2012 and $3 in 2011)	9	—	3
Comprehensive Income	$ 81	$ 24	$ 72

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

EL PASO NATURAL GAS COMPANY, L.L.C.

CONSOLIDATED BALANCE SHEETS
(In Millions, Except Share Amounts)

	Successor December 31, 2012	Predecessor December 31, 2011
ASSETS		
Current assets		
Cash and cash equivalents	$ 9	$ —
Accounts receivable, net	46	30
Inventories	45	48
Deferred income taxes	—	12
Prepaids	16	16
Regulatory assets	6	8
Other	2	—
Total current assets	124	114
Property, plant and equipment, net	2,325	2,468
Goodwill	564	—
Note receivable from affiliate	—	873
Regulatory assets	63	56
Deferred charges and other assets	283	45
Total Assets	$ 3,359	$ 3,556
LIABILITIES AND MEMBERS' EQUITY		
Current liabilities		
Accounts payable	$ 24	$ 97
Accrued taxes	5	35
Accrued interest	21	19
Regulatory liabilities	9	16
Contractual deposits	11	21
Accrued other current liabilities	23	35
Total current liabilities	93	223
Long-term liabilities and deferred credits		
Long-term debt	1,115	1,113
Debt fair value adjustments	237	—
Deferred income taxes	—	439
Other long-term liabilities and deferred credits	171	78
Total long-term liabilities and deferred credits	1,523	1,630
Total Liabilities	1,616	1,853
Commitments and contingencies (Note 9)		
Members' equity		
Common stock, par value $1 per share; 1,000 shares authorized, issued and outstanding	—	—
Additional paid-in capital	—	1,268
Retained earnings	—	432
Members' equity	1,734	—
Accumulated other comprehensive income	9	3
Total Members' Equity	1,743	1,703
Total Liabilities and Members' Equity	$ 3,359	$ 3,556

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

EL PASO NATURAL GAS COMPANY, L.L.C.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(In Millions)

	Successor	Predecessor	
	Period from Acquisition May 25, 2012 to December 31, 2012	Period from January 1, 2012 to May 24, 2012	Year Ended December 31, 2011
Cash Flows From Operating Activities			
Net income	$ 72	$ 24	$ 69
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	54	33	92
Deferred income tax expense	1	15	21
Other	3	(3)	13
Changes in components of working capital:			
Accounts receivable	(25)	10	1
Accounts payable	(13)	(20)	(20)
Accrued taxes	(37)	—	(3)
Other, net	(12)	(5)	19
Other long-term assets and liabilities	10	50	29
Net Cash Provided by Operating Activities	53	104	221
Cash Flows From Investing Activities			
Capital expenditures	(41)	(27)	(88)
Net change in note receivable from affiliate	56	(3)	(37)
Other	(2)	—	7
Net Cash Provided by (Used in) Investing Activities	13	(30)	(118)
Cash Flows From Financing Activities			
Distributions to members	(71)	(60)	(103)
Net Cash Used in Financing Activities	(71)	(60)	(103)
Net Increase (Decrease) in Cash and Cash Equivalents	(5)	14	—
Cash and Cash Equivalents, beginning of period	14	—	—
Cash and Cash Equivalents, end of period	$ 9	$ 14	$ —
Supplemental Cash Flow Information			
Cash paid during the period for interest (net of capitalized interest)	$ 54	$ 29	$ 83
Income tax payments	53	—	23

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

EL PASO NATURAL GAS COMPANY, L.L.C.

CONSOLIDATED STATEMENTS OF MEMBERS' EQUITY
(In Millions, except share amounts)

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Stockholder's Equity	Members' Equity	Accumulated Other Comprehensive Income	Total Members' Equity
Predecessor									
Balance at December 31, 2010	1,000	$ —	$ 1,268	$ 466	$ —	$ 1,734	$ —	$ —	$ —
Net income				69		69			
Dividend paid to parent				(103)		(103)			
Other comprehensive income					3	3			
Balance at December 31, 2011	1,000	—	1,268	432	3	1,703	—	—	—
Net income				24		24			
Dividend paid to parent				(60)		(60)			
Balance at May 24, 2012	1,000	$ —	$ 1,268	$ 396	$ 3	$ 1,667	$ —	$ —	$ —
Successor									
Balance at May 25, 2012	1,000	$ —	$ 2,175	$ —	$ —	$ 2,175	$ —	$ —	$ —
May 25, 2012 to July 31, 2012:									
Net income				4		4			
Other comprehensive income					1	1			
Conversion to limited liability company	(1,000)		(2,175)	(4)	(1)	(2,180)	2,179	1	2,180
August 1, 2012 to December 31, 2012:									
Net income							68		68
Other comprehensive income								8	8
Dividends paid to members							(71)		(71)
Non-cash distribution to members (Note 8)							(442)		(442)
Balance at December 31, 2012	—	$ —	$ —	$ —	$ —	$ —	$ 1,734	$ 9	$ 1,743

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

EL PASO NATURAL GAS COMPANY, L.L.C.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. General

We are a Delaware limited liability company, originally formed in 1928 as a corporation. Effective May 25, 2012, Kinder Morgan, Inc. (KMI) completed the acquisition of El Paso Corporation (our former parent, hereafter referred to as El Paso). We converted our legal structure to a limited liability company on August 1, 2012 and changed our name to El Paso Natural Gas Company, L.L.C. On August 1, 2012, Kinder Morgan Energy Partners, L.P. (KMP), a master limited partnership, acquired a 50% interest in us from KMI, with KMI retaining the remaining 50% ownership interest. KMP is controlled by its general partner, Kinder Morgan G.P., Inc., a wholly owned subsidiary of KMI. When we refer to “us,” “we,” “our,” “ours,” “the company,” or “EPNG” we are describing El Paso Natural Gas Company, L.L.C. and/or our subsidiaries.

Our primary business consists of the interstate transportation and storage of natural gas. We are the sole owner of (i) the EPNG natural gas pipeline system and (ii) the Mojave Pipeline Company, L.L.C., the sole owner of the Mojave natural gas pipeline system. The EPNG system consists of approximately 10,200 miles of pipeline with a design capacity of 5.65 billion cubic feet per day for natural gas. The Mojave system consists of approximately 500 miles of pipeline with a design capacity of 400 million cubic feet per day. In addition to our two pipeline systems, we utilize our Washington Ranch underground natural gas storage facility located in New Mexico to manage transportation needs and to offer interruptible storage services. This storage facility has up to 44 billion cubic feet of underground working natural gas storage capacity.

On March 1, 2013, KMP acquired the remaining 50% interest in us from KMI and we became an indirect wholly owned subsidiary of KMP. Management has evaluated subsequent events through April 26, 2013, the date the financial statements were available to be issued.

2. Summary of Significant Accounting Policies

Basis of Presentation

We have prepared our accompanying consolidated financial statements in accordance with the accounting principles contained in the Financial Accounting Standards Board's Accounting Standards Codification, the single source of generally accepted accounting principles in the United States of America (GAAP) and referred to in this report as the Codification. Under such rules and regulations, all significant intercompany items have been eliminated in consolidation. Additionally, certain amounts from prior years have been reclassified to conform to the current presentation. In this report, we refer to the Financial Accounting Standards Board as the FASB and the FASB Accounting Standards Codification as the Codification.

On May 25, 2012, our senior unsecured notes and debentures were deregistered with the United States Securities and Exchange Commission (SEC) and our reporting obligation to the SEC was terminated.

Business Combination Accounting

KMI's May 25, 2012 acquisition of El Paso was accounted for by KMI using business combination accounting. Under this method, the purchase price paid by the acquirer is allocated to the assets acquired and liabilities assumed as of the acquisition date based on their fair value. By the application of “push-down” accounting, our assets, liabilities and equity were accordingly adjusted to fair value on May 25, 2012. Determining the fair value of certain assets and liabilities assumed is judgmental in nature and often involves the use of significant estimates and assumptions. See Note 3 for a discussion of the estimated fair values of assets and liabilities recorded in connection with KMI's acquisition of El Paso.

Due to the application of “push-down” accounting, our financial statements and certain footnote disclosures are presented in two distinct periods to indicate the application of two different bases of accounting. Periods prior to May 25, 2012 are identified herein as “Predecessor,” while the period subsequent to KMI’s acquisition of El Paso is identified as “Successor.” As a result of the change in the basis of accounting from historical cost to reflect KMI’s purchase cost, the financial statements for Predecessor periods are not comparable to the Successor period.

Principles of Consolidation

We consolidate entities when we have the ability to control or direct the operating and financial decisions of the entity or when we have a significant interest in the entity that gives us the ability to direct the activities that are significant to that entity. The determination of our ability to control, direct or exert significant influence over an entity involves the use of judgment.

Use of Estimates

Certain amounts included in or affecting our financial statements and related disclosures must be estimated, requiring us to make certain assumptions with respect to values or conditions which cannot be known with certainty at the time our financial statements are prepared. These estimates and assumptions affect the amounts we report for certain assets and liabilities, our revenues and expenses during the reporting period, and our disclosure of contingent assets and liabilities at the date of our financial statements. We evaluate these estimates on an ongoing basis, utilizing historical experience, consultation with experts and other methods we consider reasonable in the particular circumstances. Nevertheless, actual results may differ significantly from our estimates. Any effects on our business, financial position or results of operations resulting from revisions to these estimates are recorded in the period in which the facts that give rise to the revision become known.

In addition, we believe that certain accounting policies are of more significance in our financial statement preparation process than others. Below are the principal accounting policies we apply in the preparation of our consolidated financial statements.

Cash Equivalents

We consider short-term investments with an original maturity of less than three months to be cash equivalents.

Accounts Receivable

The amounts reported as "Accounts receivable, net" on our accompanying Consolidated Balance Sheets as of December 31, 2012 and 2011 primarily consist of $45 million and $27 million respectively, due from third party payors (unrelated entities). For information on receivables due to us from related parties, see Note 8.

We establish provisions for losses on accounts receivable and for natural gas imbalances due from shippers and operators if we determine that we will not collect all or part of the outstanding balance. We regularly review collectability and establish or adjust our allowance as necessary using the specific identification method. The allowance for doubtful accounts and related provision for bad debt expense was not significant for the years ended December 31, 2012 and 2011.

Inventories

Our inventories, which consist of materials and supplies, are valued at cost, and periodically reviewed for physical deterioration and obsolescence.

Natural Gas Imbalances

Natural gas imbalances occur when the amount of natural gas delivered from or received by a pipeline system differs from the scheduled amount of gas delivered or received. We value these imbalances due to or from shippers and operators at current index prices. Imbalances are settled in cash or made up in-kind, subject to the terms of the applicable Federal Energy Regulatory Commission (FERC) tariff. Imbalances due from others are reported in our Consolidated Balance Sheets as “Accounts receivable, net.” Imbalances owed to others are reported in our Consolidated Balance Sheets as “Accounts payable.” We classify all imbalances as current as we expect them to be settled within a year.

Property, Plant and Equipment

Our property, plant and equipment is recorded at its original cost of construction or, upon acquisition, at either the fair value of the assets acquired or the cost to the entity that first placed the asset in service. For constructed assets, we capitalize all construction-related direct labor and material costs, as well as indirect construction costs. Our indirect construction costs primarily include an interest and equity return component (as more fully described below) and labor and related costs of departments associated with supporting construction activities. The indirect capitalized labor and related costs are based upon estimates of time spent supporting construction projects.

We use the composite method to depreciate regulated property, plant and equipment. Under this method, assets with similar lives and characteristics are grouped and depreciated as one asset. The FERC-accepted depreciation rate is applied to the total cost of the group until the net book value equals the salvage value. For certain general plant, the asset is depreciated to zero. We re-evaluate depreciation rates each time we redevelop our transportation and storage rates to file with the FERC for an increase or decrease in rates. When property, plant and equipment is retired, accumulated depreciation and amortization is charged for the original cost of the assets in addition to the cost to remove, sell or dispose of the assets, less salvage value. We do not recognize gains or losses unless we sell or retire an entire operating unit, as determined by the FERC. We generally include gains or losses on dispositions of operating units in “Operation and maintenance” expense in our Consolidated Statements of Income and Comprehensive Income.

In the Predecessor period, our property balances included additional acquisition costs, which represented the excess purchase costs associated with a previous purchase business combination allocated to us. These costs were amortized on a straight-line basis and were not recoverable in our rates under FERC policies. See Note 5 for additional related information.

Also included in our property balances are base gas and working gas at our storage facilities. The unrecoverable portion of the base gas is depreciated over the facility’s useful life. We periodically evaluate natural gas volumes at our storage facilities for gas losses. When events or circumstances indicate a loss has occurred, we recognize a loss in our income statement or defer the loss as a regulatory asset on our balance sheets if deemed probable of recovery through future rates charged to customers.

We capitalize a carrying cost (an allowance for funds used during construction or AFUDC) on debt and equity funds related to the construction of long-lived assets. This carrying cost consists of a return on the investment financed by debt and a return on the investment financed by equity. The debt portion is calculated based on the average cost of debt. Interest costs capitalized are included as a reduction to “Interest and debt expense, net” on our Consolidated Statements of Income and Comprehensive Income. The equity portion is calculated based on the most recent FERC approved rate of return. Equity amounts capitalized are included in “Other income, net” on our Consolidated Statements of Income and Comprehensive Income. The amount of capitalized AFUDC was not significant for the periods presented in our accompanying Consolidated Statements of Income and Comprehensive Income.

Asset Retirement Obligations

We record liabilities for obligations related to the retirement and removal of long-lived assets used in our businesses. We record, as liabilities, the fair value of asset retirement obligations on a discounted basis when they are incurred and can be reasonably estimated, which is typically at the time the assets are installed or acquired. Amounts recorded for the related assets are increased by the amount of these obligations. Over time, the liabilities increase due to the change in their present value, and the initial capitalized costs are depreciated over the useful lives of the related assets. The liabilities are eventually extinguished when the asset is taken out of service.

We are required to operate and maintain our natural gas pipelines and storage systems, and intend to do so as long as supply and demand for natural gas exists, which we expect for the foreseeable future. Therefore, we believe that we cannot reasonably estimate the asset retirement obligation for the substantial majority of our natural gas pipeline system assets because these assets have indeterminate lives. We continue to evaluate our asset retirement obligations and future developments could impact the amounts we record. Our asset retirement obligations were not significant as of December 31, 2012 and 2011.

Asset Impairments

We evaluate our assets for impairment when events or circumstances indicate that their carrying values may not be recovered. These events include market declines that are believed to be other than temporary, changes in the manner in which we intend to use a long-lived asset, decisions to sell an asset or investment and adverse changes in the legal or business environment such as adverse actions by regulators. If an event occurs, which is a determination that involves judgment, we evaluate the recoverability of our carrying value based on the long-lived asset's ability to generate future cash flows on an undiscounted basis. If an impairment is indicated, or if we decide to sell a long-lived asset or group of assets, we adjust the carrying value of the asset downward, if necessary, to its estimated fair value.

Our fair value estimates are generally based on assumptions market participants would use, including market data obtained through the sales process or an analysis of expected discounted cash flows.

Goodwill

Goodwill represents the excess of the cost of an acquisition price over the fair value of acquired net assets and such amounts are reported separately as "Goodwill" on our Consolidated Balance Sheets. Our total goodwill, which resulted from the application of "push-down" accounting associated with KMI's acquisition of El Paso on May 25, 2012, was $564 million as of December 31, 2012. Goodwill cannot be amortized, but instead must be tested for impairment annually or on an interim basis if events or circumstances indicate that the fair value of the asset had decreased below its carrying value.

We perform our goodwill impairment test on May 31 of each year. We performed a qualitative assessment and determined there were no indicators of impairment during the period from the May 25, 2012 acquisition date to our May 31, 2012 impairment assessment date. Additionally, we determined no event indicating an impairment has occurred subsequent to May 31, 2012. See above "Business Combination Accounting" discussion and Note 3 for additional related information.

Revenue Recognition

Our revenues are primarily generated from natural gas transportation and storage services and include estimates of amounts earned but unbilled. We estimate these unbilled revenues based on contract data, regulatory information, and preliminary throughput and allocation measurements, among other items. Revenues for all services are based on the thermal quantity of gas delivered or subscribed at a price specified in the contract. For our transportation services and storage services, we recognize reservation revenues on firm contracted capacity ratably over the contract period regardless of the amount of natural gas that is transported or stored. For interruptible or volumetric-based services, we record revenues when physical deliveries of natural gas are made at the agreed upon delivery point or when gas is injected or withdrawn from the storage facility. For contracts with step-up or step-down rate provisions that are not related to changes in levels of service, we recognize reservation revenues ratably over the contract life. We are subject to FERC regulations and, as a result, revenues we collect may be subject to refund in a rate proceeding. We establish reserves for these potential refunds. We had $94 million in reserves for potential refunds as of December 31, 2012 pursuant to the rate case settlements filed with FERC. See Note 13 for further discussion of our regulatory matters.

Environmental Matters

We expense or capitalize, as appropriate, environmental expenditures that relate to current operations. We expense expenditures that relate to an existing condition caused by past operations, which do not contribute to current or future revenue generation. We generally do not discount environmental liabilities to a net present value, and we record environmental liabilities when environmental assessments and/or remedial efforts are probable and we can reasonably estimate the costs. Generally, our recording of these accruals coincides with our completion of a feasibility study or our commitment to a formal plan of action. We recognize receivables for anticipated associated insurance recoveries when such recoveries are deemed to be probable.

We routinely conduct reviews of potential environmental issues and claims that could impact our assets or operations. These reviews assist us in identifying environmental issues and estimating the costs and timing of remediation efforts. We also routinely adjust our environmental liabilities to reflect changes in previous estimates. In making environmental liability estimations, we consider the material effect of environmental compliance, pending legal actions against us, and potential third-party liability claims. Often, as the remediation evaluation and effort progresses, additional information is obtained, requiring revisions to estimated costs. These revisions are reflected in our income in the period in which they are reasonably determinable. For more information on our environmental disclosures, see Note 9.

Legal

We are subject to litigation and regulatory proceedings as the result of our business operations and transactions. We utilize both internal and external counsel in evaluating our potential exposure to adverse outcomes from orders, judgments or settlements. When we identify specific litigation that is expected to continue for a significant period of time, is reasonably possible to occur, and may require substantial expenditures, we identify a range of possible costs expected to be required to litigate the matter to a conclusion or reach an acceptable settlement, and we accrue for such amounts. To the extent that actual outcomes differ from our estimates, or additional facts and circumstances cause us to revise our estimates, our earnings will be affected. In general, we expense legal costs as incurred and all recorded legal liabilities are revised as better information becomes available. For more information on our legal disclosures, see Note 9.

Other Contingencies

We recognize liabilities for other contingencies when we have an exposure that indicates it is both probable that a liability has been incurred and the amount of loss can be reasonably estimated. Where the most likely outcome of a contingency can be reasonably estimated, we accrue a liability for that amount. Where the most likely outcome cannot be estimated, a range of potential losses is established and if no one amount in that range is more likely than any other, the low end of the range is accrued.

Postretirement Benefits

We maintain a postretirement benefit plan covering certain of our former employees. The plan requires us to make contributions to fund the benefits to be paid out under the plan. These contributions are invested until the benefits are paid out to plan participants. The net benefit cost of this plan is recorded in our Consolidated Statements of Income and Comprehensive Income and is a function of many factors including benefits earned during the year by plan participants (which is a function of factors such as the level of benefits provided under the plan, actuarial assumptions and the passage of time), expected returns on plan assets and amortization of certain deferred gains and losses. For a further discussion of our policies with respect to our postretirement benefit plans, see Note 7.

In accounting for our postretirement benefit plan, we record an asset or liability based on the overfunded or underfunded status. Any deferred amounts related to unrecognized gains and losses or changes in actuarial assumptions are recorded on our Consolidated Balance Sheets as “Accumulated Other comprehensive income” until those gains or losses are recognized on the Consolidated Statements of Income and Comprehensive Income.

Income Taxes

Prior to KMI’s acquisition of El Paso, El Paso maintained a tax accrual policy to record both regular and alternative minimum taxes for companies included in its consolidated federal and state income tax returns. The policy provided, among other things, that (i) each company in a taxable income position would accrue a current expense equivalent to its federal and state income taxes, and (ii) each company in a tax loss position would accrue a benefit to the extent its deductions, including general business credits, could be utilized in the consolidated returns. El Paso paid all consolidated U.S. federal and state income taxes directly to the appropriate taxing jurisdictions and, under a separate tax billing agreement, El Paso could bill or refund its subsidiaries for their portion of these income tax payments. Prior to our conversion to a limited liability company which is further discussed below, we filed and paid taxes directly to certain state taxing authorities.

Effective August 1, 2012, we converted into a limited liability company and settled our current and deferred tax balances with El Paso with recoveries of our note receivable from KMI under its cash management program. Effective with KMP's acquisition of a 50% ownership interest in us from KMI on August 1, 2012, we are no longer subject to either federal income taxes or generally to state income taxes. See Notes 4 and 8 for further discussion of our income taxes.

Prior to our conversion date, we recorded current income taxes based on our taxable income and we provided for deferred income taxes to reflect estimated future tax payments and receipts. Deferred taxes represented the tax impacts of differences between the financial statement and tax bases of assets and liabilities and carryovers as of each year end. We accounted for tax credits under the flow-through method, which reduced the provision for income taxes in the year the tax credits first became available. We reduced deferred tax assets by a valuation allowance when, based on our estimates, it was more likely than not that a portion of those assets would not be realized in a future period. The estimates utilized in the recognition of deferred tax assets were subject to revision, either up or down, in future periods based on new facts or circumstances.

Regulated Operations

Our natural gas pipeline and storage operations are subject to the jurisdiction of the FERC and follow the FASB Accounting Standards Codification (ASC) 980 for Regulated Operations. Under ASC 980, we record regulatory assets and liabilities that would not be recorded for non-regulated entities. Regulatory assets and liabilities represent probable future revenues or expenses associated with certain charges or credits that are expected to be recovered from or refunded to customers through the rate making process. Items to which we apply regulatory accounting requirements include certain postretirement benefit plan costs, loss on reacquired debt, taxes related to an equity return component on regulated capital projects, and certain costs related to gas not used in operations and other costs included in, or expected to be included in, future rates. See Note 11 for additional information related to our regulatory assets and liabilities.

Recent Accounting Pronouncement

On July 27, 2012, the FASB issued Accounting Standards Update (ASU) No. 2012-02, "Intangibles-Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment." This ASU allows an entity the option to first assess qualitative factors to determine whether the existence of events and circumstances indicates that it is more likely than not (that is, a likelihood of more than 50%) that an indefinite-lived intangible asset other than goodwill is impaired. If, after this assessment, an entity concludes that it is not more likely than not that the indefinite-lived intangible asset is impaired, the entity is not required to take further action. However, if an entity concludes otherwise, then it is required to determine the fair value of the indefinite-lived intangible asset and perform the quantitative impairment test prescribed by current accounting principles. Moreover, an entity can bypass the qualitative assessment for any indefinite-lived intangible asset in any period and proceed directly to the quantitative impairment test, and then resume performing the qualitative assessment in any subsequent period. For us, ASU No. 2012-02 was effective January 1, 2013, and the adoption of this ASU is not expected to have a material impact on our consolidated financial statements.

3. KMI's Acquisition of El Paso

KMI's acquisition of El Paso was effective on May 25, 2012. The acquisition was accounted for using business combination accounting under applicable accounting principles. Business combination accounting requires, among other things, that assets acquired and liabilities assumed be recognized on the balance sheet at their fair values as of the acquisition date.

The table below represents management's estimate of the fair value of our tangible and intangible assets and liabilities as of May 25, 2012 (in millions).

Current assets	$ 100
Property, plant and equipment, net[1]	2,391
Goodwill[2]	564
Other noncurrent assets[3]	1,222
Long-term debt[4]	(1,363)
Deferred income taxes[5]	(410)
Other liabilities	(329)
Total purchase price	$ 2,175

(1) Property, plant and equipment includes a $49 million reduction to record our business at its regulatory value in conformity with our accounting policy.
(2) Goodwill of $0.6 billion represents the excess of consideration paid over the fair value of the assets acquired and liabilities assumed.
(3) Other non-current assets include a purchase price adjustment of $249 million to record a deferred charge offset to the fair value of debt purchase price adjustment described in footnote (4) below.
(4) Our long-term debt assumed in the acquisition was recorded at its fair market value resulting in a $249 million purchase price adjustment. This purchase price adjustment has been reported as "Debt fair value adjustments" on our Consolidated Balance Sheets.
(5) Deferred income taxes include a purchase price reduction adjustment of $34 million which primarily consisted of an adjustment to reduce deferred tax liabilities associated with the tax effects of purchase price adjustments described herein.

The goodwill resulting from the acquisition is primarily due to expected commercial and operational synergies and is not deductible for tax purposes.

We used appraisers to assist in the determination of fair value of certain assets. As of December 31, 2012, the purchase price allocation was preliminarily based on available information. Management is reviewing the valuation and confirming results to determine the final purchase price allocation, which is expected to be completed in the second quarter of 2013.

Expenses Related to KMI's acquisition of El Paso

We incurred acquisition-related expenses of $29 million in the Successor period in 2012, primarily related to allocated severance costs which are included in "Operation and maintenance" expense in our Consolidated Statements of Income and Comprehensive Income.

4. Income Taxes

Effective with KMP's acquisition of a 50% ownership interest in us from KMI on August 1, 2012, we are no longer subject to either federal income taxes or generally to state income taxes. As a result of this acquisition, we settled our current and deferred income tax balances of $431 million with recoveries of our note receivable from KMI. See Note 8 for further discussion of these transactions.

Components of Income Tax Expense

The following table reflects the components of income tax expense included in net income for each of the periods presented below (in millions):

	Successor	Predecessor	
	Period from Acquisition May 25, 2012 to December 31, 2012	Period from January 1, 2012 to May 24, 2012	Year Ended December 31, 2011
Current			
Federal	$ —	$ —	$ 19
State	—	—	2
	—	—	21
Deferred			
Federal	1	13	19
State	—	2	2
	1	15	21
Total income tax expense	$ 1	$ 15	$ 42

Effective Tax Rate Reconciliation

Our income tax expense differs from the amount computed by applying the statutory federal income tax rate of 35 percent for the following reasons for each of the periods presented below (in millions, except for tax rates):

	Successor	Predecessor	
	Period from Acquisition May 25, 2012 to December 31, 2012	Period from January 1, 2012 to May 24, 2012	Year Ended December 31, 2011
Income tax expense at the statutory federal rate of 35%	$ 25	$ 14	$ 39
Increase (decrease)			
Non-taxable earnings	(24)	—	—
State income taxes, net of federal income tax effect	—	1	3
Income tax expense	$ 1	$ 15	$ 42
Effective tax rate	2%	38%	38%

Deferred Tax Assets and Liabilities

The following are the components of our net deferred tax liability as of December 31, 2011(in millions):

	Predecessor
Deferred tax liabilities	
Property, plant and equipment	$ 512
Regulatory and other assets	34
Total deferred tax liability	546
Deferred tax assets	
U.S. net operating loss and tax credit carryovers	77
Regulatory and other liabilities	42
Total deferred tax asset	119
Net deferred tax liability	$ 427

5. Property, Plant and Equipment

Classes of Assets and Depreciation Rates

As of December 31, 2012 and 2011, our property, plant and equipment consisted of the following (in millions, except for %):

	Successor		Predecessor
	Annual Depreciation Rates (%)	December 31, 2012	December 31, 2011
Transmission and storage facilities	1.09 - 50.0	$ 2,188	$ 3,612
General plant	1.66 - 33.0	54	62
Intangible plant	4.0 - 15.0	17	16
Other[(1)]		71	267
Accumulated depreciation and amortization[(1)(2)]		(50)	(1,525)
		2,280	2,432
Construction work in progress		45	36
Property, plant and equipment, net		$ 2,325	$ 2,468

(1) The amounts for the Predecessor period included additional acquisition costs and the related accumulated depreciation that are further discussed below.

(2) The composite weighted average depreciation rates for the 2012 Successor period, 2012 Predecessor period and the year ended December 31, 2011 were approximately 2.4%, 2.4% and 2.5%, respectively.

Additional Acquisition Costs

In the periods prior to KMI's acquisition of El Paso, our property, plant and equipment balances included additional acquisition costs assigned to utility plant, which represented the excess of allocated purchase costs over the historical costs of the facilities. As of December 31, 2011, additional acquisition costs assigned to utility plant was approximately $151 million and accumulated depreciation was approximately $101 million. These additional acquisition costs were being amortized on a straight-line basis over 21 years and were not recoverable in our rates under FERC policies. Our amortization expense related to these additional acquisition costs was approximately $1 million and $2 million for the January 1, 2012 to May 24, 2012 period and the year ended December 31, 2011, respectively. As a result of KMI's May 25, 2012 acquisition of El Paso and the application of "push-down" accounting, these additional acquisition costs were removed from property, plant and equipment. The reduction was to record our property, plant and equipment at its regulatory value in conformity with our accounting policy.

6. Debt

We classify our debt based on the contractual maturity dates of the underlying debt instruments. The following table summarizes the net carrying value of our outstanding debt, excluding debt fair value adjustments, as of December 31 (in millions):

	Successor 2012	Predecessor 2011
5.95% Notes due April 2017	$ 355	$ 355
8.625% Debentures due January 2022	260	260
7.50% Debentures due November 2026	200	200
8.375% Notes due June 2032	300	300
	1,115	1,115
Less: Unamortized discount	—	2
Total long-term debt	$ 1,115	$ 1,113

Debt Covenants

Under our various financing documents, we are subject to a number of restrictions and covenants. The most restrictive of these include limitations on the incurrence of liens and limitations on sale-leaseback transactions. For the Successor and Predecessor periods in 2012 and the year ended December 31, 2011, we were in compliance with our debt-related covenants.

7. Retirement Benefits

Pension and Retirement Savings Plans

KMI maintains a pension plan and a retirement savings plan covering substantially all of its United States employees, including our former employees. The benefits under the pension plan are determined under a cash balance formula. Under its retirement savings plan, KMI contributes an amount equal to 5% of participants' eligible compensation per year. KMI is responsible for benefits accrued under its plans and allocates the related costs to its affiliates.

Postretirement Benefits Plan

We provide postretirement medical benefits for a closed group of retirees. These benefits may be subject to deductibles, co-payment provisions, and other limitations and dollar caps on the amount of employer costs and are subject to further benefit changes by KMI, the plan sponsor. In addition, certain former employees continue to receive limited postretirement life insurance benefits. Our postretirement benefit plan costs are prefunded and were recoverable under prior rate case settlements. Currently, there is no cost recovery or related funding that is required as part of our current FERC approved rates, however, we can seek to recover any funding shortfall that may be required in the future. We do not expect to make any contributions to our postretirement benefit plan in 2013, and there were no contributions made in the Predecessor and Successor periods in 2012 and 2011.

Accumulated Postretirement Benefit Obligation, Plan Assets and Funded Status

In accounting for our postretirement benefit plan, we record an asset or liability based on the overfunded or underfunded status. Any deferred amounts related to unrecognized gains and losses or changes in actuarial assumptions are recorded in "Accumulated other comprehensive income," a component of "Members' equity," until those gains and losses are recognized in our Consolidated Statements of Income and Comprehensive Income. Prior to the third quarter of 2011, we recorded a regulatory asset or liability for these unrecognized amounts as allowed by the FERC. During 2011, we reclassified $6 million (net of income taxes of $4 million) from a regulatory liability to "Accumulated other comprehensive income" pursuant to our rate case settlement whereby these amounts are no longer included in the rates we charge our customers.

The table below provides information about our postretirement benefit plan for each of the periods presented (in millions):

	Successor	Predecessor	
	Period from Acquisition May 25, 2012 to December 31, 2012	Period from January 1, 2012 to May 24, 2012	Year Ended December 31, 2011
Change in accumulated postretirement benefit obligation:			
Accumulated postretirement benefit obligation — beginning of period	$ 52	$ 51	$ 50
Interest cost	1	1	2
Actuarial (gain) loss	(5)	—	1
Plan amendments	(1)	—	—
Benefits paid[1]	(3)	(2)	(2)
Accumulated postretirement benefit obligation — end of period	$ 44	$ 50	$ 51
Change in plan assets:			
Fair value of plan assets — beginning of period	$ 84	$ 84	$ 84
Actual return on plan assets	7	2	3
Benefits paid	(3)	(2)	(3)
Fair value of plan assets — end of period	$ 88	$ 84	$ 84
Reconciliation of funded status:			
Fair value of plan assets	$ 88		$ 84
Less: accumulated postretirement benefit obligation	44		51
Net asset at December 31[2]	$ 44		$ 33

(1) Amounts shown are net of a subsidy of less than $1 million for each of the periods presented above related to the Medicare Prescription Drug, Improvement, and Modernization Act of 2003.

(2) Net asset amounts are included in "Deferred charges and other assets" on our Consolidated Balance Sheets.

Components of Accumulated Other Comprehensive Income

The amounts recognized in "Other comprehensive income" on our Consolidated Statements of Income and Comprehensive Income for the Successor period in 2012 and the year ended December 31, 2011 of $9 million and $3 million (net of income taxes of $3 million), respectively, are primarily related to unrecognized gains. There was no "Other comprehensive income" recognized during the Predecessor period of January 1, 2012 to May 24, 2012. We anticipate that less than $1 million of "Other comprehensive income" will be recognized as part of our net periodic benefit income in 2013.

Plan Assets

The primary investment objective of our plan is to ensure that, over the long-term life of the plan, an adequate pool of sufficiently liquid assets exists to meet the benefit obligations to retirees and beneficiaries. Investment objectives are long-term in nature covering typical market cycles. Any shortfall of investment performance compared to investment objectives is generally the result of economic and capital market conditions. Although actual allocations vary from time to time from our targeted allocations, the target allocations of our postretirement plan's assets are 65% equity and 35% fixed income securities. We may invest plan assets in a manner that replicates, to the extent feasible, the Russell 3000 Index and the Barclays Capital Aggregate Bond Index to achieve equity and fixed income diversification, respectively.

We use various methods to determine the fair values of the assets in our other postretirement benefit plans, which are impacted by a number of factors, including the availability of observable market data over the contractual term of the underlying assets. We separate these assets into three levels (Level 1, 2 and 3) based on our assessment of the availability of this market data and the significance of non-observable data used to determine the fair value of these assets. As of December 31, 2012, assets were comprised of an exchange-traded mutual fund with a fair value of $2 million and common/collective trust funds with a fair value of $86 million. As of December 31, 2011, assets were comprised of an exchange-traded mutual fund with a fair value of $2 million and common/collective trust funds with a fair value of $82 million. Our exchange-traded mutual fund invests primarily in dollar-denominated securities, and its fair value (which is considered a Level 1 measurement) is determined based on the price quoted for the fund in actively traded markets. Our common/collective trust funds are invested in approximately 65% equity and 35% fixed income securities, and their fair values (which are considered Level 2 measurements) are determined primarily based on the net asset value reported by the issuer, which is based on similar assets in active markets. Certain restrictions on withdrawals exist for these common/collective trust funds where the issuer reserves the right to temporarily delay withdrawals in certain situations such as market conditions or at the issuer's discretion. We do not have any assets that are considered Level 3 measurements. The methods described above may produce a fair value that may not be indicative of net realizable value or reflective of future fair values, and there have been no changes in the methodologies used as of December 31, 2012 and 2011.

Expected Payment of Future Benefits

As of December 31, 2012, we expect the following benefit payments under our plan (in millions):

Year Ending December 31,	Successor Expected Payments[1]
2013	$ 4
2014	4
2015	4
2016	4
2017	4
2018 - 2022	15

(1) Includes a reduction of approximately $1 million in each of the years 2013 – 2017 and approximately $5 million in aggregate for 2018 – 2022 for an expected subsidy related to the Medicare Prescription Drug, Improvement, and Modernization Act of 2003.

Actuarial Assumptions and Sensitivity Analysis

Accumulated postretirement benefit obligations and net benefit costs are based on actuarial estimates and assumptions. The following table details the weighted average actuarial assumptions used in determining our postretirement plan obligations and net benefit costs:

	Successor	Predecessor	
	Period from Acquisition May 25, 2012 to December 31, 2012	Period from January 1, 2012 to May 24, 2012	Year Ended December 31, 2011
	(%)	(%)	(%)
Assumptions related to benefit obligations at period end:			
Discount rate	3.14	4.16	4.16
Assumptions related to benefit costs for the period:			
Discount rate[1]	3.81	4.16	4.53
Expected return on plan assets[2]	7.50	7.50	7.75

(1) We select our discount rate by matching the timing and amount of our expected future benefit payments for our postretirement benefit obligation to the average yields of various high-quality bonds with corresponding maturities.
(2) The expected return on plan assets listed in the table above is a pre-tax rate of return based on our portfolio of investments. We utilize an after-tax expected return on plan assets to determine our benefit costs, which is based on unrelated business income taxes with a weighted average rate of 22% for calendar year 2012 and a rate of 35% for 2011.

Actuarial estimates for our postretirement benefit plan assumed a weighted average annual rate of increase in the per capita costs of covered health care benefits of 7%, gradually decreasing to 5% by the year 2019. A one-percentage point change would not have had a significant effect on interest costs in the Successor or Predecessor periods in 2012 or the year ended December 31, 2011. A one-percentage point change in assumed health care cost trends would have the following effect as of December 31 (in millions):

	Successor 2012	Predecessor 2011
One percentage point increase:		
Accumulated postretirement benefit obligation	$ 4	$ 4
One percentage point decrease:		
Accumulated postretirement benefit obligation	$ (3)	$ (4)

Components of Net Benefit Income

For each of the periods presented, the components of net benefit income are as follows (in millions):

	Successor	Predecessor	
	Period from Acquisition May 25, 2012 to December 31, 2012	Period from January 1, 2012 to May 24, 2012	Year Ended December 31, 2011
Interest cost	$ 1	$ 1	$ 2
Expected return on plan assets	(4)	(2)	(6)
Net benefit (income) expense	$ (3)	$ (1)	$ (4)

8. Related Party Transactions

Distributions

During the Successor period ended December 31, 2012 and the Predecessor period ended May 24, 2012, we made cash distributions to our owners of $71 million and $60 million, respectively. During 2011, we made cash distributions to our owners of $103 million.

Income Taxes

Effective August 1, 2012, we converted into a limited liability company as discussed in Note 1 and settled our current and deferred income tax balances of approximately $431 million with El Paso with recoveries of our note receivable from KMI under its cash management program. Effective with KMP's acquisition of a 50% ownership interest in us from KMI on August 1, 2012, we are no longer subject to either federal income taxes or generally to state income taxes.

Prior to our conversion into a limited liability company, El Paso filed consolidated U.S. federal and certain state tax returns which include our taxable income. In certain states, we file and pay taxes directly to the state taxing authorities. As of December 31, 2011, we had federal and state income taxes payable of $21 million.

Cash Management Program

We participate in the cash management program with KMI and its affiliates (and El Paso's for periods prior to KMI's acquisition of El Paso) which matched short-term cash surpluses and needs of participating affiliates, thus minimizing total borrowings from outside sources. KMI and its affiliates use the cash management program to settle intercompany transactions between participating affiliates. As of December 31, 2011, we had a note receivable from El Paso of $873 million. The interest rate on this note was variable and was 2.5% as of December 31, 2011. In conjunction with KMP's acquisition of a 50% ownership interest in us in August 2012, we settled our current and deferred income tax balances of approximately $431 million with recoveries of our note receivable from KMI. In addition, we made non-cash distributions totaling $442 million to KMP and KMI, which eliminated the remaining note receivable balance from KMI.

Other Affiliate Balances

We enter into transactions with our affiliates within the ordinary course of business and the services are based on the same terms as non-affiliates, including natural gas transportation services to and from affiliates under long-term contracts and various operating agreements.

We do not have employees. Employees of KMI and its affiliates provide services to us and our subsidiaries. We are managed and operated by officers of KMI and its affiliates. Under policies with KMI and its affiliates, we reimburse KMI and its affiliates without a profit component for the provision of various general and administrative services for our benefit and for direct expenses incurred by KMI or its affiliates on our behalf. KMI bills us directly for certain general and administrative costs and allocates a portion of its general and administrative costs without a profit component to us. Prior to KMI's acquisition of El Paso, we were allocated costs from El Paso and Tennessee Gas Pipeline Company, L.L.C. (TGP), our affiliate, for services provided to us. We also allocated costs to Colorado Interstate Gas Company, our affiliate, for its share of our pipeline services. The allocations from El Paso and TGP are based on the estimated level of effort devoted to our operations and the relative size of our earnings before interest expense and income taxes, gross property and payroll.

As of December 31, 2011, we had accounts receivable, accounts payable and contractual deposits with affiliates of $3 million, $20 million and $9 million, respectively. As of December 31, 2012, our other affiliate balances were less than $1 million.

The following table shows revenues, expenses and reimbursements from our affiliates for the each of the periods presented (in millions):

	Successor	Predecessor	
	Period from Acquisition May 25, 2012 to December 31, 2012	Period from January 1, 2012 to May 24, 2012	Year Ended December 31, 2011
Revenues	$ 12	$ 8	$ 20
Operation and maintenance expense[(1)]	52	29	76
Reimbursement of operating expense	2	4	10

(1) The Successor period includes severance costs of $29 million allocated to us from El Paso as a result of KMI's acquisition of El Paso.

9. Litigation, Environmental and Other Contingencies

Legal Proceedings

Bank of America

We are a named defendant, along with Burlington Resources, Inc. (Burlington), now a subsidiary of ConocoPhillips Company, in a class action lawsuit styled *Bank of America, et al. v. El Paso Natural Gas and Burlington Resources Oil and Gas Company, L.P.*, filed in October 2003 in the District Court of Kiowa County, Oklahoma asserting royalty underpayment claims related to specified shallow wells in Oklahoma, Texas and New Mexico. The Plaintiffs assert that royalties were underpaid starting in the 1980s when the purchase price of gas was lowered below the Natural Gas Policy Act maximum lawful prices. The Plaintiffs have only alleged an amount of damages against our co-defendant, Burlington. We believe that our actions in the 1980s were proper in light of a declining market. We also contend that we are entitled to an indemnity from Burlington under our 1992 separation agreement for all claims related to royalty payments, which Burlington denies. The Plaintiffs assert that royalties were further underpaid by Burlington as a result of post-production cost deductions taken starting in the late 1990s. We have no liability for the post-production claims as they pertain to periods after our separation from Burlington.

This action was transferred to Washita County District Court in 2004. A tentative settlement reached in November 2005 was rejected by the court in June 2007. A class certification hearing occurred in April 2009. The court certified a Texas and Oklahoma class of royalty owners and stayed the claims pertaining to New Mexico wells. The class certification was upheld by the Oklahoma Court of Appeals, and a petition for review was denied by the Oklahoma Supreme Court. The Plaintiffs have proceeded with discovery of the post-production claims against Burlington. The stay of the New Mexico claims has been lifted, and the Plaintiffs' motion to certify a class of New Mexico royalty owners is scheduled to be heard in April 2013.

State of Texas v. EPNG

On behalf of the Texas Commission on Environmental Quality, the State of Texas has filed a lawsuit against us related to allegedly unauthorized emissions of air contaminants associated with the rupture of one of our pipelines in the vicinity of Bushland, Texas in 2009. The parties have reached an agreement to settle this matter, the agreement has been signed by both parties and EPNG paid a $128,000 penalty to resolve the matter, while admitting no guilt. The settlement did not have a material adverse effect on our financial condition.

Other Legal Matters

We and our affiliates are named defendants in numerous lawsuits and governmental proceedings and claims that arise in the ordinary course of our business. There are also other regulatory rules and orders in various stages of adoption, review and/or implementation. For each of these matters, we evaluate the merits of the case or claim, our exposure to the matter, possible legal or settlement strategies and the likelihood of an unfavorable outcome. If we determine that an unfavorable outcome is probable and can be estimated, we establish the necessary accruals. While the outcome of these matters, including those discussed above, cannot be predicted with certainty, and there are still uncertainties related to the costs we may incur, based upon our evaluation and experience to date, we believe we have established appropriate reserves for these matters. It is possible, however, that new information or future developments could require us to reassess our potential exposure related to these matters and establish accruals accordingly, and these adjustments could be material.

As of December 31, 2012 and 2011, we had less than $1 million accrued for our outstanding legal proceedings. We do not have any other litigation or claim contingency matters assessed as probable or reasonably possible that would require disclosure in the financial statements.

Environmental Matters

We are subject to federal, state and local laws and regulations governing environmental quality and pollution control. These laws and regulations require us to remove or remedy the effect of the disposal or release of specified substances at current and former operating sites. As of December 31, 2012 and 2011, our accrual was approximately $41 million and $14 million, respectively for environmental matters. Our accrual includes amounts for expected remediation costs and associated onsite, offsite and groundwater technical studies and related environmental legal costs. As of December 31, 2012 and 2011, our accrual includes $33 million and $13 million, respectively for environmental contingencies related to properties we previously owned.

For 2013, we estimate that our total remediation expenditures will be approximately $5 million, most of which will be expended under government directed clean-up plans. In addition, we expect to make capital expenditures for environmental matters of approximately $9 million in the aggregate for the years of 2013 through 2017, including capital expenditures associated with the impact of the United States Environmental Protection Agency's (EPA) rule on emissions of hazardous air pollutants from reciprocating internal combustion engines which are subject to regulations with which we have to be in compliance by October 2013.

Our recorded environmental liabilities reflect our current estimates of amounts we will expend on remediation projects in various stages of completion. However, depending on the stage of completion or assessment, the ultimate extent of contamination or remediation required may not be known. As additional assessments occur or remediation efforts continue, we may incur additional liabilities.

Clean Air Act Emission Regulation

On April 17, 2012, the EPA issued regulations pursuant to the federal Clean Air Act to reduce various air pollutants from the oil and natural gas industry. These regulations will limit emissions from certain equipment including compressors, storage vessels and natural gas processing plants. Based on our evaluation of the regulations and their impact on our operations and our financial results, we do not anticipate a material impact on our operations or financial results.

Superfund Matters

Included in our recorded environmental liabilities are projects where we have received notice that we have been designated or could be designated as a Potentially Responsible Party (PRP) under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), commonly known as Superfund, or state equivalents for three active sites. Liability under the federal CERCLA statute may be joint and several, meaning that we could be required to pay in excess of our pro rata share of remediation costs. We consider the financial strength of other PRPs in estimating our liabilities. Accruals for these issues are included in the environmental reserve discussed above.

Tuba City Uranium Milling Facility

For approximately ten years, beginning in the mid to late 1950s, Rare Metals Corporation of America, a historical affiliate, conducted uranium mining and milling operations in the vicinity of Tuba City, Arizona. The site of the mill, which Rare Metals operated under a contract with the United States and which is within the Navajo Indian Reservation, reverted to the Navajo Nation after the mill closed in 1966. The tailings at the mill site were encapsulated and a ground water remediation system was installed by the United States Department of Energy (DOE) under the Federal Uranium Mill Tailings Radiation Control Act of 1978. In May 2007, we filed suit against the DOE and other federal agencies requesting a judicial determination that the DOE must also remediate mill-related wastes allegedly disposed of at two sites in the vicinity of the mill. In March 2009, the United States District Court for the District of Columbia dismissed one of our claims, which was affirmed by the Court of Appeals. The United States filed a motion to dismiss our remaining claims, which was granted by the district court in March 2012, but is on appeal. In a matter related to Rare Metals' uranium mining operations, we have received a General Notice Letter from the EPA notifying us of our potential liability to perform remedial measures at 20 historical uranium mine sites in the vicinity of the mill. We currently are negotiating the terms of an Administrative Order on Consent, pursuant to which we would investigate the environmental condition of the mines we operated. The final outcome of these legal proceedings, negotiations and environmental assessments is uncertain.

Other

It is possible that new information or future developments could require us to reassess our potential exposure related to environmental matters. We may incur significant costs and liabilities in order to comply with existing environmental laws and regulations. It is also possible that other developments, such as increasingly strict environmental laws, regulations and orders of regulatory agencies, as well as claims for damages to property and the environment or injuries to other persons resulting from our current or past operations, could result in substantial costs and liabilities in the future. As this information becomes available, or other relevant developments occur, we will adjust our accrual amounts accordingly. While there are still uncertainties related to the ultimate costs we may incur, based upon our evaluation and experience to date, we believe our reserves are adequate.

Other Commitments

Capital Commitments

We have planned capital projects that are discretionary in nature, with no substantial contractual capital commitments made in advance of the actual expenditures.

Other Commercial Commitment

We hold cancelable easements or rights-of-way arrangements from landowners permitting the use of land for the construction and operation of our pipeline systems. Our obligations under these easements are not material to our results of operations.

Operating Leases

We lease property, facilities and equipment under various operating leases. Future minimum annual rental commitments under our operating leases as of December 31, 2012, were as follows (in millions):

Year Ending December 31,	
2013	$ 3
2014	3
2015	1
2016	1
Thereafter	1
Total	$ 9

Rental expense on our lease obligations for the Successor period in 2012, the Predecessor period in 2012 and the year ended December 31, 2011 was approximately $14 million, $10 million and $23 million, respectively, and is reflected in ”Operation and Maintenance” expense on our Consolidated Statements of Income and Comprehensive Income. Included in our rental expense is approximately $20 million of annual expense associated with right-of-way and other arrangements, principally related to a long-term commitment which extends through 2025.

10. Fair Value

The following table reflects the carrying amount and estimated fair value of our long-term debt (in millions):

	Successor December 31, 2012		Predecessor December 31, 2011	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Total debt	$ 1,352 (1)	$ 1,450	$ 1,113	$ 1,348

(1) Includes increase of $237 million of unamortized excess fair value adjustment resulting from the application of “push down” accounting associated with KMI’s acquisition of El Paso on May 25, 2012.

As of December 31, 2012 and 2011, the carrying amounts of cash and cash equivalents, accounts receivable and accounts payable represent their fair values based on the short-term nature of these instruments. The carrying amount of our affiliate note receivable as of December 31, 2011 approximated its fair value due to the note being due on demand and its market-based interest rate.

As of December 31, 2012 and 2011, our financial instruments measured at fair value consisted of our long-term debt. We separate the fair values of our financial instruments into levels based on our assessment of the availability of observable market data and the significance of non-observable data used to determine the estimated fair value. We estimated the fair values of our long-term debt primarily based on quoted market prices for the same or similar issues, a Level 2 fair value measurement. Our assessment and classification of an instrument within a level can change over time based on the maturity or liquidity of the instrument and this change would be reflected at the end of the period in which the change occurs. During the Predecessor and Successor periods in 2012 and the year ended December 31, 2011, there were no changes to the inputs and valuation techniques used to measure fair value, the types of instruments, or the levels in which they are classified.

11. Regulatory Assets and Liabilities

Our regulatory asset and liability balances are recoverable or reimbursable over various periods. Below are the details of our regulatory assets and liabilities as of December 31 (in millions**)**

	Successor 2012	Predecessor 2011
Current regulatory assets		
Difference between gas retained and gas consumed in operations	$ 4	$ 6
Other	2	2
Total current regulatory assets	6	8
Non-current regulatory assets		
Taxes on capitalized funds used during construction	21	21
Unamortized loss on reacquired debt	27	18
Postretirement benefits	6	8
Other	9	9
Total non-current regulatory assets	63	56
Total regulatory assets	$ 69	$ 64
Current regulatory liabilities		
Property and plant depreciation	$ 1	$ 1
Difference between gas retained and gas consumed in operations	7	12
Other	1	3
Total current regulatory liabilities	9	16
Non-current regulatory liabilities		
Property and plant depreciation	28	25
Postretirement benefits	8	8
Other	2	2
Total non-current regulatory liabilities[1]	38	35
Total regulatory liabilities	$ 47	$ 51

(1) Included in "Other long-term liabilities and deferred credits" on our Consolidated Balance Sheets.

Substantially all of our regulatory assets as of December 31, 2012 are being recovered as cost of service in our rates. These assets are expected to be recovered in rates over a period of approximately one year to twenty-five years.

The significant regulatory assets and liabilities include:

Difference between gas retained and gas consumed in operations

These amounts reflect the value of the volumetric difference between the gas retained and consumed in our operations. These amounts are not included in the rate base, but given our tariffs, are expected to be recovered from our customers or returned to our customers in subsequent fuel filing periods.

Taxes on capitalized funds used during construction

These regulatory asset balances were established to offset the deferred tax for the equity component of AFUDC capitalized in long-lived assets. Taxes on capitalized funds used during construction and the offsetting deferred income taxes are included in the rate base and are recovered over the depreciable lives of the long lived asset to which they relate. These balances were established on our pipeline prior to our conversion to a non-taxable entity.

Unamortized loss on reacquired debt

Amount represents the deferred and unamortized portion of losses on reacquired debt which are recovered through the cost of service over the life of the new debt issue, or in the case of refinanced debt, over the life of the new debt issue.

Postretirement benefits

Represents differences in postretirement benefit costs expensed and the amounts previously recovered in rates. Prior to our 2011 rate case settlement, these balances also included unrecognized gains and losses or changes in actuarial assumptions related to our postretirement benefit plan. As part of our rate case settlement, we no longer include these costs in our rates and during the third quarter of 2011, we reclassified $6 million (net of income taxes of $4 million) to "Accumulated other comprehensive income."

Property and plant depreciation

Represents the deferral of customer-funded amounts for costs of future asset retirements and costs previously collected in our rates for the depreciation of certain assets in excess of normal depreciation rates.

12. Transactions with Major Customers

For the Successor period in 2012, revenue from one non-affiliate customer was approximately $47 million, which exceeded 10% of our operating revenues. For the Predecessor period in 2012, revenues from three non-affiliate customers were approximately $30 million, $29 million and $25 million, each of which exceeded 10% of our operating revenues. For the year ended December 31, 2011, revenues from three non-affiliate customers were approximately $80 million, $63 million and $59 million, each of which exceeded 10% of our operating revenues.

13. Accounts Receivable Sales Program

We participated in an accounts receivable sales program where we sold receivables in their entirety to a third-party financial institution (through a wholly owned special purpose entity). On June 20, 2012, we terminated the accounts receivable sales program and paid $23 million to the third-party financial institution, which consisted of sales proceeds received up front and servicing fees. The sale of these accounts receivable (which were short-term assets that generally settled within 60 days) qualified for sale accounting. The third-party financial institution involved in our accounts receivable sales program acquired interests in various financial assets and issued commercial paper to fund those acquisitions. We did not consolidate the third-party financial institution because we did not have the power to control, direct or exert significant influence over its overall activities since our receivables did not comprise a significant portion of its operations.

In connection with our accounts receivable sales, we received a portion of the sales proceeds up front and received an additional amount upon the collection of the underlying receivables (which we referred to as a deferred purchase price). Our ability to recover the deferred purchase price was based solely on the collection of the underlying receivables. The tables below contain information related to our accounts receivable sales program (in millions).

	Successor	Predecessor	
	Period from Acquisition May 25, 2012 to December 31, 2012	Period from April 1, 2012 to May 24, 2012	Year Ended December 31, 2011
Accounts receivable sold to the third-party financial institution[(1)]	$ 34	$ 190	$ 549
Cash received for accounts receivable sold under the program	24	103	318
Deferred purchase price related to accounts receivable sold	9	87	231
Cash received related to the deferred purchase price	—	99	223
Cash paid in conjunction with terminated program	23	—	—

(1) During the Successor period in 2012, the Predecessor period in 2012 and the year ended December 31, 2011, losses recognized on the sale of accounts receivable were immaterial.

	Predecessor December 31, 2011[(2)]
Accounts receivable sold and held by third party financial institution	$ 50
Uncollected deferred purchase price related to accounts receivable sold [(2)(3)]	21

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(2) Initially recorded at an amount which approximated its fair value using observable inputs other than quoted prices in active markets, a Level 2 fair value measurement.

(3) There were no balances outstanding as of December 31, 2012 since all balances were settled in June 2012 when the accounts receivable sales program was terminated.

The deferred purchase price related to the accounts receivable sold was reflected as "Accounts receivable, net" on our Consolidated Balance Sheets. Because the cash received up front and the deferred purchase price related to the sale or ultimate collection of the underlying receivables, and were not subject to significant other risks given their short term nature, we reflected all cash flows under the accounts receivable sales program as "Net Cash Provided by Operating Activities" on our Consolidated Statements of Cash Flows. Under the accounts receivable sales program, we serviced the underlying receivables for a fee. The fair value of these servicing agreements, as well as the fees earned, were not material to our financial statements for the Predecessor and Successor periods in 2012 and the year ended December 31, 2011.

14. Regulatory Matters

Below is a brief description of our ongoing regulatory matters, including any material developments that occurred during the Predecessor and Successor periods in 2012 and the year ended December 31, 2011.

Rate Cases

In April 2010, the FERC approved an offer of settlement which increased our base tariff rates, effective January 1, 2009. The settlement resolved all but four issues in the proceeding. In January 2011, the Presiding Administrative Law Judge (ALJ) issued a decision that for the most part found against us on the four issues. In May 2012, the FERC upheld the initial decision of the ALJ on three of the issues and found in favor of us on one of the issues. We along with other parties have sought rehearing of those decisions to the FERC and may also seek review of any of the FERC's decisions to the U.S. Court of Appeals. In addition, we filed with the FERC to implement certain aspects of the May 2012 order as required. Although the final outcome is not currently determinable, we believe our accruals established for this matter are adequate.

In September 2010, we filed a new rate case with the FERC proposing an increase in base tariff rates which would increase revenues by approximately $100 million annually over previously effective tariff rates. In October 2010, the FERC issued an order accepting and suspending the effective date of the proposed rates to April 1, 2011, subject to refund, the outcome of a hearing and other proceedings. In June 2012, the ALJ issued an initial decision after a hearing which was overall favorable to us. Participants have appealed this decision to the FERC and ultimately may seek review of the FERC's decision to the U.S. Court of Appeals. Additionally, certain customers have requested that the FERC require us to decrease our rates based on an order issued in May 2012 in another proceeding. We have objected to any such interim decrease and have requested adequate surcharge authority in the event the final rates are above the interim rates. It is uncertain whether the increase in revenues will be achieved in the context of any settlement between our customers and us or following the outcome of the hearing in the rate case. Although the final outcome is not currently determinable, we believe our accruals established for this matter are adequate.

On November 15, 2012, the FERC approved and adopted an Initial ALJ Decision which dismissed a complaint filed on July 7, 2010 by Texas Gas Service Company, a Division of ONEOK, Inc., which contended that EPNG's existing postage stamp rate design for fuel rates was unjust and unreasonable. Texas Gas Service Company filed a request for rehearing of the FERC's order and the outcome is uncertain.

Other Regulatory Matters

Temporary Deactivation of Nine Compression Facilities (Docket No. CP11-17)

In October 2010, we filed with the FERC to temporarily idle nine compressor stations along our south mainline system in 2011. This was done to better align our capacity to the current lower level of contract demand resulting from, in part, the weakened economic conditions along this line. Our intent was to bring the idled facilities back into service over the next several years as market demand improves. We will continue to incur related operating costs and depreciation expense until the compressor stations are idled. In April 2011, the FERC denied our request to temporarily idle the nine compressor stations. On May 27, 2011, we filed a request for rehearing of the FERC's decision. Our request for rehearing was granted by the FERC only for the purpose of allowing it more time to consider the merits of our rehearing request. We filed a Notice to Withdraw Application on April 16, 2013.

San Juan Triangle/North Mainline Abandonment Project (Docket No. CP12-45-000)

In January 2012, separately from our October 2010 filing, we filed with the FERC to permanently abandon two compressor stations and four compressor units on our north mainline and San Juan triangle to better align our capacity with current contract demand. Several customers filed protests to our application. We requested an order by December 31, 2012. On September 7, 2012, we withdrew our application to permanently abandon these facilities.

Norte Crossing Project (Docket No. CP12-96-00)

In March 2012, we filed an application seeking Section 3 authorization and a Presidential Permit for the siting, construction, connection, operation and maintenance of natural gas export facilities (Norte Crossing) at the international boundary between the United States and Mexico in El Paso County, Texas. The cost of these border crossing facilities along with additional metering facilities is approximately $10 million. The FERC approved this application on August 31, 2012 and the new border crossing facilities are anticipated to be in-service by the summer of 2013.

Willcox Lateral Expansion Project (Docket No. CP12-6)

In October 2011, we filed an application seeking authorization to expand the Willcox Lateral facilities by reconfiguring its Willcox Compressor Station from mainline service to lateral service by completing certain piping and facility modifications to the station and existing delivery meter stations in Cochise County, Arizona. The cost of the expansion facilities is approximately $23 million. The FERC approved this application on October 12, 2012 and the expansion facilities were placed in-service in April 2013.

Sierrita Pipeline Project (Docket Nos. CP13-73-000 and CP13-74-000)

On February 7, 2013, KMP's wholly-owned subsidiary Sierrita Gas Pipeline LLC (a newly created interstate natural gas pipeline company) filed an application with the FERC to build a new 60-mile, 36-inch diameter pipeline and new border crossing facilities that would extend from our existing south mainlines (near the City of Tucson, Arizona) to the U.S.-Mexico border (near the Town of Sasabe, Arizona). At an approximate cost of $200 million, the new Sierrita Pipeline would interconnect with a new 36-inch diameter natural gas pipeline to be built in Mexico. The new facilities will provide approximately 200 million cubic feet per day of firm natural gas transportation capacity. Sierrita Gas Pipeline LLC entered into a 25-year transportation service agreement for the entire capacity. Pending FERC approval, the construction of the Sierrita Pipeline would begin as early as the first quarter of 2014. We anticipate that the pipeline would be placed into service in the fall of 2014.