

**TENNESSEE GAS PIPELINE 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



TENNESSEE GAS PIPELINE COMPANY, L.L.C.

TABLE OF CONTENTS

	<u>Page Number</u>
Independent Auditor's Reports.....	1
Consolidated Financial Statements	
Consolidated Statements of Income and Comprehensive Income .....	4
Consolidated Balance Sheets .....	5
Consolidated Statements of Cash Flows.....	6
Consolidated Statements of Member's Equity .....	7
Notes to Consolidated Financial Statements.....	8



## Report of Independent Auditors

To the Member and Management of Tennessee Gas Pipeline 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 Tennessee Gas Pipeline 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 provides 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 Tennessee Gas Pipeline Company, L.L.C.

We have audited the accompanying consolidated financial statements of Tennessee Gas Pipeline 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 Tennessee Gas Pipeline 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.



***Emphasis of Matter***

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. Our opinion is not modified with respect to this matter.

*PricewaterhouseCoopers LLP*

April 26, 2013

**TENNESSEE GAS PIPELINE COMPANY, L.L.C.**  
**CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME**  
(In Millions)

	<u>Successor</u>	<u>Predecessor</u>	
	<u>Period from</u> <u>Acquisition</u> <u>May 25, 2012 to</u> <u>December 31,</u> <u>2012</u>	<u>Period from</u> <u>January 1,</u> <u>2012</u> <u>to May 24,</u> <u>2012</u>	<u>Year</u> <u>Ended</u> <u>December 31,</u> <u>2011</u>
Revenues.....	\$ 602	\$ 414	\$ 976
Operating Costs and Expenses			
Operation and maintenance .....	228	154	353
Loss on long lived assets .....	—	125	—
Depreciation and amortization .....	101	83	198
Taxes, other than income taxes.....	29	24	56
Total Operating Costs and Expenses .....	<u>358</u>	<u>386</u>	<u>607</u>
Operating Income .....	<u>244</u>	<u>28</u>	<u>369</u>
Other Income (Expense)			
Earnings from equity investment .....	8	5	14
Other income, net .....	6	3	40
Interest expense .....	(79)	(55)	(134)
Affiliated interest income, net .....	4	5	16
Total Other Expense .....	<u>(61)</u>	<u>(42)</u>	<u>(64)</u>
Income (Loss) Before Income Taxes.....	183	(14)	305
Income Tax Benefit (Expense) .....	<u>(1)</u>	<u>5</u>	<u>(102)</u>
Net Income (Loss) .....	182	(9)	203
Other Comprehensive Income			
Adjustments to postretirement benefit plan liabilities (net of income tax expense of \$0 during May 25 to December 31, 2012, \$0 during January 1 to May 24, 2012 and \$2 in 2011) .....	3	—	4
Comprehensive Income (Loss) .....	<u>\$ 185</u>	<u>\$ (9)</u>	<u>\$ 207</u>

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

**TENNESSEE GAS PIPELINE COMPANY, L.L.C.**  
**CONSOLIDATED BALANCE SHEETS**  
(In Millions)

	<u>Successor</u> <u>December 31,</u> <u>2012</u>	<u>Predecessor</u> <u>December 31,</u> <u>2011</u>
<b>ASSETS</b>		
Current assets		
Cash and cash equivalents.....	\$ 6	\$ —
Accounts and note receivable, net.....	169	104
Inventories.....	48	57
Deferred income taxes .....	—	52
Assets held for sale .....	32	—
Other .....	<u>20</u>	<u>10</u>
Total current assets.....	275	223
Property, plant and equipment, net .....	3,865	6,039
Goodwill .....	3,249	—
Note receivable from affiliate .....	79	519
Investment .....	58	57
Regulatory assets .....	188	55
Deferred charges and other assets.....	<u>433</u>	<u>29</u>
Total Assets .....	<u>\$ 8,147</u>	<u>\$ 6,922</u>
<b>LIABILITIES AND MEMBER'S EQUITY</b>		
Current liabilities		
Accounts payable .....	\$ 118	\$ 189
Accrued taxes .....	24	23
Contractual deposits .....	17	29
Asset retirement obligations.....	21	22
Accrued interest .....	32	32
Regulatory liabilities .....	2	40
Accrued other current liabilities.....	<u>8</u>	<u>81</u>
Total current liabilities .....	222	416
Long-term liabilities and deferred credits		
Long-term debt.....	1,790	1,768
Debt fair value adjustments.....	401	—
Deferred income taxes .....	—	1,514
Other long-term liabilities and deferred credits .....	<u>47</u>	<u>41</u>
Total long-term liabilities and deferred credits.....	2,238	3,323
Total Liabilities .....	2,460	3,739
Commitments and contingencies (Note 10)		
Member's equity .....	5,684	3,179
Accumulated other comprehensive income .....	<u>3</u>	<u>4</u>
Total Member's Equity .....	<u>5,687</u>	<u>3,183</u>
Total Liabilities and Member's Equity .....	<u>\$ 8,147</u>	<u>\$ 6,922</u>

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

**TENNESSEE GAS PIPELINE COMPANY, L.L.C.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In Millions)

	<u>Successor</u>	<u>Predecessor</u>	
	<u>Period from Acquisition May 25, 2012 to December 31, 2012</u>	<u>Period from January 1, 2012 to May 24, 2012</u>	<u>Year Ended December 31, 2011</u>
<b>Cash Flows From Operating Activities</b>			
Net income (loss) .....	\$ 182	\$ (9)	\$ 203
Adjustments to reconcile net income to net cash from operating activities:			
Depreciation and amortization .....	101	83	198
Deferred income tax expense .....	10	(5)	85
Earnings from equity investment .....	(8)	(5)	(14)
Distributions from equity investment .....	6	6	13
Loss on long-lived assets .....	—	125	—
Other .....	(5)	(1)	(70)
Change in components of working capital:			
Accounts receivable .....	(58)	48	(26)
Accounts payable .....	62	(57)	8
Accrued taxes .....	(38)	(3)	1
Regulatory liabilities .....	(3)	(40)	(49)
Other, net .....	(5)	(56)	32
Other long-term assets and liabilities .....	<u>2</u>	<u>1</u>	<u>(16)</u>
Net Cash Provided by Operating Activities .....	<u>246</u>	<u>87</u>	<u>365</u>
<b>Cash Flows From Investing Activities</b>			
Capital expenditures .....	(141)	(97)	(683)
Net change in note receivable from affiliate .....	(121)	11	400
Other .....	19	2	4
Net Cash Used in Investing Activities .....	<u>(243)</u>	<u>(84)</u>	<u>(279)</u>
<b>Cash Flows From Financing Activities</b>			
Payments of debt .....	—	—	(86)
Net Cash Used in Financing Activities .....	<u>—</u>	<u>—</u>	<u>(86)</u>
Net Increase in Cash and Cash Equivalents .....	3	3	—
Cash and Cash Equivalents, beginning of period .....	<u>3</u>	<u>—</u>	<u>—</u>
Cash and Cash Equivalents, end of period .....	<u>\$ 6</u>	<u>\$ 3</u>	<u>\$ —</u>
<b>Supplemental Cash Flow Information</b>			
Cash paid during the period for interest (net of capitalized interest) .....	\$ 75	\$ 56	\$ 128
Income tax payments .....	11	—	12

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



**TENNESSEE GAS PIPELINE COMPANY, L.L.C.**  
**CONSOLIDATED STATEMENTS OF MEMBER'S EQUITY**  
(In Millions, Except Share Amounts)

	<u>Common Stock</u>		<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Total Stockholder's Equity</u>	<u>Member's Equity</u>	<u>Accumulated Other Comprehensive Income</u>	<u>Total Member's Equity</u>
	<u>Shares</u>	<u>Amount</u>						
<i>Predecessor</i>								
Balance at December 31, 2010.....	208	\$ —	\$ 2,209	\$ 1,092	\$ 3,301	\$ —	\$ —	\$ —
January 1, 2011 to September 30, 2011								
Net Income .....				125	125			
Conversion to limited liability company (October 1, 2011) .....	(208)		(2,209)	(1,217)	(3,426)	3,426		3,426
October 1, 2011 to December 31, 2011								
Net Income .....						78		78
Non-cash distribution to parent (Note 9).....						(325)		(325)
Other comprehensive income .....							4	4
Balance at December 31, 2011.....	—	—	—	—	—	3,179	4	3,183
Net loss.....						(9)		(9)
Balance at May 24, 2012 .....	<u>—</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 3,170</u>	<u>\$ 4</u>	<u>\$ 3,174</u>
<i>Successor</i>								
Balance at May 25, 2012 .....	—	\$ —	\$ —	\$ —	\$ —	\$ 5,258	\$ —	\$ 5,258
Net income .....						182		182
Other comprehensive income .....							3	3
Non-cash contribution from parent (Note 9).....						244		244
Balance at December 31, 2012 .....	<u>—</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 5,684</u>	<u>\$ 3</u>	<u>\$ 5,687</u>

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

**TENNESSEE GAS PIPELINE COMPANY, L.L.C.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. General**

We are a Delaware limited liability company, originally formed in 1947 as a corporation. Effective October 1, 2011, we converted our legal structure to a limited liability company and changed our name to Tennessee Gas Pipeline Company, L.L.C. When we refer to “us,” “we,” “our,” or “ours,” we are describing Tennessee Gas Pipeline Company, L.L.C. and/or our subsidiaries. We were an indirect wholly owned subsidiary of El Paso LLC (formerly El Paso Corporation) (El Paso). El Paso became a wholly owned subsidiary of Kinder Morgan, Inc. (KMI) when it was acquired by KMI on May 25, 2012. Effective August 1, 2012, Kinder Morgan Energy Partners, L.P. (KMP), a master limited partnership, acquired the full ownership interest in us from KMI. KMP is controlled by its general partner, Kinder Morgan G.P., Inc., a wholly owned subsidiary of KMI.

Our primary business consists of the interstate transportation and storage of natural gas. Our natural gas pipeline system consists of approximately 13,900 miles of pipeline with a design capacity of approximately 8.0 billion cubic feet per day for natural gas. This multiple-line system begins in the natural gas producing regions of Louisiana, the Gulf of Mexico and south Texas and extends to the northeast section of the U.S., including the metropolitan areas of New York City and Boston. Our system has interconnects at the U.S.-Mexico border, the U.S.-Canada border and major shale formations. Along our pipeline system, we have 93 billion cubic feet of underground working natural gas storage capacity through partially owned facilities or long-term contracts.

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 was assigned 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 and note receivable, net" on our accompanying Consolidated Balance Sheets as of December 31, 2012 and 2011 primarily consist of \$101 million and \$84 million, respectively, due from third party payors (unrelated entities). For information on receivables due to us from related parties, see Note 9.

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 or storage facility 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 and note 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 those instances where we receive recovery in rates related to losses on dispositions of operating units, we record a regulatory asset for the estimated recoverable amount. See Note 12 for information related to a regulatory asset that we recorded associated with our assets held for sale.

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 6 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 estimated 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.

#### ***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. See Note 6 for a further discussion of our asset retirement obligations.

#### ***Asset and Investment Impairments***

We evaluate our assets and investments 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 values based on either (i) the long-lived asset's ability to generate future cash flows on an undiscounted basis or (ii) the fair value of the investment in an unconsolidated affiliate. 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.

We classify assets (or groups of assets) to be disposed of as held for sale when specific criteria have been met. The lower of the carrying value or the estimated fair value less cost to sell of those assets is considered to determine if recognition of an impairment is required. We cease depreciation and amortization of the assets in the period they are considered held for sale.

### ***Equity Method of Accounting***

We account for investments, which we do not control but do have the ability to exercise significant influence, by the equity method of accounting. Under this method, our equity investments are carried originally at our acquisition costs, increased by our proportionate share of the investee's net income and by contributions made, and decreased by our proportionate share of the investee's net losses and by distributions received. We have a 50% ownership interest in Bear Creek Storage Company, L.L.C. (Bear Creek), a joint venture equally owned with Southern Natural Gas Company, L.L.C. (SNG), our affiliate. We accounted for our investment in Bear Creek using the equity method of accounting. We and SNG provide storage services to our customers utilizing the Bear Creek storage facilities.

### ***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 \$3,249 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. Prior to the implementation of a fuel volume tracker effective June 1, 2011 as part of our rate case filed with the FERC, gas not used in operations was based on the volumes we were allowed to retain relative to the amounts of gas we used for operating purposes. We recognized revenue on gas not used in operations from our shippers when we retained the volumes at the market prices required under our tariff.

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 no reserves for potential refunds as of December 31, 2012.

### ***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 10.

### ***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 10.

### ***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. This 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 8.

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 October 1, 2011, we changed our tax entity status from a corporation to a limited liability company. Prior to KMP's acquisition further discussed below, we continued to record federal income taxes on a separate return basis as a single member limited liability company. Pursuant to El Paso's policy, 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.

Effective with KMP's acquisition of us 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 tax balances with recoveries of our note receivable from KMI under its cash management program pursuant to our tax sharing agreement with El Paso. See Notes 4 and 9 for further discussion of our income taxes.

### ***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, 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 in periods prior to 2011 when our rate case was settled, losses on reacquired debt, losses on assets held for sale, taxes related to an equity return component on regulated capital projects in periods prior to our change in legal structure to non taxable entity, 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 12 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.....	\$	132
Property, plant and equipment, net <sup>(1)</sup> .....		4,070
Goodwill <sup>(2)</sup> .....		3,249
Other non-current assets <sup>(3)</sup> .....		1,089
Long-term debt <sup>(4)</sup> .....		(2,211)
Deferred income taxes <sup>(5)</sup> .....		(732)
Other liabilities .....		(339)
Total purchase price .....	\$	<u>5,258</u>

- (1) Property, plant and equipment includes a \$1.9 billion reduction to record our business at its regulatory value in conformity with our accounting policy.
- (2) Goodwill of \$3.2 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 \$442 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 \$442 million purchase price adjustment. This purchase price adjustment has been reported as "Debt fair value adjustments" on our Consolidated Balance Sheet.
- (5) Deferred income taxes include a purchase price reduction adjustment of \$722 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 second quarter of 2013.

#### *Expenses Related to KMI's Acquisition of El Paso*

We incurred acquisition-related expenses of \$45 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 October 1, 2011, we changed our tax entity status from a corporation to a limited liability company. Prior to KMP's acquisition further discussed below, we continued to record federal income taxes on a separate return basis and reflected current and deferred income taxes in our financial statements as a single member limited liability company.

Effective with KMP's acquisition of us 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 net current and deferred income tax liability balances of \$745 million, pursuant to our tax sharing agreement with El Paso with recoveries of our accounts and note receivable from KMI of \$501 million and a non-cash contribution from KMP of \$244 million. See Note 9 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).

	<u>Successor</u>	<u>Predecessor</u>	
	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 .....	\$ —	\$ —	\$ 13
State .....	(9)	—	4
	<u>(9)</u>	<u>—</u>	<u>17</u>
Deferred			
Federal .....	9	(5)	96
State .....	1	—	(11)
	<u>10</u>	<u>(5)</u>	<u>85</u>
Total income tax expense (benefit) .....	<u>\$ 1</u>	<u>\$ (5)</u>	<u>\$ 102</u>

### Effective Tax Rate Reconciliation

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

	<u>Successor</u>	<u>Predecessor</u>	
	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% .....	\$ 64	\$ (5)	\$ 107
State income taxes, net of federal income tax effect .....	1	—	(5)
Non-taxable earnings .....	(55)	—	—
Uncertain tax positions reversal .....	(9)	—	—
Income tax expense (benefit) .....	<u>\$ 1</u>	<u>\$ (5)</u>	<u>\$ 102</u>
Effective tax rate .....	<u>1%</u>	<u>38%</u>	<u>33%</u>

During 2011, we recorded a \$14 million deferred state tax benefit to correct the estimated effective tax rate applicable to differences in financial statement and tax bases of property, plant and equipment. In December 2012, we recognized a state income tax benefit of \$9 million due to the statute expiration of uncertain tax positions.

### Deferred Tax Assets and Liabilities

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

	<u>Predecessor</u>
Deferred tax liabilities	
Property, plant and equipment .....	\$ 1,787
Other .....	20
Total deferred tax liability .....	<u>1,807</u>
Deferred tax assets	
Net operating loss and tax credit carryovers	
U.S. Federal .....	250
State .....	30
Other liabilities .....	65
Total deferred tax asset .....	<u>345</u>
Net deferred tax liability .....	<u>\$ 1,462</u>

## 5. Assets Held for Sale

In November 2011, the FERC issued an order approving, in part, and rejecting certain portions of our abandonment application related to our October 2010 agreement to sell certain of our offshore pipeline assets and related facilities. The sale was contingent upon receiving approval to collect in our future rates the difference between the regulatory net book value and the purchase price (loss) and the designation of certain facilities as non-jurisdictional. In December 2011, we filed a request for partial rehearing and stay of the November order, which was denied by the FERC in March 2012. In April 2012, we entered into an amended and restated purchase and sale agreement which includes additional offshore and onshore assets. We filed a new abandonment application with the FERC in July 2012 and as a condition of the sale, we intend to recover a regulatory asset for a portion of the loss on sale. During the second quarter of 2012, we classified these assets as held for sale at fair value which approximates the sales price of \$32 million. The fair value is based on observable market data which is a Level 2 measurement. We recorded a regulatory asset of approximately \$113 million for the portion of the loss that we expect to recover through our jurisdictional transportation rates as outlined in the FERC filing. The sale is contingent upon receiving an acceptable FERC approval of the abandonment application including the ability to recover the regulatory asset in our future rates, which we believe is probable, based on the general support of our customer group and the underlying facts supporting the abandonment by sale. Additionally, we recorded a \$125 million charge to earnings to write down the book value of certain of the offshore assets, representing the portion of the loss not expected to be recovered through the rate making process.

## 6. 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.....	1.2 – 6.67	\$ 3,319	\$ 4,591
General plant .....	3.1 – 24.0	173	210
Intangible plant.....	3.1 – 14.0	102	103
Other <sup>(1)</sup> .....		238	2,491
Accumulated depreciation and amortization <sup>(1)(2)</sup> .....		(103)	(1,500)
		3,729	5,895
Land.....		10	10
Construction work in progress.....		126	134
Property, plant and equipment, net .....		\$ 3,865	\$ 6,039

(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 Successor period in 2012, the Predecessor period in 2012 and year ended December 31, 2011 were approximately 2.2%, 2.2% and 2.1%, 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 \$2.4 billion and accumulated depreciation was approximately \$498 million. These additional acquisition costs were being amortized on a straight-line basis over 62 years and were not recoverable in our rates under FERC policies. Our amortization expense related to these additional acquisition costs was approximately \$16 million and \$40 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.

### Capitalized Costs During Construction

	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
Allowance for debt amounts capitalized.....	\$ 2	\$ 1	\$ 12
Allowance for equity amounts capitalized.....	4	2	22

### Asset Retirement Obligations

We have legal obligations associated with the retirement of our natural gas pipeline, transmission facilities and storage wells. We have obligations to plug storage wells when we no longer plan to use them and when we abandon them. Our legal obligations associated with our natural gas transmission facilities primarily involve purging, sealing and possibly removing the facilities if they are abandoned. We also have obligations to remove hazardous materials associated with our natural gas transmission facilities if they are ever demolished or replaced. We continue to evaluate our asset retirement obligations and future developments could impact the amounts we record.

Where we can reasonably estimate the asset retirement obligation, we accrue a liability based on an estimate of the timing and amount of settlement. Current obligations are measured at the expected cost to complete the asset retirements. We record changes in these estimates based on changes in the expected amount and timing of payments to settle our obligations. We intend on operating and maintaining our natural gas pipeline and storage systems 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 and storage system assets because these assets have indeterminate lives.

The net asset retirement obligation reported on our balance sheets under current and other long-term liabilities, and the changes in the net liability for each of the periods presented below were 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
Net asset retirement obligation at beginning of period.....	\$ 42	\$ 23	\$ 29
Liabilities settled.....	(3)	(3)	(2)
Liabilities incurred.....	—	18	—
Changes in estimate.....	(17)	4	(4)
Net asset retirement obligation at end of period <sup>(1)</sup> .....	<u>\$ 22</u>	<u>\$ 42</u>	<u>\$ 23</u>

(1) As of December 31, 2012 and 2011, approximately \$21 million and \$22 million were reflected as current “Asset retirement obligations” on our Consolidated Balance Sheets, respectively.

### 7. Debt

We classify our debt based on the contractual maturity dates of the underlying debt instruments. We defer costs associated with debt issuance over the applicable term. These costs are then amortized as interest expense in our Consolidated Statements of Income and Comprehensive Income. 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
8.0% Notes due February 2016 .....	\$ 250	\$ 250
7.5% Debentures due April 2017.....	300	300
7.0% Debentures due March 2027.....	300	300
7.0% Debentures due October 2028 .....	400	400
8.375% Notes due June 2032.....	240	240
7.625% Debentures due April 2037.....	<u>300</u>	<u>300</u>
	1,790	1,790
Less: unamortized discount .....	—	<u>22</u>
Total long-term debt .....	<u>\$ 1,790</u>	<u>\$ 1,768</u>

## *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 period in 2012, the Predecessor period in 2012 and the year ended December 31, 2011, we were in compliance with our debt-related covenants.

## **8. 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 were 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. We made a contribution of approximately \$2 million in 2011. There was no contribution made in both the Successor and Predecessor periods in 2012.

### *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 "Member's 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 \$4 million (net of income taxes of \$2 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):

	<b>Successor</b>	<b>Predecessor</b>	
	<b>Period from Acquisition May 25, 2012 to December 31, 2012</b>	<b>Period from January 1, 2012 to May 24, 2012</b>	<b>Year Ended December 31, 2011</b>
Change in accumulated postretirement benefit obligation:			
Accumulated postretirement benefit obligation — beginning of period .....	\$ 18	\$ 18	\$ 18
Interest cost .....	—	—	1
Participant contributions .....	—	—	1
Plan amendments .....	(2)	—	—
Benefits paid <sup>(1)</sup> .....	(1)	(1)	(2)
Actuarial loss .....	1	—	—
Accumulated postretirement benefit obligation — end of period .....	\$ 16	\$ 17	\$ 18

Change in plan assets:		
Fair value of plan assets — beginning of period .....	\$ 45	\$ 44 \$ 41
Actual return on plan assets .....	4	1 2
Employer contributions.....	—	— 2
Participant contributions .....	—	— 1
Benefits paid.....	(1)	(1) (2)
Fair value of plan assets — end of period.....	<u>\$ 48</u>	<u>\$ 44</u> <u>\$ 44</u>
Reconciliation of funded status:		
Fair value of plan assets.....	\$ 48	\$ 44
Less: accumulated postretirement benefit obligation.....	<u>16</u>	<u>18</u>
Net asset at December 31 <sup>(2)</sup> .....	<u>\$ 32</u>	<u>\$ 26</u>

(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” in our Consolidated Balance Sheets.

### ***Components of Accumulated Other Comprehensive Income***

The amount 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 \$3 million and \$4 million (net of income taxes of \$2 million), respectively, is 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 plan, 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 \$46 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 \$42 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).

<u>Year Ending December 31,</u>	<u>Successor Expected Payments<sup>(1)</sup></u>
2013 .....	\$ 2
2014 .....	2
2015 .....	1
2016 .....	1
2017 .....	1
2018 - 2022 .....	5

(1) Includes a reduction of less than \$1 million in each of the years 2013 – 2017 and approximately \$1 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.

	<u>Successor</u>	<u>Predecessor</u>	
	<u>Period from Acquisition May 25, 2012 to December 31, 2012</u>	<u>Period from January 1, 2012 to May 24, 2012</u>	<u>Year Ended December 31, 2011</u>
	(%)	(%)	(%)
Assumptions related to benefit obligations at period end:			
Discount rate .....	3.13	4.30	4.30
Assumptions related to benefit costs for the period:			
Discount rate <sup>(1)</sup> .....	4.08	4.30	4.82
Expected return on plan assets <sup>(2)</sup> .....	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 the accumulated postretirement benefit obligation or interest costs for the Successor period in 2012, the Predecessor period in 2012 and the year ended December 31, 2011.

### Components of Net Benefit Income

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

	<u>Successor</u>	<u>Predecessor</u>	
	<u>Period from Acquisition May 25, 2012 to December 31, 2012</u>	<u>Period from January 1, 2012 to May 24, 2012</u>	<u>Year Ended December 31, 2011</u>
Interest cost .....	\$ —	\$ —	\$ 1
Expected return on plan assets .....	(2)	(1)	(2)
Net benefit (income) expense .....	<u>\$ (2)</u>	<u>\$ (1)</u>	<u>\$ (1)</u>

## **9. Related Party Transactions**

### ***Non-cash Contribution and Distributions***

Effective August 1, 2012, KMP acquired the full ownership interest in us from KMI. In conjunction with this acquisition, we settled our net current and deferred income tax liability balances of \$745 million with a non-cash contribution of \$244 million from KMP and recoveries of our accounts and note receivable from KMI of \$501 million as of July 31, 2012.

In October 2011, we made a non-cash distribution of our corporate facilities and certain other assets and liabilities to our then parent, El Paso. The net distributions were approximately \$325 million, which represented the historical costs of these assets and liabilities.

### ***Income Taxes***

Effective October 1, 2011, we changed our tax entity status from a corporation to a limited liability company. Prior to KMP's acquisition, we continued to record federal income taxes on a separate return basis as a single member limited liability company. El Paso filed consolidated U.S. federal and certain state tax returns which included our taxable income. As of December 31, 2011, we had net federal and state income tax receivable with El Paso of approximately \$1 million.

Effective with KMP's acquisition of us on August 1, 2012, we are no longer subject to either federal income taxes or generally to state income taxes.

### ***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 matches 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, 2012 and 2011, we had a note receivable from KMI and its affiliates and El Paso of \$139 million and \$519 million, respectively. The interest rate on this note was variable and was 0.5% and 2.5% as of December 31, 2012 and 2011, respectively. In conjunction with KMP's acquisition of us on August 1, 2012, we settled the outstanding note receivable from KMI under the cash management program for \$466 million.

### ***Other Affiliate Balances***

We enter into transactions with our affiliates within the ordinary course of our business and the services are based on the same terms as non-affiliates. In addition, we store natural gas in an affiliated storage facility and utilize the pipeline system of an affiliate to transport some of our natural gas.

During the first half of 2011, we sold 9.5 trillion British thermal units of natural gas not used in operations at a price of \$6.48 per million British thermal units to El Paso Marketing, L.P. In June 2011, we terminated the El Paso Marketing, L.P. contract to sell gas due to our implementation of a fuel volume tracker as part of our rate case filed with the FERC. See Note 15 for additional related information.

We do not have employees. Employees of KMI and its affiliates provide services to us. We are managed and operated by the officers of KMI and its affiliates. Under a master services agreement with El Paso and other 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. We also allocated costs to our pipeline affiliates, for their proportionate share of our pipeline services. The allocation from El Paso was 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.

The following table summarizes our other balance sheet affiliate balances (in millions):

	<u>Successor</u> <u>December 31,</u> <u>2012</u>	<u>Predecessor</u> <u>December 31,</u> <u>2011</u>
Accounts receivable.....	\$ 8	\$ 20
Accounts payable.....	43	45
Contractual deposits .....	—	10

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

	<u>Successor</u> <u>Period from</u> <u>Acquisition</u> <u>May 25, 2012</u> <u>to December 31,</u> <u>2012</u>	<u>Predecessor</u>	
		<u>Period from</u> <u>January 1,</u> <u>2012</u> <u>to May 24,</u> <u>2012</u>	<u>Year</u> <u>Ended</u> <u>December 31,</u> <u>2011</u>
Revenues <sup>(1)</sup> .....	\$ 4	\$ 11	\$ 90
Operation and maintenance expense <sup>(2)</sup> .....	144	120	131
Reimbursements of operating expense .....	15	27	77

(1) During the year ended December 31, 2011, we sold 9.5 trillion British thermal units of natural gas not used in operations to our affiliate, El Paso Marketing, L.P.

(2) The Successor period includes severance costs of \$45 million allocated to us from El Paso as a result of KMI's acquisition of El Paso.

## 10. Litigation, Environmental and Other Contingencies

### *Legal Proceedings*

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 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 adjust our accruals accordingly, and these adjustments could be material.

As of December 31, 2012 and 2011, we had approximately \$16 million and \$2 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 for environmental matters was each approximately \$5 million. Our accrual includes amounts for expected remediation costs and associated onsite, offsite and groundwater technical studies and related environmental legal costs. Our accrual as of December 31, 2012 includes approximately \$1 million for environmental contingencies related to properties we previously owned.

For 2013, we estimate that our total remediation expenditures will be approximately \$1 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 \$1 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 (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 United States 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.

#### *Polychlorinated Biphenyls (PCB) Cost Recoveries and Refund*

Since 1994, we have been conducting remediation activities at certain of our compressor stations associated with PCBs and other hazardous materials. We have collected amounts, substantially in excess of remediation costs incurred to date, through a surcharge to our customers under a settlement approved by the FERC in November of 1995. In November 2009, the FERC approved an amendment to the 1995 settlement that provides for interim refunds over a three year period of approximately \$157 million of our collected amounts plus interest of 8%. As of December 31, 2011, we reported approximately \$40 million for these refund obligations, including interest, as current "Regulatory liabilities" in our Consolidated Balance Sheets. We settled these remaining refund obligations during 2012.

#### *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 four 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 matters are included in the environmental reserve discussed above.

#### *Other Matters*

##### *Pipeline Hazardous Materials Safety Administration (PHMSA) Penalty*

On April 25, 2012, the U.S. Department of Transportation PHMSA issued a Notice of Proposed Violation (NOPV) against us proposing \$118,500 in penalties for alleged violations discovered during an inspection. We responded to the NOPV and paid the penalty.

##### *Administrative Order and Notice of Civil Administrative Penalty Assessment (AONOCAPA)*

On March 28, 2013, the New Jersey Department of Environmental Protection, Division of Compliance and Enforcement issued an AONOCAPA against us for \$175,000 and an action plan to address alleged deficiencies in our reforestation efforts following the 300 Line Project, which we placed into commercial operations on November 1, 2011. We are evaluating the AONOCAPA and will respond by requesting an administrative hearing and submitting a corrective action plan.

##### *Pennsylvania Department of Environmental Protection (PADEP)*

During construction and restoration of the 300 Line Project in 2011 and 2012, we received notices of violation from county conservation districts alleging noncompliance with permits from PADEP. The allegations focus on erosion control devices and best management practices to prevent sediment-laden water from leaving the construction right-of-way. PADEP has not taken any official action against us but has publicly confirmed that we are engaged in discussions regarding the notices.

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*

As of December 31, 2012, we have capital commitments of approximately \$215 million related to our Northeast Upgrade Project, which will be spent in 2013. We have other 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.

#### *Purchase Obligations*

We have entered into unconditional purchase obligations primarily for transportation, storage and other services, totaling \$154 million as of December 31, 2012. Our annual obligations under these purchase obligations are \$35 million in 2013, \$24 million in 2014, \$20 million in 2015, \$15 million in 2016, \$11 million in 2017, and \$49 million in total thereafter.

#### *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):

<b>Year Ending December 31,</b>	
2013 .....	\$ 1
2014 .....	1
2015 .....	1
2016 and thereafter .....	<u>—</u>
Total .....	<u>\$ 3</u>

Rental expense on our lease obligations for the Successor period in 2012, the Predecessor period in 2012 and the year ended December 31, 2011 were approximately \$1 million, \$1 million and \$2 million, respectively, and is reflected in “Operation and maintenance” expense on our Consolidated Statements of Income and Comprehensive Income.

## **11. Fair Value**

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

	<b>Successor</b>		<b>Predecessor</b>	
	<b>December 31, 2012</b>		<b>December 31, 2011</b>	
	<b>Carrying Amount</b>	<b>Fair Value</b>	<b>Carrying Amount</b>	<b>Fair Value</b>
Long-term debt .....	\$ 2,191 <sup>(1)</sup>	\$ 2,392	\$ 1,768	\$ 2,096

(1) Includes \$401 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 approximates 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 consist 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 Successor period in 2012, the Predecessor period 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.

## 12. 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):

	<u>Successor</u> <u>2012</u>	<u>Predecessor</u> <u>2011</u>
Current regulatory assets		
Difference between gas retained and gas consumed in operations .....	\$ 10	\$ 4
Other .....	4	3
Total current regulatory assets <sup>(1)</sup> .....	<u>14</u>	<u>7</u>
Non-current regulatory assets		
Taxes on capitalized funds used during construction .....	50	50
Unamortized loss on assets held for sale .....	113	—
Unamortized loss on reacquired debt.....	22	1
Other .....	3	4
Total non-current regulatory assets .....	<u>188</u>	<u>55</u>
Total regulatory assets .....	<u>\$ 202</u>	<u>\$ 62</u>
Current regulatory liabilities		
Environmental .....	\$ —	\$ 40
Other .....	2	—
Total current regulatory liabilities.....	<u>2</u>	<u>40</u>
Non-current regulatory liabilities		
Environmental .....	7	6
Other .....	11	5
Total non-current regulatory liabilities <sup>(2)</sup> .....	<u>18</u>	<u>11</u>
Total regulatory liabilities .....	<u>\$ 20</u>	<u>\$ 51</u>

(1) Included in "Other" current assets on our Consolidated Balance Sheets.

(2) 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-three years.

Our significant regulatory assets and liabilities include:

*Difference between gas retained and gas consumed in operations*

These amounts reflect the value of volumetric differences between gas retained and consumed in our operations. These amounts are not included in the rate base, but given our tariff, 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 the 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 assets held for sale*

Amount represents the deferred and unamortized portion of losses on our assets held for sale. We expect to recover this loss through our jurisdictional natural gas transportation rates.

*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 original life of the debt issue, or in the case of refinanced debt, over the life of the new debt issue.

*Environmental*

Includes amounts collected, substantially in excess of certain PCB environmental remediation costs incurred to date, through a surcharge to our customers under a settlement approved by the FERC in November of 1995. This environmental liability was not deducted from the rate base on which we are allowed to earn a return. For a further discussion of this PCB environmental matter, see Note 10.

### **13. Transactions with Major Customers**

For the Successor period in 2012, revenues from two non-affiliate customers were approximately \$70 million and \$63 million, each of which exceeded 10% of our operating revenues. For the Predecessor period in 2012, revenues from two non-affiliate customers were approximately \$52 million and \$45 million, each of which exceeded 10% of our operating revenues. For the year ended December 31, 2011, revenues from one non-affiliate customer was approximately \$132 million, which exceeded 10% of our operating revenues.

### **14. 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 \$45 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).

	<u>Successor</u>	<u>Predecessor</u>	
	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 <sup>(1)</sup> .....	\$ 69	\$ 381	\$ 981
Cash received for accounts receivable sold under the program .....	45	180	510
Deferred purchase price related to accounts receivable sold .....	24	201	471
Cash received related to the deferred purchase price .....	—	248	443
Cash paid in conjunction with terminated program .....	45	—	—

(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.

	<u>Predecessor</u>
	December 31, 2011 <sup>(2)</sup>
Accounts receivable sold and held by third-party financial institution .....	\$ 108
Uncollected deferred purchase price related to accounts receivable sold <sup>(2)(3)</sup> .....	63

(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 and note 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 Successor period in 2012, the Predecessor period in 2012 and the year ended December 31, 2011.

## 15. Regulatory Matters

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

### *Rate Case*

In December 2011, the FERC approved our settlement that resolved the outstanding rate issues arising from our general rate case filing. The settlement provides for, among other things, (i) an increase in our base tariff rates effective June 1, 2011, (ii) implementation of cost trackers for fuel and pipeline safety and greenhouse gas, (iii) significant contract extensions to October 2014, (iv) a filing requirement for our next general rate case to be effective no earlier than April 2014 but no later than November 2015, and (v) a revenue sharing mechanism with certain of our customers for certain revenues above an annual threshold. In addition, as part of the settlement, we refunded approximately \$69 million, including interest, to our customers in March 2012.

In addition to the provisions discussed above, the settlement also required us to reduce the net regulatory liabilities associated with our postretirement benefit plan and certain deferred taxes. We have reflected these adjustments in 2011 as an increase to our operating revenues of approximately \$40 million since these items were provided for under prior rate settlements and there is no funding requirement or cost recovery in our current rates for these items.

#### ***Proposed Sale of Production Area Facilities***

See assets held for sale discussion in Note 5.

#### ***Bear Creek***

In November 2011, Bear Creek, our unconsolidated affiliate, received an order from the FERC related to an investigation into the rates charged to customers. The FERC ordered Bear Creek to file a full cost and revenue study within 75 days of the order. Bear Creek filed the cost and revenue study in January 2012. In June 2012, Bear Creek filed an uncontested settlement which resolved all of the issues in the proceedings. Under the settlement, Bear Creek agreed to reduce its rates to its two customers including us and SNG, our affiliate. The settlement was approved by the FERC on August 15, 2012. The impact of the settlement is not expected to materially affect our financial statements.

#### ***Northeast Supply Diversification Project (Docket No. CP11-30-000)***

On September 10, 2011, the FERC issued an order authorizing the expansion of our pipeline facilities in northern Pennsylvania and western New York along with an associated lease of transportation capacity from Dominion Transmission, Inc. in order to provide incremental firm transportation service to shippers of approximately 245 million cubic feet per day of natural gas produced in the Marcellus Shale supply area to northeast markets. The capital cost of the project was approximately \$55 million and the capacity is fully subscribed under long-term contracts. The project was completed and placed into service on November 1, 2012.

#### ***Northeast Upgrade Project (Docket No. CP11-161-000)***

On May 29, 2012, the FERC issued an order authorizing the expansion of our pipeline facilities in Pennsylvania and New Jersey that will provide needed infrastructure to support continued development of Marcellus shale natural gas production and increase our delivery capacity in the region by approximately 620 million cubic feet per day. The estimated capital cost of the project is approximately \$450 million and the capacity is fully subscribed under long term contracts. With no stay of construction granted, and subject to receipt of final FERC and other regulatory agency approvals, the project is anticipated to be placed in service on November 1, 2013.

#### ***MPP Project (Docket No. CP12-28-000)***

On August 9, 2012, the FERC issued an order authorizing the expansion of our pipeline facilities in northwestern Pennsylvania that will provide needed infrastructure to support continued development of Marcellus shale natural gas production and increase our delivery capacity in the region by approximately 240 million cubic feet per day. The estimated capital cost of the project is approximately \$86 million, and the capacity is fully subscribed under long term contracts. The Marcellus Pooling project is anticipated to be placed in service on November 1, 2013.

#### ***Rose Lake Expansion Project (Docket No. CP13-03-000)***

On October 10, 2012, we filed an application with the FERC requesting authority to expand our pipeline capacity in northern Pennsylvania through the installation and modification of new and existing compression facilities that will result in increased capacity of approximately 225 million cubic feet per day and will improve the efficiency and reduce emissions by replacing certain older existing compression facilities. The project will further support continued development of Marcellus shale natural gas production in the region. The estimated capital cost of the project is approximately \$92 million and the capacity is fully subscribed under long term contracts. The project is anticipated to be placed in service on November 1, 2014.