



**Northern Natural Gas Company**

**Financial Statements and Independent Auditors' Report  
as of and for the  
Years Ended December 31, 2019 and 2018**



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## **INDEPENDENT AUDITORS' REPORT**

To the Board of Directors and Shareholder of  
Northern Natural Gas Company  
Omaha, Nebraska

We have audited the accompanying financial statements of Northern Natural Gas Company (the "Company"), which comprise the balance sheets as of December 31, 2019 and 2018, and the related statements of income, comprehensive income, changes in shareholder's equity, and cash flows for the years then ended, and the related notes to the financial statements.

### **Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these 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 financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditors' Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the 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 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 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 financial statements referred to above present fairly, in all material respects, the financial position of Northern Natural Gas Company as of December 31, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*Deloitte & Touche LLP*

Omaha, Nebraska  
March 30, 2020

**Northern Natural Gas Company**  
**Balance Sheets**  
(Amounts in thousands, except share data)

	<b>As of December 31,</b>	
	<b>2019</b>	<b>2018</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 38,792	\$ 14,749
Accounts receivable, net	94,427	107,776
Accounts receivable from affiliates	8,278	9,246
Notes receivable from BHE	240,000	305,000
Transportation and exchange gas receivables	5,365	16,231
Inventories	41,951	35,657
Income tax receivable	9,519	466
Other current assets	31,886	27,571
Total current assets	<u>470,218</u>	<u>516,696</u>
Property, plant and equipment, net	3,970,699	3,359,034
Regulatory assets	100,340	116,848
Other assets	61,538	49,424
<b>Total assets</b>	<u><b>\$ 4,602,795</b></u>	<u><b>\$ 4,042,002</b></u>
<b>LIABILITIES AND SHAREHOLDER'S EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 101,077	\$ 71,735
Accounts payable to affiliates	1,199	1,191
Accrued interest	19,877	15,804
Accrued property, income and other taxes	54,246	56,395
Transportation and exchange gas payables	3,309	14,740
Other current liabilities	52,530	34,176
Total current liabilities	<u>232,238</u>	<u>194,041</u>
Long-term debt	1,247,108	1,041,512
Regulatory liabilities	426,624	434,362
Deferred income taxes	583,407	523,715
Asset retirement obligations	15,290	33,290
Other long-term liabilities	45,834	38,921
Total liabilities	<u>2,550,501</u>	<u>2,265,841</u>
Commitments and contingencies (Note 12)		
Shareholder's equity:		
Series A preferred stock - 1,000 shares authorized, \$0.01 par value, no shares issued and outstanding	—	—
Common stock - 10,000 shares authorized, \$1.00 par value, 1,002 shares issued and outstanding	1	1
Additional paid-in capital	981,868	981,868
Retained earnings	1,068,149	794,292
Accumulated other comprehensive income, net	2,276	—
Total shareholder's equity	<u>2,052,294</u>	<u>1,776,161</u>
<b>Total liabilities and shareholder's equity</b>	<u><b>\$ 4,602,795</b></u>	<u><b>\$ 4,042,002</b></u>

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



**Northern Natural Gas Company**  
**Statements of Income**  
(Amounts in thousands)

	<b>Years Ended December 31,</b>	
	<b>2019</b>	<b>2018</b>
<b>Operating revenue:</b>		
Transportation	\$ 745,358	\$ 691,550
Storage	65,008	67,545
Gas, liquids and other sales	41,882	130,526
Total operating revenue	<u>852,248</u>	<u>889,621</u>
<b>Operating expenses:</b>		
Operations and maintenance	297,135	299,116
Cost of gas and liquids sales	39,262	137,987
Depreciation and amortization	89,209	81,763
Taxes, other than income taxes	45,675	53,424
Total operating expenses	<u>471,281</u>	<u>572,290</u>
<b>Operating income</b>	<u>380,967</u>	<u>317,331</u>
<b>Other income (expense):</b>		
Interest expense, net	(49,548)	(41,513)
Interest income	13,991	8,455
Other, net	21,169	12,402
Total other income (expense)	<u>(14,388)</u>	<u>(20,656)</u>
<b>Income before income tax expense</b>	366,579	296,675
Income tax expense	92,722	70,552
<b>Net income</b>	<u>\$ 273,857</u>	<u>\$ 226,123</u>

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

**Northern Natural Gas Company**  
**Statements of Comprehensive Income**  
(Amounts in thousands)

	<b>Years Ended December 31,</b>	
	<b>2019</b>	<b>2018</b>
Net income	\$ 273,857	\$ 226,123
Other comprehensive income, net of tax-		
Unrealized gains on cash flow hedges, net of tax of \$828 and \$-	2,276	—
Comprehensive income	<u>\$ 276,133</u>	<u>\$ 226,123</u>

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

**Northern Natural Gas Company**  
**Statements of Changes in Shareholder's Equity**  
(Amounts in thousands)

	<u>Common Stock</u>	<u>Additional Paid-In Capital</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income, net</u>	<u>Total</u>
<b>Balance, December 31, 2017</b>	\$ 1	\$ 981,868	\$ 598,169	\$ —	\$ 1,580,038
Net income	—	—	226,123	—	226,123
Dividends on common stock	—	—	(30,000)	—	(30,000)
<b>Balance, December 31, 2018</b>	1	981,868	794,292	—	1,776,161
Net income	—	—	273,857	—	273,857
Other comprehensive income - cash flow hedges	—	—	—	2,276	2,276
<b>Balance, December 31, 2019</b>	<u>\$ 1</u>	<u>\$ 981,868</u>	<u>\$ 1,068,149</u>	<u>\$ 2,276</u>	<u>\$ 2,052,294</u>

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

**Northern Natural Gas Company**  
**Statements of Cash Flows**  
(Amounts in thousands)

	<b>Years Ended December 31,</b>	
	<b>2019</b>	<b>2018</b>
<b>Cash flows from operating activities:</b>		
Net income	\$ 273,857	\$ 226,123
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation and amortization	89,209	81,763
Amortization of debt issuance costs	401	452
Deferred income taxes	52,625	19,108
Other, net	(6,543)	714
Changes in other operating assets and liabilities:		
Accounts receivable and other assets	(22,007)	(7,351)
Inventories	(6,294)	(5,619)
Accounts payable and other accrued liabilities	7,357	11,523
Gas balancing activities	39,517	(28,203)
Accrued property, income and other taxes	(11,203)	13,897
Net cash flows from operating activities	<u>416,919</u>	<u>312,407</u>
<b>Cash flows from investing activities:</b>		
Capital expenditures	(659,265)	(396,311)
Purchases of marketable securities	(16,535)	(9,520)
Proceeds from sales of marketable securities	15,459	5,786
Other	—	206
Net cash flows from investing activities	<u>(660,341)</u>	<u>(399,839)</u>
<b>Cash flows from financing activities:</b>		
Proceeds from long-term debt	205,252	445,248
Repayment of long-term debt	—	(200,000)
Issuance of promissory notes by BHE	(350,000)	(570,000)
Proceeds from redemption of promissory notes from BHE	415,000	440,000
Dividends on common stock	—	(30,000)
Net cash flows from financing activities	<u>270,252</u>	<u>85,248</u>
<b>Net change in cash and cash equivalents and restricted cash and cash equivalents</b>	<b>26,830</b>	<b>(2,184)</b>
<b>Cash and cash equivalents and restricted cash and cash equivalents at beginning of period</b>	<b>27,575</b>	<b>29,759</b>
<b>Cash and cash equivalents and restricted cash and cash equivalents at end of period</b>	<b>\$ 54,405</b>	<b>\$ 27,575</b>
<b>Supplemental Disclosure:</b>		
Interest paid, net of amounts capitalized	\$ 44,976	\$ 37,379
Income taxes paid	\$ 52,610	\$ 38,467
Non-cash investing transactions-		
Accruals related to property, plant and equipment additions	\$ 95,786	\$ 63,456

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

## **Northern Natural Gas Company**

### **Notes to Financial Statements**

#### **(1) Organization and Operations**

Northern Natural Gas Company (the "Company") is an indirect wholly owned subsidiary of Berkshire Hathaway Energy Company ("BHE"), a holding company that owns locally managed businesses principally engaged in the energy industry. BHE is a consolidated subsidiary of Berkshire Hathaway Inc. ("Berkshire Hathaway"). The Company owns the largest interstate natural gas pipeline system in the United States, as measured by pipeline miles, which reaches from west Texas to Michigan's Upper Peninsula (the "System"). The Company primarily transports and stores natural gas for utilities, municipalities, gas marketing companies and industrial and commercial users. The System consists of two commercial segments. Its traditional end-use and distribution market area in the northern part of its system, referred to as the Market Area, includes points in Iowa, Nebraska, Minnesota, Wisconsin, South Dakota, Michigan and Illinois. Its natural gas supply and delivery service area in the southern part of its system, referred to as the Field Area, includes points in Kansas, Texas, Oklahoma and New Mexico. The Market Area and Field Area are separated at a Demarcation Point. The System consists of 14,600 miles of natural gas pipelines, including 6,100 miles of mainline transmission pipelines and 8,500 miles of branch and lateral pipelines, with a Market Area design capacity of 6.3 billion cubic feet ("Bcf") per day, a Field Area delivery capacity of 1.7 Bcf per day to the Market Area and 1.4 Bcf per day to the West Texas area and over 79 Bcf of firm service and operational storage cycle capacity in five storage facilities. The System is configured with approximately 2,250 active receipt and delivery points which are integrated with the facilities of local distribution companies ("LDC"). Many of the Company's LDC customers are part of combined utilities that also use natural gas as a fuel source for electric generation. The Company delivered over 1.4 trillion cubic feet of natural gas to its customers in 2019.

#### **(2) Summary of Significant Accounting Policies**

##### *Basis of Presentation*

The Company has no subsidiaries and does not hold a controlling financial interest in any other entity. The Financial Statements are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP").

##### *Use of Estimates in Preparation of Financial Statements*

The preparation of the Financial Statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. These estimates include, but are not limited to, the effects of regulation; unbilled revenue; income taxes; valuation of certain financial assets and liabilities, including derivative contracts; long-lived asset recovery; asset retirement obligations ("AROs"); and accounting for contingencies. Actual results may differ from the estimates used in preparing the Financial Statements. The Company has evaluated subsequent events through March 30, 2020, which is the date the audited Financial Statements were available to be issued. There were no subsequent events that required adjustment to, or disclosure in, the Financial Statements, except as disclosed in Notes 12 and 15.



### *Accounting for the Effects of Certain Types of Regulation*

The Company prepares its financial statements in accordance with authoritative guidance for regulated operations, which recognizes the economic effects of regulation. Accordingly, the Company is required to defer the recognition of certain costs or income if it is probable that, through the ratemaking process, there will be a corresponding increase or decrease in future regulated rates. Regulatory assets and liabilities are established to reflect the impacts of these deferrals.

The Company continually evaluates the applicability of the guidance for regulated operations and whether its regulatory assets and liabilities are probable of inclusion in future regulated rates by considering factors such as a change in the regulator's approach to setting regulated rates from cost-based ratemaking to another form of regulation, other regulatory actions or the impact of competition that could limit the Company's ability to recover its costs. The Company believes the application of the guidance for regulated operations is appropriate and its existing regulatory assets and liabilities are probable of inclusion in future regulated rates. The evaluation reflects the current political and regulatory climate at the federal level. If it becomes no longer probable that the deferred costs or income will be included in future regulated rates, the related regulatory assets and liabilities will be written-off to net income, returned to customers or re-established as accumulated other comprehensive income (loss) ("AOCI").

### *Fair Value Measurements*

As defined under GAAP, fair value is the price that would be received to sell an asset or paid to transfer a liability between market participants in the principal market or in the most advantageous market when no principal market exists. Adjustments to transaction prices or quoted market prices may be required in illiquid or disorderly markets in order to estimate fair value. Alternative valuation techniques may be appropriate under the circumstances to determine the value that would be received to sell an asset or paid to transfer a liability in an orderly transaction. Market participants are assumed to be independent, knowledgeable, able and willing to transact an exchange and not under duress. Nonperformance or credit risk is considered in determining fair value. Considerable judgment may be required in interpreting market data used to develop the estimates of fair value. Accordingly, estimates of fair value presented herein are not necessarily indicative of the amounts that could be realized in a current or future market exchange.

### *Cash Equivalents and Restricted Cash and Cash Equivalents*

Cash equivalents consist of funds invested in money market mutual funds and other investments with a maturity of three months or less when purchased. Cash and cash equivalents exclude amounts where availability is restricted by legal requirements or other contractual provisions. Restricted amounts are included in other current assets and other assets on the Balance Sheets.

### *Allowance for Doubtful Accounts*

Accounts receivable are stated at the outstanding principal amount, net of an estimated allowance for doubtful accounts. The allowance for doubtful accounts is based on the Company's assessment of the collectability of amounts owed to the Company by its customers. This assessment requires judgment regarding the ability of



customers to pay or the outcome of any pending disputes. As of December 31, 2019 and 2018, the allowance for doubtful accounts was insignificant and is included in accounts receivable, net on the Balance Sheets.

### *Transportation Imbalances*

Shippers schedule their volumes into the Company's System with subsequent deliveries to various markets. Imbalance receivables from and payables to shippers are created when receipts to the System from shippers vary from deliveries off the System, excluding quantities retained by the pipeline for fuel. Receipts and deliveries from third parties in connection with balancing and other gas service contracts also result in imbalances. Such imbalances are valued at contractual or market rates and recorded as transportation and exchange gas receivables or payables on the Balance Sheets with offsetting entries to cost of gas and liquids sales on the Statements of Income. The imbalances cause offsetting changes in the volumes of system balancing gas, which are priced at contractual or market rates, and are recorded as adjustments to system gas balances in property, plant and equipment, net on the Balance Sheets and to cost of gas and liquids sales on the Statements of Income. Settlement of imbalances occurs in accordance with the contractual terms of the agreements and timing of delivery of gas based on operational conditions.

### *Inventories*

Inventories consist primarily of materials and supplies, which mainly include replacement parts used in the periodic overhaul of gas compressor units and materials for construction, operation and maintenance and are stated at average cost.

### *Derivatives*

The Company employs a number of different derivative contracts, which may include forward gas purchase and gas sale contracts and gas price commodity and basis swaps to manage price risk for natural gas. Derivative contracts are recorded on the Balance Sheets as either assets or liabilities and are stated at estimated fair value unless they are designated as normal purchases or normal sales and qualify for the exception afforded by GAAP. Derivative balances reflect offsetting permitted under master netting agreements with counterparties.

Commodity derivatives used in normal business operations that are settled by physical delivery, among other criteria, are eligible for and may be designated as normal purchases or normal sales. Normal purchases or normal sales contracts are not marked-to-market and settled amounts are recognized as operating revenue or cost of gas and liquids sales on the Statements of Income.

For the Company's derivatives not designated as hedging contracts, the settled amount is generally includable in regulated rates. Accordingly, the net unrealized gains and losses associated with interim price movements on contracts that are accounted for as derivatives and probable of inclusion in regulated rates are recorded as regulatory assets and liabilities.

For the Company's derivatives designated as hedging contracts, the Company formally assesses, at inception and thereafter, whether the hedging contract is highly effective in offsetting changes in the hedged item. The Company formally documents hedging activity by transaction type and risk management strategy.

## *Property, Plant and Equipment, Net*

### *General*

Additions to property, plant and equipment are recorded at cost. The Company capitalizes all construction-related material, direct labor and contract services, as well as indirect construction costs, which include debt and equity allowance for funds used during construction ("AFUDC") on rate base assets. The cost of additions and betterments are capitalized, while costs incurred that do not improve or extend the useful lives of the related assets are generally expensed. The Company is permitted to earn a return on the cost of its rate base assets as well as recover these costs through depreciation expense over the useful lives of the assets.

Depreciation and amortization are computed by applying the composite or straight-line method based on either estimated useful lives or mandated recovery periods as prescribed by the Federal Energy Regulatory Commission ("FERC"). Depreciation studies are completed by the Company to determine the appropriate group lives, net salvage and group depreciation rates. These studies are reviewed and rates are ultimately approved by the FERC. Under the composite method when property, plant and equipment is retired, the original cost of the property retired is charged to accumulated depreciation and amortization, net of salvage and removal costs. For general plant, the original cost of the property retired is charged to accumulated depreciation and amortization at the end of the depreciable lives of the asset vintages. Retirement gains or losses are not included in income except in the case of sales of operating units.

The Company capitalizes debt and equity AFUDC, which represents the cost of debt and equity funds necessary to finance the construction of regulated facilities, as a component of property, plant and equipment, with offsetting credits to the Statements of Income. AFUDC is computed based on guidelines set forth by the FERC.

AFUDC on borrowed funds totaled \$2.4 million and \$1.6 million for the years ended December 31, 2019 and 2018, respectively, and is included in interest expense, net on the Statements of Income. AFUDC on equity funds totaled \$10.7 million and \$7.5 million for the years ended December 31, 2019 and 2018, respectively, and is included in other, net on the Statements of Income.

### *System Gas*

Storage base gas and system balancing gas are accounted for utilizing the fixed asset accounting method as prescribed by the FERC. Under this approach, system gas volumes are classified as property, plant and equipment, net and valued at cost. Temporary encroachments upon system gas are valued at contractual or current market prices.

### *Asset Retirement Obligations*

The Company recognizes AROs when it has a legal obligation to remove or abandon-in-place an asset upon retirement. The Company's AROs are related to the decommissioning of all offshore Gulf Coast facilities. The fair value of an ARO liability is recognized in the period in which it is incurred, if a reasonable estimate of fair value can be made, and is added to the carrying amount of the associated asset, which is then depreciated over the remaining useful life of the asset. Subsequent to the initial recognition, the ARO liability is adjusted for



any revisions to the original estimate of undiscounted cash flows (with corresponding adjustments to property, plant and equipment) and for accretion of the ARO liability due to the passage of time. The difference between the ARO liability, the corresponding ARO asset included in property, plant and equipment, net and amounts recovered in regulated rates to satisfy such liabilities is recorded as a regulatory asset or liability.

### *Impairment*

The Company evaluates long-lived assets for impairment, including property, plant and equipment, when events or changes in circumstances indicate that the carrying value of such assets may not be recoverable, or the assets are being held for sale. Upon the occurrence of a triggering event, the asset is reviewed to assess whether the estimated undiscounted cash flows expected from the use of the asset plus the residual value from the ultimate disposal exceeds the carrying value of the asset. If the carrying value exceeds the estimated recoverable amounts, the asset is written down to the estimated fair value and any resulting impairment loss is reflected on the Statements of Income. The impacts of regulation are considered when evaluating the carrying value of rate base assets.

### *Revenue Recognition*

The Company uses a single five-step model to identify and recognize revenue from contracts with customers ("Customer Revenue") upon transfer of control of promised services in an amount that reflects the consideration to which the Company expects to be entitled in exchange for those services.

Substantially all of the Company's revenue is derived from tariff-based transportation and storage arrangements approved by FERC. These tariff-based revenues have performance obligations to deliver services to customers which are satisfied over time as services are provided.

Revenue recognized is equal to what the Company has the right to invoice as it corresponds directly with the value to the customer of the Company's performance to date and includes billed and unbilled amounts. As of December 31, 2019 and 2018, unbilled revenue was \$6.9 million and \$6.2 million, respectively, and is included in accounts receivable, net on the Balance Sheets. The Company's transportation and storage revenue is primarily derived from fixed reservations charges based on contractual quantities and regulated rates. The remaining revenue, consisting primarily of commodity charges, is based on contractual rates and estimated usage based on scheduled quantities. Differences between scheduled quantities and actual measured quantities are reflected in revenue during the following month and historically have been immaterial.

The Company is subject to FERC regulations and, accordingly, certain revenue collected may be subject to possible refunds upon final FERC orders in pending regulated rate proceedings. The Company may record revenue that is subject to refund based on its best estimates of the final outcomes of such proceedings and other third party regulatory proceedings, advice of counsel and estimated total exposure, as well as collection and other risks. The Company had no earned revenue subject to refund for the years ended December 31, 2019 and 2018.

## *Income Taxes*

Berkshire Hathaway includes the Company in its consolidated United States federal income tax return. Consistent with established regulatory practice, the Company's provision for income tax expense has been computed on a stand-alone basis.

Deferred income tax assets and liabilities are based on differences between the financial statement and income tax basis of assets and liabilities using estimated income tax rates expected to be in effect for the year in which the differences are expected to reverse. Changes in deferred income tax assets and liabilities that are associated with components of other comprehensive income ("OCI") are charged or credited directly to OCI. Changes in deferred income tax assets and liabilities that are associated with property-related basis differences and other various differences that the Company deems probable of being reflected in future regulatory rates, are charged or credited directly to a regulatory asset or liability and will be included in rates when the temporary differences reverse. Other changes in deferred income tax assets and liabilities are included as a component of income tax expense. Changes in deferred income tax assets and liabilities attributable to changes in enacted income tax rates are charged or credited to income tax expense or a regulatory asset or liability in the period of enactment. Valuation allowances are established when necessary to reduce certain deferred income tax assets to the amount that is more-likely-than-not to be realized.

In determining the Company's income taxes, management is required to interpret complex income tax laws and regulations, which includes consideration of regulatory implications imposed by the FERC. The Company's income tax returns are subject to continuous examinations by federal and state income tax authorities that may give rise to different interpretations of these complex laws and regulations. Due to the nature of the examination process, it generally takes years before these examinations are completed and these matters are resolved. The Company recognizes the tax benefit from an uncertain tax position only if it is more-likely-than-not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the Financial Statements from such a position are measured based on the largest benefit that is more-likely-than-not of being realized upon ultimate settlement. Although the ultimate resolution of the Company's federal, state and local income tax examinations is uncertain, the Company believes it has made adequate provisions for these income tax positions. The aggregate amount of any additional income tax liabilities that may result from these examinations, if any, is not expected to have a material adverse impact on the Company's financial results. The Company's unrecognized tax benefits are included in other current assets and other long-term liabilities on the Balance Sheets. Estimated interest and penalties, if any, related to uncertain tax positions are included as a component of income tax expense on the Statements of Income.

## *New Accounting Pronouncements*

In February 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-02, which creates FASB Accounting Standards Codification ("ASC") Topic 842, "Leases" and supersedes Topic 840 "Leases." This guidance increases transparency and comparability among entities by recording lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. A lessee should recognize on the balance sheet a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. The recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee have



not significantly changed from previous guidance. Following the issuance of ASU No. 2016-02, the FASB issued several ASUs that clarified the implementation guidance for ASU No. 2016-02 but did not change the core principle of the guidance. The Company has elected to utilize various practical expedients available to adopt ASU No. 2016-02, including (1) the package of three not requiring a reassessment of (i) whether any expired or existing contracts are or contain leases; (ii) the lease classification for any expired or existing leases; and (iii) initial direct costs for any existing leases; (2) using hindsight in determining the lease term; and (3) not requiring a reassessment of whether existing or expired land easements that were not previously accounted for as leases under ASC Topic 840 are or contain a lease under ASC Topic 842. The Company adopted this guidance for all applicable contracts in effect as of January 1, 2019 under a modified retrospective method and the adoption did not have a cumulative effect impact at the date of initial adoption.

### **(3) Cash and Cash Equivalents and Restricted Cash and Cash Equivalents**

Cash equivalents consist of funds invested in money market mutual funds and other investments with a maturity of three months or less when purchased. Cash and cash equivalents exclude amounts where availability is restricted by legal requirements, loan agreements or other contractual provisions. Restricted cash and cash equivalents as of December 31, 2019 and December 31, 2018, consist substantially of escrow funds held to provide the Company with protection against customer credit risk. A reconciliation of cash and cash equivalents and restricted cash and cash equivalents as of December 31, 2019 and 2018, as presented in the Statements of Cash Flows is outlined below and disaggregated by the line items in which they appear on the Balance Sheets (in thousands):

	<b>As of December 31,</b>	
	<b>2019</b>	<b>2018</b>
Cash and cash equivalents	\$ 38,792	\$ 14,749
Restricted cash and cash equivalents in other current assets	2,156	337
Restricted cash and cash equivalents in other assets	13,457	12,489
Total cash and cash equivalents and restricted cash and cash equivalents	<u>\$ 54,405</u>	<u>\$ 27,575</u>

#### (4) Property, Plant and Equipment, Net

Property, plant and equipment, net consists of the following as of December 31 (in thousands):

	Depreciation Rates	2019	2018
Transmission and other plant	1.5% to 10.0%	\$ 4,150,000	\$ 3,648,045
Storage plant <sup>(1)</sup>	1.25% to 2.34%	796,636	725,685
Intangible plant <sup>(2)</sup>	4.4% to 10.0%	182,845	156,514
General plant and buildings	2.75% to 10.0%	129,377	105,439
Total operating assets		5,258,858	4,635,683
Accumulated depreciation and amortization		(1,336,567)	(1,367,461)
Net operating assets		3,922,291	3,268,222
Construction work-in-progress		48,408	90,812
Property, plant and equipment, net		\$ 3,970,699	\$ 3,359,034

- (1) Includes system-gas and market-based underground storage facilities. Recoverable system gas is not depreciated.
- (2) Includes costs for capitalized software development, contributions in aid of construction, organization and leasehold improvements.

The Company had gross costs for capitalized software development of \$167.3 million and \$134.9 million and accumulated amortization of \$71.4 million and \$65.2 million as of December 31, 2019 and 2018, respectively, which is included in intangible plant and reflected in property, plant and equipment, net on the Balance Sheets. Capitalized software development costs are amortized at a rate of 4.4%.

The Company had gross costs for capitalized right of use or right of way of \$109.5 million and \$109.7 million and accumulated amortization of \$39.8 million and \$37.9 million as of December 31, 2019 and 2018, respectively, which is included in transmission and other plant and storage plant and reflected in property, plant and equipment, net on the Balance Sheets. Capitalized right of use or right of way costs are amortized at rates ranging from 1.5% to 10.0%.

For the years ended December 31, 2019 and 2018, depreciation expense of \$80.2 million and \$73.2 million, respectively, and amortization expense of \$9.0 million and \$8.6 million, respectively, were included in depreciation and amortization on the Statements of Income. The Company expects amortization expense to be \$37.5 million for 2020, \$37.5 million for 2021, \$37.3 million for 2022, \$36.2 million for 2023 and \$34.7 million for 2024.

Effective January 1, 2020, the Company implemented new depreciation and amortization rates in its Docket No. RP19-1353 general rate case. The proposed depreciation and amortization rate changes in that docket include increases to 2.79% for onshore transmission plant, 3.11% for underground storage plant, 2.95% for LNG storage plant, 20.0% for intangible plant and 20.0% for computer equipment within general plant. The Company also proposed negative salvage rates of 0.96% for onshore transmission plant and 0.92% for LNG



storage plant. The depreciation, amortization and negative salvage rates are subject to the final outcome of the rate case proceedings in Docket Nos. RP19-1353. See Note 12.

## (5) Regulatory Matters

Regulatory assets represent costs that are expected to be recovered in future regulated rates. The Company's regulatory assets reflected on the Balance Sheets consist of the following as of December 31 (in thousands):

	<b>Remaining Life</b>	<b>2019</b>	<b>2018</b>
Deferred unamortized loss on derivative contract value	3 years	\$ 32,059	\$ 43,616
Smart pigging and hydrostatic testing costs <sup>(1)</sup>	7 years	26,344	26,708
Deferred income taxes associated with equity AFUDC <sup>(2)</sup>	67 years	20,406	16,756
Offshore negative salvage, including ARO <sup>(3)</sup>	3 years	3,251	14,896
Employee benefit plan <sup>(4)</sup>	12 years	15,013	14,533
Fuel trackers periodic rate adjustments	Various	—	11,568
Other	Various	4,763	1,673
Total regulatory assets		<u>\$ 101,836</u>	<u>\$ 129,750</u>
Reflected as:			
Other current assets		\$ 1,496	\$ 12,902
Noncurrent assets		100,340	116,848
Total regulatory assets		<u>\$ 101,836</u>	<u>\$ 129,750</u>

- (1) In compliance with a prior rate case settlement, the Company was able to defer \$7.5 million annually of smartpigging and hydrostatic testing costs and amortize over seven years. This treatment ended on January 1, 2020 in conjunction with the filing of the Section 4 rate case. See Note 12.
- (2) Amortized at the same rate as onshore transmission plant.
- (3) The Company was collecting \$4.3 million annually for ARO. In conjunction with the filing of the Section 4 rate case, the Company proposed to recover its remaining ARO costs over 16 years.
- (4) Represents amounts not yet recognized as a component of net periodic benefit cost that are expected to be included in regulated rates when recognized.

The Company had regulatory assets not earning a return on investment of \$38.4 million and \$56.5 million as of December 31, 2019 and 2018, respectively.

Regulatory liabilities represent income to be recognized or amounts to be returned to customers in future periods. The Company's regulatory liabilities reflected on the Balance Sheets consist of the following as of December 31 (in thousands):

	<b>Remaining Life</b>	<b>2019</b>	<b>2018</b>
Excess deferred income taxes <sup>(1)</sup>	Various	\$ 394,873	\$ 401,113
Employee benefit plan <sup>(2)</sup>	12 years	31,751	27,423
Encroachment revaluation	1 year	—	4,867
Other	Various	7,805	4,710
Total regulatory liabilities		<u>\$ 434,429</u>	<u>\$ 438,113</u>
Reflected as:			
Other current liabilities		\$ 7,805	\$ 3,751
Noncurrent liabilities		426,624	434,362
Total regulatory liabilities		<u>\$ 434,429</u>	<u>\$ 438,113</u>

- (1) Amounts represent income tax liabilities related to tax rate changes on deferred income tax assets and liabilities that the Company deems probable of being reflected in future regulatory rates.
- (2) Represents amounts not yet recognized as a component of net periodic benefit cost that are to be returned to customers in future periods when recognized.

#### **(6) Long-Term Debt**

Long-term debt consists of the following, including unamortized premiums, discounts, and debt issuance costs as of December 31 (dollars in thousands):

	<b>Par Value</b>	<b>2019</b>	<b>2018</b>
Long-term debt:			
4.25% Senior Notes, due 2021	\$ 200,000	\$ 199,657	\$ 199,424
5.8% Senior Bonds, due 2037	150,000	149,146	149,118
4.1% Senior Bonds, due 2042	250,000	247,747	247,688
4.3% Senior Bonds, due 2049	650,000	650,558	445,282
Total long-term debt	<u>\$ 1,250,000</u>	<u>\$ 1,247,108</u>	<u>\$ 1,041,512</u>

All of the Company's senior notes and bonds are due and payable on their respective maturity dates and none have mandatory prepayment terms.

The Company is prohibited from making distributions in respect of the shares of its capital stock unless, on the date of any such distribution, none of certain specified events of default exist under its senior unsecured debt and either (1) at the time and as a result of such distribution, the ratio of its debt to its total capital does not exceed 0.65 to 1.0 and the ratio of its earnings before interest, taxes, depreciation and amortization, to its interest expense is not less than 2.5 to 1.0, or (2) if the Company is not in compliance with such ratios, its

senior unsecured long-term debt rating is at least BBB (or its then equivalent) from Standard and Poor's and Baa2 (or its then equivalent) from Moody's Investors Service, Inc.

**(7) Income Taxes**

Income tax expense consists of the following for the years ended December 31 (in thousands):

	<u>2019</u>	<u>2018</u>
<b>Current:</b>		
Federal	\$ 31,611	\$ 41,525
State	8,486	9,919
	<u>40,097</u>	<u>51,444</u>
<b>Deferred:</b>		
Federal	35,004	9,116
State	17,621	9,992
	<u>52,625</u>	<u>19,108</u>
Total	<u>\$ 92,722</u>	<u>\$ 70,552</u>

A reconciliation of the federal statutory income tax rate to the effective income tax rate applicable to income before income tax expense is as follows for the years ended December 31:

	<u>2019</u>	<u>2018</u>
Federal statutory income tax rate	21.0%	21.0%
State income tax, net of federal income tax benefit	5.7	5.2
Effects of tax rate change	<u>(1.4)</u>	<u>(2.4)</u>
Effective income tax rate	<u>25.3%</u>	<u>23.8%</u>



The net deferred income tax liability consists of the following as of December 31 (in thousands):

	<b>2019</b>	<b>2018</b>
<b>Deferred income tax assets:</b>		
Regulatory liabilities	\$ 113,692	\$ 114,202
AROs	4,076	8,876
State carryforwards	3,997	4,138
Other	11,444	19,024
Total deferred income tax assets	133,209	146,240
Valuation allowance	(1,277)	(744)
Total deferred income tax assets, net	131,932	145,496
<b>Deferred income tax liabilities:</b>		
Property, plant and equipment, net	(674,974)	(627,207)
Regulatory assets	(30,007)	(32,656)
Employee benefits	(8,465)	(7,312)
Other	(1,893)	(2,036)
Total deferred income tax liabilities	(715,339)	(669,211)
Net deferred income tax liability	\$ (583,407)	\$ (523,715)

The Company did not have federal net operating loss or credit carryforwards as of December 31, 2019. The following table provides the Company's state net operating loss and credit carryforwards and expiration dates as of December 31, 2019 (in thousands):

Net operating loss carryforwards	\$ 71,948
Deferred income taxes on net operating loss carryforwards	\$ 3,986
Expiration dates	2020-2035
Other tax credits	\$ 11
Expiration dates	2020-2027

The valuation allowance primarily relates to Kansas net operating loss carryforwards that are not expected to be realized.

The United States Internal Revenue Service has closed its examination of the Company's income tax returns through December 31, 2011. The statute of limitations for the Company's income tax returns have expired through December 31, 2009, for Nebraska, through December 31, 2011 for Minnesota, through December 31, 2015, except for the impact of any federal audit adjustments, for Illinois, Iowa and Kansas. The closure of examinations, or the expiration of the statute of limitations, for state filings may not preclude the state from adjusting the state net operating loss carryforward utilized in a year for which the statute of limitations is not closed.

## **(8) Employee Benefit Plans**

The Company is a participant in benefit plans sponsored by MidAmerican Energy Company ("MEC"), an indirect wholly owned subsidiary of BHE. The MidAmerican Energy Company Retirement Plan provides pension benefits for eligible employees ("pension plan") and the MidAmerican Energy Company Welfare

Benefit Plan provides certain postretirement health care and life insurance benefits for eligible retirees ("other postretirement plan") on behalf of the Company. The Company's contributions to the pension plan and other postretirement plan totaled \$1.3 million and \$0.6 million for the years ended December 31, 2019 and 2018, respectively. As of December 31, 2019, the Company recorded in other long-term liabilities its portion of the under funded status of the pension plan and in other assets its portion of the over funded status of the other postretirement plan of \$15.0 million and \$31.7 million, respectively. As of December 31, 2018, the Company recorded in other long-term liabilities its portion of the under funded status of the pension plan and in other assets its portion of the over funded status of the other postretirement plan of \$14.5 million and \$27.4 million, respectively. Amounts attributable to the Company were allocated from MEC to the Company in accordance with the intercompany administrative service agreement. Offsetting regulatory assets and liabilities have been recorded related to the amounts not yet recognized as a component of net periodic benefit costs that will be included in regulated rates.

### (9) Asset Retirement Obligations

The Company estimates its ARO liabilities based upon detailed engineering calculations of the amount and timing of the future cash spending for a third party to perform the required work. Spending estimates are escalated for inflation and then discounted at a credit-adjusted, risk-free rate. Changes in estimates could occur for a number of reasons, including plan revisions, inflation and changes in the amount and timing of the expected work.

The Company has concluded that it is legally obligated to remove, or abandon-in-place, its onshore pipeline and related equipment upon the final retirement of the pipeline. While interim removal or abandonment-in-place and replacement of such equipment is probable, the final retirement dates of these assets are not determinable, and therefore, the liabilities for their removal cannot be reasonably estimated. The Company has also identified AROs related to asbestos siding on some of its buildings. Because both the methods of settlement and the timing of the retirements are unknown, the amounts of these obligations cannot be reasonably estimated to determine the fair value of these obligations.

The Company's ARO liability relates to the abandonment of pipeline assets located in offshore waters. The following table reconciles the beginning and ending balances of the Company's ARO liabilities for the years ended December 31(in thousands):

	2019	2018
<b>Beginning balance</b>	\$ 33,290	\$ 32,367
Change in estimated costs	(9,045)	—
Retirements	(9,909)	—
Accretion	954	923
<b>Ending balance</b>	<u>\$ 15,290</u>	<u>\$ 33,290</u>

Based on an analysis of costs required to abandon offshore assets, the Asset Retirement Obligation was reduced by \$9.0 million. During 2019, the Company abandoned a portion of its High Island Pipeline System and all of its West Cameron pipeline assets.

## **(10) Fair Value Measurements**

The carrying value of the Company's cash, certain cash equivalents, receivables, payables and accrued liabilities approximates fair value because of the short-term maturity of these instruments. The Company has various financial assets and liabilities that are measured at fair value on the Financial Statements using inputs from the three levels of the fair value hierarchy. A financial asset or liability classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement. The three levels are as follows:

- Level 1 - Inputs are unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.
- Level 2 - Inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability and inputs that are derived principally from or corroborated by observable market data by correlation or other means (market corroborated inputs).
- Level 3 - Unobservable inputs reflect the Company's judgments about the assumptions market participants would use in pricing the asset or liability since limited market data exists. The Company develops these inputs based on the best information available, including its own data.



The following table presents the Company's assets and liabilities recognized on the Balance Sheets and measured at fair value on a recurring basis (in thousands):

	Input Levels for Fair Value Measurements				
	Level 1	Level 2	Level 3	Other <sup>(1)</sup>	Total
<b><u>As of December 31, 2019</u></b>					
<b>Assets:</b>					
Commodity derivatives	\$ —	\$ 9,192	\$ —	\$ (4,582)	\$ 4,610
Money market mutual funds <sup>(2)</sup>	73,436	—	—	—	73,436
Investment funds	11,596	—	—	—	11,596
	<u>\$ 85,032</u>	<u>\$ 9,192</u>	<u>\$ —</u>	<u>\$ (4,582)</u>	<u>\$ 89,642</u>
<b>Liabilities - commodity derivatives</b>	<u>\$ —</u>	<u>\$ (6,087)</u>	<u>\$ —</u>	<u>\$ 4,582</u>	<u>\$ (1,505)</u>
<b><u>As of December 31, 2018</u></b>					
<b>Assets:</b>					
Commodity derivatives	\$ —	\$ 3,383	\$ —	\$ (1,585)	\$ 1,798
Money market mutual funds <sup>(2)</sup>	42,526	—	—	—	42,526
Investment funds	6,102	—	—	—	6,102
	<u>\$ 48,628</u>	<u>\$ 3,383</u>	<u>\$ —</u>	<u>\$ (1,585)</u>	<u>\$ 50,426</u>
<b>Liabilities - commodity derivatives</b>	<u>\$ —</u>	<u>\$ (2,425)</u>	<u>\$ —</u>	<u>\$ 1,585</u>	<u>\$ (840)</u>

(1) Represents netting under master netting arrangements.

(2) Amounts are included in cash and cash equivalents, other current assets and other assets on the Balance Sheets. The fair value of these money market mutual funds approximates cost.

Derivative contracts are recorded on the Balance Sheets as either assets or liabilities and are stated at estimated fair value unless they are designated as normal purchases or normal sales and qualify for the exception afforded by GAAP. When available, the fair value of derivative contracts is estimated using unadjusted quoted prices for identical contracts in the market in which the Company transacts. When quoted prices for identical contracts are not available, the Company uses forward price curves. Forward price curves represent the Company's estimates of the prices at which a buyer or seller could contract today for delivery or settlement at future dates. The Company bases its forward price curves upon market price quotations, when available, or internally developed and commercial models, with internal and external fundamental data inputs. Market price quotations are obtained from independent energy brokers, exchanges, direct communication with market participants and actual transactions executed by the Company. Market price quotations for certain major natural gas trading hubs are generally readily obtainable for the applicable term of the Company's outstanding derivative contracts; therefore, the Company's forward price curves for those locations and periods reflect observable market quotes. The estimated fair value of these derivative contracts is a function of underlying forward commodity prices, related volatility, counterparty creditworthiness and duration of contracts.

The Company's investments in money market mutual funds are accounted for as available-for-sale securities and are stated at fair value. Investment funds are accounted for as trading securities and are stated at fair value. Trading securities are carried at fair value with realized and unrealized gains and losses recognized in earnings. A readily observable quoted market price or net asset value of an identical security in an active market is used to record the fair value.

The Company's long-term debt is carried at cost on the Financial Statements. The fair value of the Company's long-term debt is a Level 2 fair value measurement and has been estimated based upon quoted market prices, where available, or at the present value of future cash flows discounted at rates consistent with comparable maturities with similar credit risks. The following table presents the carrying value and estimated fair value of the Company's long-term debt as of December 31 (in thousands):

	2019		2018	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Long-term debt	\$ 1,247,108	\$ 1,401,627	\$ 1,041,512	\$ 1,048,161

#### (11) Credit Risk

The Company has a concentration of customers in the electric and gas utility industries, principally in the upper Midwestern states. This concentration of customers may impact the Company's overall exposure to credit risk in that the customer base may be similarly affected by changes in economic, industry, weather or other conditions. The Company's ten largest customers accounted for 61% of its system-wide transportation and storage revenue in 2019.

The following customers accounted for 10% or more of the Company's total revenues for the years ended December 31 and trade receivables as of December 31:

	Revenue		Accounts Receivable	
	2019	2018	2019	2018
Xcel Energy, Inc. <sup>(1)</sup>	12%	12%	10%	8%
CenterPoint Energy Resources Corporation <sup>(2)</sup>	11	10	17	12

(1) The Company's agreements are with Northern States Power-Minnesota, Northern States Power-Wisconsin, Northern States Power-Generation and Southwestern Public Service Company, subsidiaries of Xcel Energy, Inc.

(2) The Company's agreements are with CenterPoint Energy Minnesota Gas, CenterPoint Energy Services and CenterPoint Energy Gas Transmission, subsidiaries of CenterPoint Energy Resources Corporation.

For shippers that have withdrawn gas prior to injection under the Company's deferred delivery services, the Company is exposed to credit risk with respect to those counterparties based upon the value of the gas withdrawn. The balances in transportation and exchange gas receivables were \$5.4 million and \$16.2 million as of December 31, 2019 and 2018, respectively. Included in these amounts were balances owed of



\$1.1 million and \$11.2 million as of December 31, 2019 and 2018, respectively, which were related to the Company's deferred delivery services.

As a general policy, collateral is not required for receivables from creditworthy customers. Customers' financial condition and creditworthiness are regularly evaluated, and historical losses have been minimal. In order to provide protection against credit risk, and as permitted by the terms of the Company's tariff, the Company has, among other alternatives, required customers that lack creditworthiness as defined by the tariff to provide letters of credit, cash security deposits or to establish separate legally restricted escrow funds to be held until these customers' creditworthiness can be demonstrated. As of December 31, 2019 and 2018, the Company has reflected on the Balance Sheets escrow funds of \$2.2 million and \$0.3 million, respectively, in other current assets and \$13.5 million and \$12.5 million, respectively, in other assets with offsetting amounts in other current liabilities and long-term liabilities, respectively.

## **(12) Commitments and Contingencies**

### *Regulatory Matters*

In July 2018, FERC issued a final rule adopting procedures for determining whether natural gas pipelines were collecting unjust and unreasonable rates in light of the reduction in the federal corporate tax rate from 2017 Tax Cuts and Jobs Act. Pursuant to the final rule, in October 2018, the Company filed an informational filing on FERC Form No. 501-G and a Statement Demonstrating Why No Rate Adjustment is Necessary. In January 2019, FERC initiated a Section 5 investigation to determine whether the rates currently charged by the Company are just and reasonable. As required by the FERC Section 5 order, the Company filed a cost and revenue study in April 2019. In July 2019, the Company filed a Section 4 rate case requesting increases in its transportation and storage rates. The rate filing provided evidence in support of a \$300 million increase to the Company's annual revenue requirement. The rate increase is primarily attributed to the capital investment made by the Company since the last rate case, an increase in the Company's depreciation rates, the addition of negative salvage and increased return on equity. In September 2019, FERC consolidated the Section 5 investigation and the Section 4 rate case into one procedural process set for hearing commencing June 2020. In January 2020, the FERC approved the Company's filing to implement its interim rates, including an increase of 77% from its current Market Area transmission reservation rate, subject to refund, effective January 1, 2020.

### *Legal Matters*

The Company is party to a variety of legal actions arising out of the normal course of business. Plaintiffs occasionally seek punitive or exemplary damages. The Company does not believe that such normal and routine litigation will have a material impact on its financial results. The Company is also involved in other kinds of legal actions, some of which assert or may assert claims or seek to impose fines, penalties and other costs in substantial amounts and are described below.

The Company's storage gas migrated from its former certificated storage field boundaries near Cunningham, Kansas and was produced on leaseholds held by Nash Oil & Gas, Inc. ("Nash"), L.D. Drilling Company ("LD Drilling"), Val Energy, Inc. ("Val Energy") and Iuka-Carmi Development, LLC. In order to mitigate its losses, the Company initiated the following actions:

- In September 2009, the Company filed an application with the FERC to extend the boundaries of the Cunningham natural gas storage facility. In June 2010, FERC issued an order granting the Company certificate authority to extend the boundaries of the Cunningham natural gas storage facility by 12,320 acres. The Company either acquired the storage rights or purchased the property on 3,696 acres, or 30% of the extension area. In July 2010, the Company filed a complaint in federal district court to acquire the remaining necessary interests by eminent domain. The federal district court issued a decision in February 2015, awarding a total value of \$7.3 million. In July 2017, the Tenth Circuit Court of Appeals reduced the condemnation award by approximately \$6.0 million. The case was remanded to the federal district court for final disposition. In March 2019 the federal district court entered a Memorandum and Order adopting the Company's position on the remaining issues. Motions to reconsider the decision have been filed by the defendants and were denied by the court. In July 2019, the defendants filed a notice of appeal to the Tenth Circuit Court of Appeals. The appeals were dismissed as premature as a final order has not been issued by the district court.
- The Company filed a lawsuit in December 2008 against Nash, LD Drilling and Val Energy in the United States District Court for the District of Kansas for nuisance, conversion and unjust enrichment related to the storage gas losses from the June 2010 FERC order through February 2011 after which the third-party wells in the extension area were shut-in. The conversion claims related to production of storage gas before the date of the certificate expansion order have been dismissed. In May 2016, the court issued an order lifting the stay that had been in place since August 2011. The trial commenced in October 2019, on the nuisance and unjust enrichment claims. In November 2019, the jury returned a verdict in favor of the defendants.
- In December 2009, the Company filed a lawsuit in the 13th Judicial District, District Court, Pratt County, Kansas ("Pratt County State District Court") against ONEOK Field Services Company ("ONEOK") and Lumen Energy Corporation ("Lumen") alleging conversion based on their purchase of the storage gas from the producers after the June 2010 FERC order. In August 2014, the Pratt County State District Court granted the producers' motion for summary judgment, finding the Company did not have a viable conversion claim related to the gas produced after June 2010. The Company appealed the decision to the Kansas Court of Appeals and the case was transferred to the Kansas Supreme Court in October 2017. In September 2019, the Kansas Supreme Court reversed the decision of the trial court finding the Company held title to storage gas produced after the June 2010 Order. The case has been remanded for further proceedings. The proceeds from June 2010 through February 2011 when the wells were shut-in will continue to be held in suspense pending their further proceedings. The Company has valued these amounts at approximately \$3.4 million.

In December 2011, state court petitions were filed against the Company in three counties in Kansas, alleging trespass, nuisance and unjust enrichment, arising out of the migration of the Company's storage gas. The cases were moved to federal district court in Wichita, Kansas in December 2011, at the request of the Company. The case will likely be resolved in light of the completion of the condemnation and nuisance matters described above.

While it is not possible to predict with certainty the outcome of the aforementioned litigation and other contingencies, the Company believes that the ultimate resolution of these matters will not have a material adverse effect on the Company's financial results.



### *Purchase Obligations*

The Company expects to incur significant future capital expenditures to meet increased customer growth and system reliability objectives. As of December 31, 2019, the Company had firm construction commitments of \$18.2 million, primarily related to branch line and compressor replacements. Capital expenditure needs are reviewed regularly by management and may change significantly as a result of such reviews. Estimates may change significantly at any time as a result of, among other factors, changes in rules and regulations, including environmental; changes in income tax laws; general business conditions; load projections; system reliability standards; the cost and efficiency of construction labor, equipment, and materials; and the cost and availability of capital. Additionally, the Company has commitments to two of its largest customers to meet minimum levels of incremental capacity requests through 2027 and 2034.

### *Easements and Leases*

The Company has non-cancelable easements with minimum payment commitments as of December 31, 2019 of \$1.1 million, \$1.0 million, \$1.1 million, \$1.1 million and \$1.1 million for the years 2020 through 2024, respectively, and \$5.6 million for the total of the years thereafter. The Company also has non-cancelable operating leases with minimum payment commitments as of December 31, 2019 of \$0.5 million, \$0.4 million, \$0.4 million, \$0.3 million and \$0.1 million for the years 2020 through 2024, respectively, and insignificant amounts for the years thereafter.

## **(13) Revenue from Contracts with Customers**

The following table summarizes the Company's revenue from contracts with customers ("Customer Revenue") (in thousands):

	<b>Years Ended December 31,</b>	
	<b>2019</b>	<b>2018</b>
Customer Revenue:		
Transportation service	\$ 745,215	\$ 691,550
Storage service	65,008	67,545
Gas, liquids and other sales	39,211	137,537
Total Customer Revenue	849,434	896,632
Other Revenue <sup>(1)</sup>	2,814	(7,011)
Total	<u>\$ 852,248</u>	<u>\$ 889,621</u>

- (1) Revenue not considered Customer Revenue ("Other Revenue") consists of revenue recognized in accordance with Accounting Standards Codification 815, "Derivative and Hedging" and includes net payments to counterparties for the financial settlement of certain derivative contracts.

### *Contract Assets and Liabilities*

In the event one of the parties to a contract has performed before the other, the Company would recognize a contract asset or contract liability depending on the relationship between the Company's performance and the customer's payment. As of December 31, 2019 and December 31, 2018, there were no contract assets or contract liabilities recorded on the Balance Sheets.

### *Remaining Performance Obligations*

The following table summarizes the Company's revenue it expects to recognize in future periods related to significant unsatisfied performance obligations for fixed contracts with expected durations in excess of one year as of December 31, 2019 (in thousands):

Less than 12 months	\$ 667,324
More than 12 months	3,896,749
Total	<u>\$ 4,564,073</u>

### **(14) Other Related Party Transactions**

The Company provided gas transportation, storage and other services to MEC totaling \$61.2 million and \$65.2 million for the years ended December 31, 2019 and 2018, respectively. MEC provides certain administrative and management services, including executive, financial, legal, human resources, payroll and tax, to the Company. Expenses incurred by MEC and billed to the Company are based on the individual services and expense items provided and were \$8.8 million and \$7.4 million for the years ended December 31, 2019 and 2018, respectively. MEC also provided electricity and other services to the Company of \$0.7 million and \$0.6 million for the years ended December 31, 2019 and 2018, respectively. The Company reimbursed MEC \$81.3 million and \$71.7 million for the years ended December 31, 2019 and 2018, respectively, for payroll, healthcare benefits and other benefit payments that MEC processed on behalf of the Company.

BHE provides certain administrative and management services, including executive, financial, legal and tax, to the Company. Expenses incurred by BHE and billed to the Company are based on the individual services and expense items provided and were \$3.8 million and \$3.6 million for the years ended December 31, 2019 and 2018, respectively. Income tax transactions with BHE resulted in net payments of \$51.9 million and \$38.5 million for the years ended December 31, 2019 and 2018, respectively.

As of December 31, 2019 and 2018, the Company had net accounts payable to BHE and certain subsidiaries for intercompany transactions totaling \$1.2 million, for the years ended December 31, 2019 and 2018, respectively. The Company also had accounts receivable from affiliates of \$8.3 million and \$9.2 million as of December 31, 2019 and 2018, respectively.

The Company provides certain administrative and management services, including executive, financial, regulatory, legal, information technology, human resources and procurement, to Kern River Gas Transmission Company ("Kern River"), an indirect wholly owned subsidiary of BHE. The Company billed Kern River \$1.9 million and \$2.1 million for the years ended December 31, 2019 and 2018, respectively, for these services.



The Company possesses demand promissory notes from BHE. The balance of the demand promissory notes as of December 31, 2019 and 2018 was \$240.0 million and \$305.0 million, respectively. The notes contain variable interest rates based on 30-day LIBOR plus a fixed spread per annum. Interest income of \$11.9 million and \$7.4 million was recorded for the years ended December 31, 2019 and 2018, respectively.

**(15) Subsequent Events**

In February and March 2020, BHE issued promissory notes to the Company totaling \$180.0 million.