Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholder of Tennessee Gas Pipeline Company:

We have audited the accompanying consolidated balance sheets of Tennessee Gas Pipeline Company (the Company) as of December 31, 2007 and 2006, and the related consolidated statements of income, stockholder's equity, and cash flows for each of the two years in the period ended December 31, 2007. Our audits also included the financial statement schedule listed in the Index at Item 15(a) for each of the two years in the period ended December 31, 2007. These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing 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 over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Tennessee Gas Pipeline Company at December 31, 2007 and 2006, and the consolidated results of its operations and its cash flows for each of the two years in the period ended December 31, 2007, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

As discussed in Note 1 to the consolidated financial statements, effective January 1, 2007, the Company adopted the provisions of Financial Accounting Standards Board Interpretation No. 48, *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109;* effective December 31, 2006, the Company adopted the recognition provisions of Statement of Financial Accounting Standards No. 158, *Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans — An Amendment of FASB Statements No. 87, 88, 106, and 132 (R);* and effective January 1, 2006, the Company adopted the Federal Energy Regulatory Commission's accounting release related to pipeline assessment costs.

/s/ Ernst & Young LLP

Houston, Texas
February 25, 2008

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholder of Tennessee Gas Pipeline Company:

In our opinion, the consolidated statements of income, stockholder's equity and cash flows for the year ended December 31, 2005 listed in the Index appearing under Item 15(a) (1), present fairly, in all material respects, the results of operations and cash flows of Tennessee Gas Pipeline Company and its subsidiaries (the "Company") for the year ended December 31, 2005, in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule for the year ended December 31, 2005 listed in the Index appearing under Item 15(a) (2) presents fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and the financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and the financial statement schedule based on our audit. We conducted our audit of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). 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.

/s/ PricewaterhouseCoopers LLP

Houston, Texas
February 28, 2006

TENNESSEE GAS PIPELINE COMPANY
CONSOLIDATED STATEMENTS OF INCOME
(In millions)

	Year Ended December 31,		
	2007	2006	2005
Operating revenues	$ 862	$ 793	$ 757
Operating expenses			
Operation and maintenance	338	315	328
Depreciation and amortization	170	164	161
Taxes, other than income taxes	56	55	51
	564	534	540
Operating income	298	259	217
Earnings from unconsolidated affiliate	13	15	14
Other income, net	19	14	5
Interest and debt expense	(130)	(129)	(131)
Affiliated interest income, net	44	43	25
Income before income taxes	244	202	130
Income taxes	91	75	48
Income before cumulative effect of accounting change	153	127	82
Cumulative effect of accounting change, net of income taxes	—	—	(3)
Net income	$ 153	$ 127	$ 79

See accompanying notes.

TENNESSEE GAS PIPELINE COMPANY
CONSOLIDATED BALANCE SHEETS
(In millions, except share amounts)

	December 31, 2007	December 31, 2006
ASSETS		
Current assets		
Cash and cash equivalents	$ —	$ —
Accounts receivable		
Customer	14	21
Affiliates	71	70
Other	27	43
Materials and supplies	34	28
Deferred income taxes	10	117
Assets held for sale	—	28
Other	9	7
Total current assets	165	314
Property, plant and equipment, at cost	4,048	3,707
Less accumulated depreciation and amortization	740	606
	3,308	3,101
Additional acquisition cost assigned to utility plant, net	2,040	2,079
Total property, plant and equipment, net	5,348	5,180
Other assets		
Notes receivable from affiliates	1,034	1,073
Investment in unconsolidated affiliate	84	98
Other	52	37
	1,170	1,208
Total assets	$ 6,683	$ 6,702
LIABILITIES AND STOCKHOLDER'S EQUITY		
Current liabilities		
Accounts payable		
Trade	$ 66	$ 90
Affiliates	23	26
Other	56	44
Current maturities of long-term debt	—	300
Taxes payable	31	78
Asset retirement obligations	4	33
Accrued interest	24	24
Contractual deposits	32	28
Other	13	12
Total current liabilities	249	635
Long-term debt, less current maturities	1,603	1,302
Other liabilities		
Deferred income taxes	1,302	1,407
Regulatory liabilities	178	160
Other	57	41
	1,537	1,608
Commitments and contingencies (Note 8)		
Stockholder's equity		
Common stock, par value $5 per share; 300 shares authorized; 208 shares issued and outstanding	—	—
Additional paid-in capital	2,209	2,207
Retained earnings	1,085	947
Accumulated other comprehensive income	—	3
Total stockholder's equity	3,294	3,157
Total liabilities and stockholder's equity	$ 6,683	$ 6,702

See accompanying notes.

TENNESSEE GAS PIPELINE COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions)

	Year Ended December 31, 2007	2006	2005
Cash flows from operating activities			
Net income	$ 153	$ 127	$ 79
Adjustments to reconcile net income to net cash from operating activities			
Depreciation and amortization	170	164	161
Deferred income taxes	88	26	60
Earnings from unconsolidated affiliate, adjusted for cash distributions	14	2	50
Other non-cash income items	(10)	(6)	2
Asset and liability changes			
Accounts receivable	15	32	(42)
Accounts payable	(15)	27	15
Taxes payable	(40)	37	(30)
Other current assets	(6)	(3)	36
Other current liabilities	(4)	(21)	(11)
Non-current assets	(13)	(8)	31
Non-current liabilities	(66)	12	18
Net cash provided by operating activities	286	389	369
Cash flows from investing activities			
Additions to property, plant and equipment	(364)	(421)	(203)
Proceeds from the sale of asset	35	—	—
Net change in notes receivable from affiliates	39	25	(168)
Other	4	7	2
Net cash used in investing activities	(286)	(389)	(369)
Net change in cash and cash equivalents	—	—	—
Cash and cash equivalents			
Beginning of period	—	—	—
End of period	$ —	$ —	$ —

See accompanying notes.

TENNESSEE GAS PIPELINE COMPANY
CONSOLIDATED STATEMENTS OF STOCKHOLDER'S EQUITY
(In millions, except share amounts)

	Common stock		Additional paid-in capital	Retained earnings	Accumulated other comprehensive income	Total stockholder's equity
	Shares	Amount				
January 1, 2005	208	$ —	$ 2,206	$ 741	$ —	$ 2,947
Net income				79		79
Allocated tax benefit of El Paso equity plans			1			1
December 31, 2005	208	—	2,207	820	—	3,027
Net income				127		127
Adoption of SFAS No. 158, net of income taxes of $2					3	3
December 31, 2006	208	—	2,207	947	3	3,157
Net income				153		153
Adoption of FIN No. 48, net of income taxes of $(8)				(15)		(15)
Reclassification to regulatory liability (See Note 9)					(3)	(3)
Other			2			2
December 31, 2007	208	$ —	$ 2,209	$ 1,085	$ —	$ 3,294

See accompanying notes.

TENNESSEE GAS PIPELINE COMPANY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation

We are a Delaware corporation incorporated in 1947, and an indirect wholly owned subsidiary of El Paso Corporation (El Paso). Our consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles (GAAP) and include the accounts of all majority owned and controlled subsidiaries after the elimination of intercompany accounts and transactions.

We consolidate entities when we either (i) have the ability to control the operating and financial decisions and policies of that entity or (ii) are allocated a majority of the entity's losses and/or returns through our variable interests in that entity. The determination of our ability to control or exert significant influence over an entity and whether we are allocated a majority of the entity's losses and/or returns involves the use of judgment. We apply the equity method of accounting where we can exert significant influence over, but do not control, the policies and decisions of an entity and where we are not allocated a majority of the entity's losses and/or returns. We use the cost method of accounting where we are unable to exert significant influence over the entity.

Use of Estimates

The preparation of our financial statements requires the use of estimates and assumptions that affect the amounts we report as assets, liabilities, revenues and expenses and our disclosures in these financial statements. Actual results can, and often do, differ from those estimates.

Regulated Operations

Our natural gas pipeline and storage operations are subject to the jurisdiction of the Federal Energy Regulatory Commission (FERC) under the Natural Gas Act of 1938, the Natural Gas Policy Act of 1978 and the Energy Policy Act of 2005. We follow the regulatory accounting principles prescribed under Statement of Financial Accounting Standards (SFAS) No. 71, *Accounting for the Effects of Certain Types of Regulation.* Under SFAS No. 71, we record regulatory assets and liabilities that would not be recorded under GAAP for non-regulated entities. Regulatory assets and liabilities represent probable future revenues or expenses associated with certain charges or credits that will be recovered from or refunded to customers through the rate making process. Items to which we apply regulatory accounting requirements include certain postretirement employee benefit plan costs, an equity return component on regulated capital projects and certain costs included in, or expected to be included in, future rates.

Cash and Cash Equivalents

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

Allowance for Doubtful Accounts

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 collectibility and establish or adjust our allowance as necessary using the specific identification method.

Materials and Supplies

We value materials and supplies at the lower of cost or market value with cost determined using the average cost method.

Natural Gas Imbalances

Natural gas imbalances occur when the actual amount of natural gas delivered from or received by a pipeline system or storage facility differs from the contractual amount delivered or received. We value these imbalances due to or from shippers and operators utilizing current index prices. Imbalances are settled in cash or in-kind, subject to the terms of our tariff.

Imbalances due from others are reported in our balance sheet as either accounts receivable from customers or accounts receivable from affiliates. Imbalances owed to others are reported on the balance sheet as either trade accounts payable or accounts payable to affiliates. We classify all imbalances as current as we expect to settle them within a year.

Property, Plant and Equipment

Our property, plant and equipment is recorded at its original cost of construction or, upon acquisition, at the fair value of the assets acquired. For assets we construct, we capitalize direct costs, such as labor and materials, and indirect costs, such as overhead, interest and an equity return component, as allowed by the FERC. We capitalize major units of property replacements or improvements and expense minor items. Prior to January 1, 2006, we capitalized certain costs incurred related to our pipeline integrity programs as part of our property, plant and equipment. Beginning January 1, 2006, we began expensing these costs based on a FERC accounting release. During the year ended December 31, 2007 and 2006, we expensed approximately $8 million and $7 million as a result of the adoption of this accounting release.

We use the composite (group) method to depreciate regulated property, plant and equipment. Under this method, assets with similar lives and characteristics are grouped and depreciated as one asset. We apply the FERC-accepted depreciation rate to the total cost of the group until its net book value equals its salvage value. Currently, our depreciation rates vary from one percent to 25 percent per year. Using these rates, the remaining depreciable lives of these assets range from one to 30 years. We re-evaluate depreciation rates each time we file with the FERC for a change in our transportation and storage rates.

When we retire regulated property, plant and equipment, we charge accumulated depreciation and amortization for the original cost of the assets in addition to the cost to remove, sell or dispose of the assets, less their salvage value. We do not recognize a gain or loss unless we sell an entire operating unit. We include gains or losses on dispositions of operating units in operating income. For properties not subject to regulation by the FERC, we reduce property, plant and equipment for its original cost, less accumulated depreciation and salvage value with any remaining gain or loss recorded in income.

Included in our property balances are additional acquisition costs assigned to utility plant, which represents the excess of allocated purchase costs over the historical costs of the facilities. These costs are amortized on a straight-line basis over 62 years using the same rates as the related assets, and we do not recover those excess costs in our rates.

At December 31, 2007 and 2006, we had $197 million and $237 million of construction work in progress included in our property, plant and equipment.

We capitalize a carrying cost (an allowance for funds used during construction) on debt and equity funds related to our 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 our average cost of debt. Interest costs on debt amounts capitalized during the years ended December 31, 2007, 2006 and 2005, were $6 million, $5 million and $2 million. These debt amounts are included as a reduction to interest and debt expense on our income statement. The equity portion of capitalized costs is calculated using the most recent FERC-approved equity rate of return. The equity amounts capitalized (exclusive of any tax related impacts) during the years ended December 31, 2007, 2006 and 2005, were $12 million, $8 million and $3 million. These equity amounts are included as other non-operating income on our income statement.

Asset and Investment Impairments

We evaluate 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. When an event occurs, we evaluate the recoverability of our long-lived assets' 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 their estimated fair value. Our fair value estimates are generally based on market data obtained through the sales process or an analysis of expected discounted cash flows. The magnitude of any impairment is impacted by a number of factors, including the nature of the assets being sold and our established time frame for completing the sale, among other factors.

We reclassify the asset or assets to be sold as either held-for-sale or as discontinued operations, depending on, among other criteria, whether we will have significant long-term continuing involvement with those assets after they are sold. We cease depreciating assets in the period that they are reclassified as either held for sale or as discontinued operations.

Revenue Recognition

Our revenues are primarily generated from natural gas transportation and storage services. 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 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. Gas not used in operations is based on the volumes of natural gas we are allowed to retain relative to the amounts we use for operating purposes. We recognize revenue on gas not used in operations when the volumes are retained. 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.

Environmental Costs and Other Contingencies

Environmental Costs. We record liabilities at their undiscounted amounts on our balance sheet as other current and long-term liabilities when environmental assessments indicate that remediation efforts are probable and the costs can be reasonably estimated. Estimates of our liabilities are based on currently available facts, existing technology and presently enacted laws and regulations taking into consideration the likely effects of other societal and economic factors, and include estimates of associated legal costs. These amounts also consider prior experience in remediating contaminated sites, other companies' clean-up experience and data released by the Environmental Protection Agency or other organizations. Our estimates are subject to revision in future periods based on actual costs or new circumstances. We capitalize costs that benefit future periods and we recognize a current period charge in operation and maintenance expense when clean-up efforts do not benefit future periods.

We evaluate any amounts paid directly or reimbursed by government sponsored programs and potential recoveries or reimbursements of remediation costs from third parties, including insurance coverage, separately from our liability. Recovery is evaluated based on the creditworthiness or solvency of the third party, among other factors. When recovery is assured, we record and report an asset separately from the associated liability on our balance sheet.

Other Contingencies. We recognize liabilities for other contingencies when we have an exposure that, when fully analyzed, 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.

Income Taxes

El Paso maintains 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 provides, among other things, that (i) each company in a taxable income position will accrue a current expense equivalent to its federal and state income taxes, and (ii) each company in a tax loss position will accrue a benefit to the extent its deductions, including general business credits, can be utilized in the consolidated returns. El Paso pays all consolidated U.S. federal and state income taxes directly to the appropriate taxing jurisdictions and, under a separate tax billing agreement, El Paso may bill or refund its subsidiaries for their portion of these income tax payments.

Pursuant to El Paso's policy, we record current income taxes based on our taxable income and we provide for deferred income taxes to reflect estimated future tax payments and receipts. Deferred taxes represent the tax impacts of differences between the financial statement and tax bases of assets and liabilities and carryovers at each year end. We account for tax credits under the flow-through method, which reduces the provision for income taxes in the year the tax credits first become available. We reduce deferred tax assets by a valuation allowance when, based on our estimates, it is more likely than not that a portion of those assets will not be realized in a future period. The estimates utilized in the recognition of deferred tax assets are subject to revision, either up or down, in future periods based on new facts or circumstances.

Effective January 1, 2007, we adopted the provisions of Financial Accounting Standards Board (FASB) Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109.* FIN No. 48 clarifies SFAS No. 109, *Accounting for Income Taxes*, and requires us to evaluate our tax positions for all jurisdictions and for all years where the statute of limitations has not expired. FIN No. 48 requires companies to meet a more-likely-than-not threshold (i.e. a greater than 50 percent likelihood of a tax position being sustained under examination) prior to recording a benefit for their tax positions. Additionally, for tax positions meeting this more-likely-than-not threshold, the amount of benefit is limited to the largest benefit that has a greater than 50 percent probability of being realized upon effective settlement. For a further discussion of the impact of the adoption of FIN No. 48, see Note 3.

Accounting for Asset Retirement Obligations

We account for our asset retirement obligations in accordance with SFAS No. 143, *Accounting for Asset Retirement Obligations* and FIN No. 47, *Accounting for Conditional Asset Retirement Obligations.* We record a liability for legal obligations associated with the replacement, removal or retirement of our long-lived assets. Our asset retirement liabilities are recorded at their estimated fair value with a corresponding increase to property, plant and equipment. This increase in property, plant and equipment is then depreciated over the useful life of the long-lived asset to which that liability relates. An ongoing expense is also recognized for changes in the value of the liability as a result of the passage of time, which we record as depreciation and amortization expense in our income statement. We have the ability to recover certain of these costs from our customers and have recorded an asset (rather than expense) associated with the depreciation of the property, plant and equipment and accretion of the liabilities described above.

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. We record net benefit cost related to this plan in our income statement. This net benefit cost is a function of many factors including benefits earned during the year by plan participants (which is a function of 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 plan, see Note 9.

We use the recognition provisions of SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans — an Amendment of FASB Statements No. 87, 88, 106, and 132(R)* to account for our plan. Under SFAS No. 158, we record an asset or liability for our postretirement benefit plan based on its overfunded or underfunded status. Any deferred amounts related to unrealized gains and losses or changes in actuarial assumptions are recorded either as a regulatory asset or liability. For a further discussion of our application of SFAS No. 158, see Note 9.

New Accounting Pronouncements Issued But Not Yet Adopted

As of December 31, 2007, the following accounting standards had not yet been adopted by us.

Fair Value Measurements. In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*, which provides guidance on measuring the fair value of assets and liabilities in the financial statements. We will adopt the provisions of this standard for our financial assets and liabilities effective January 1, 2008. Adopting the standard is not expected to have a material impact on our financial statements. The FASB provided a one year deferral of the adoption of SFAS No. 157 for certain non-financial assets and liabilities. We have elected to defer the adoption of the standard for certain of our non-financial assets and liabilities, and are currently evaluating the impact, if any, that the deferred provisions of the standard will have on our financial statements.

Measurement Date of Postretirement Benefits. In December 2006, we adopted the recognition provisions of SFAS No. 158. Beginning in 2008, this standard will also require us to change the measurement date of our postretirement benefit plan from September 30, the date we currently use, to December 31. Adoption of the measurement date provisions of this standard is not expected to have a material impact on our financial statements.

Fair Value Option. In February 2007, the FASB issued SFAS No. 159, *Fair Value Option for Financial Assets and Financial Liabilities* — including an Amendment to FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, which permits entities to choose to measure many financial instruments and certain other items at fair value. We will adopt the provisions of this standard effective January 1, 2008, and do not anticipate that it will have a material impact on our financial statements.

Business Combinations. In December 2007, the FASB issued SFAS No. 141(R), *Business Combinations,* which provides revised guidance on the accounting for acquisitions of businesses. This standard changes the current guidance to require that all acquired assets, liabilities, minority interest and certain contingencies be measured at fair value, and certain other acquisition-related costs be expensed rather than capitalized. SFAS No. 141(R) will apply to acquisitions that are effective after December 31, 2008, and application of the standard to acquisitions prior to that date is not permitted.

Noncontrolling Interests. In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements*, which provides guidance on the presentation of minority interests in the financial statements. This standard requires that minority interest be presented as a component of equity rather than as a "mezzanine" item between liabilities and equity, and also requires that minority interest be presented as a separate caption in the income statement. This standard also requires all transactions with minority interest holders, including the issuance and repurchase of minority interests, be accounted for as equity transactions unless a change in control of the subsidiary occurs. SFAS No. 160 is effective for fiscal years beginning after December 15, 2008, and we are evaluating the impact that this standard will have on our financial statements.

2. Gain (Loss) on Long-Lived Assets

During 2007, we completed the sale of a pipeline lateral for approximately $35 million and recorded a pretax gain on the sale of approximately $7 million. During 2007, we also recorded a loss of $8 million related to a pipeline asset which was purchased to repair hurricane damage and not subsequently utilized. We record gains and losses on long-lived assets in operation and maintenance expense in our income statement.

3. Income Taxes

Components of Income Taxes. The following table reflects the components of income taxes included in income before cumulative effect of accounting change for each of the three years ended December 31:

	2007	2006	2005
		(In millions)	
Current			
Federal	$ (1)	$ 50	$ (13)
State	4	(1)	1
	3	49	(12)
Deferred			
Federal	85	18	58
State	3	8	2
	88	26	60
Total income taxes	$ 91	$ 75	$ 48

Effective Tax Rate Reconciliation. Our income taxes differ from the amount computed by applying the statutory federal income tax rate of 35 percent for the following reasons for each of the three years ended December 31:

	2007	2006	2005
		(In millions, except for rates)	
Income taxes at the statutory federal rate of 35%	$ 85	$ 71	$ 46
State income taxes, net of federal income tax effect	5	4	2
Other	1	—	—
Income taxes	$ 91	$ 75	$ 48
Effective tax rate	37%	37%	37%

Deferred Tax Assets and Liabilities. The following are the components of our net deferred tax liability at December 31:

	2007	2006
	(In millions)	
Deferred tax liabilities		
Property, plant and equipment	$ 1,510	$ 1,506
Other	11	88
Total deferred tax liability	1,521	1,594
Deferred tax assets		
Net operating loss and credit carryovers		
U.S. federal	23	110
State	43	52
Other liabilities	163	142
Total deferred tax asset	229	304
Net deferred tax liability	$ 1,292	$ 1,290

We believe it is more likely than not that we will realize the benefit of our deferred tax assets due to expected future taxable income, including the effect of future reversals of existing taxable temporary differences primarily related to depreciation.

Net Operating Loss (NOL) Carryovers. The table below presents the details of our federal and state NOL carryover periods as of December 31, 2007:

	2008	2009-2012	2013-2017	2018-2027	Total
			(In millions)		
U.S. federal NOL	$ —	$ —	$ —	$ 65	$ 65
State NOL	7	74	262	316	659

Usage of our U.S. federal carryovers is subject to the limitations provided under Sections 382 and 383 of the Internal Revenue Code as well as the separate return limitation year rules of IRS regulations.

Unrecognized Tax Benefits (Liabilities) for Uncertain Tax Matters (FIN No. 48). El Paso files consolidated U.S. federal and certain state tax returns which include our taxable income. In certain states, we file and pay taxes directly to the state taxing authorities. With a few exceptions, we and El Paso are no longer subject to U.S. federal, state and local income tax examinations by tax authorities for years before 1999. Additionally, the Internal Revenue Service has completed an examination of El Paso's U.S. income tax returns for 2003 and 2004, with a tentative settlement at the appellate level for all issues. We do not anticipate the settlement of these matters to have an impact on our unrecognized tax benefits. For our remaining open tax years, our unrecognized tax benefits (liabilities for uncertain tax matters) could increase or decrease our income tax expense and our effective income tax rates as these matters are finalized, although we are currently unable to estimate the range of potential impacts these matters could have on our financial statements.

Upon the adoption of FIN No. 48, and a related amendment to our tax sharing agreement with El Paso, we recorded a reduction of $15 million to the January 1, 2007 balance of retained earnings. As of January 1, 2007, we had unrecognized tax benefits of $17 million (excluding interest and penalties of $6 million) which had not changed as of December 31, 2007. These unrecognized tax benefits (net of federal tax benefits) would favorably affect our income tax expense and our effective income tax rate if recognized in future periods. While the amount of our unrecognized tax benefits could change in the next twelve months, we do not expect this change to have a significant impact on our results of operations or financial position.

We recognize interest and penalties related to unrecognized tax benefits in income tax expense on our income statement. As of January 1, 2007 and December 31, 2007, we had liabilities for interest and penalties related to our unrecognized tax benefits of approximately $6 million. During 2007, we accrued $1 million of interest and paid $1 million related to a settlement with a taxing authority.

4. Financial Instruments

At December 31, 2007 and 2006, the carrying amounts of cash and cash equivalents and trade receivables and payables are representative of their fair value because of the short-term maturity of these instruments. The fair value of our notes receivable from affiliates approximates their carrying value due to the market-based nature of their interest rate. The carrying amounts and estimated fair values of our long-term debt are based on quoted market prices for the same or similar issues and are as follows at December 31:

	2007		2006	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
		(In millions)		
Long-term debt, including current maturities	$1,603	$1,745	$1,602	$1,779

5. Regulatory Assets and Liabilities

Below are the details of our regulatory assets and liabilities at December 31:

	2007	2006
	(In millions)	
Non-current regulatory assets		
Taxes on capitalized funds used during construction	$ 26	$ 20
Postretirement benefits	7	9
Unamortized loss on reacquired debt	2	2
Other	2	2
Total regulatory assets	$ 37	$ 33
Current regulatory liabilities	$ 3	$ —
Non-current regulatory liabilities		
Environmental liability	143	130
Postretirement benefits	25	19
SFAS No. 109 plant regulatory liability and other	10	11
Total regulatory liabilities	$ 181	$ 160

6. Property, Plant and Equipment

Additional Acquisition Costs. At December 31, 2007 and 2006, additional acquisition costs assigned to utility plant was approximately $2.4 billion and accumulated depreciation was approximately $338 million and $299 million, respectively. These additional acquisition costs are being amortized over the life of the related pipeline assets. Our amortization expense related to additional acquisition costs assigned to utility plant was approximately $39 million, $40 million and $40 million for the years ended December 31, 2007, 2006 and 2005.

Asset Retirement Obligations. We have legal obligations associated with the retirement of our natural gas pipeline, transmission facilities and storage wells, as well as obligations related to El Paso's corporate headquarters building. Our legal obligations primarily involve purging and sealing the pipelines if they are abandoned. We also have obligations to remove hazardous materials associated with our natural gas transmission facilities and in our corporate headquarters if these facilities are ever demolished, replaced, or renovated. We continue to evaluate our asset retirement obligations and future development could impact the amounts we record.

Where we can reasonably estimate the asset retirement obligation liability, we accrue a liability based on an estimate of the timing and amount of their settlement. In estimating the fair value of the liabilities associated with our asset retirement obligations, we utilize several assumptions, including a projected inflation rate of 2.5 percent, and credit-adjusted discount rates that currently range from six to eight percent. We record changes in estimates based on the expected amount and timing of payments to settle our asset retirement obligations. In 2006, we also revised our estimates due primarily to the impacts of hurricanes Katrina and Rita. We intend on operating and maintaining our natural gas pipeline and storage system 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 liability for the substantial majority of our natural gas pipeline and storage system assets because these assets have indeterminate lives.

The net asset retirement liability as of December 31 reported on our balance sheet in other current and non-current liabilities, and the changes in the net liability for the years ended December 31, were as follows:

	2007	2006
	(in millions)	
Net asset retirement liability at January 1	$ 47	$ 43
Liabilities settled	(34)	(26)
Liabilities incurred	3	—
Change in estimate	—	29
Accretion expense	1	1
Net asset retirement liability at December 31(1)	$ 17	$ 47

(1) For the years ended December 31, 2007 and 2006, approximately $4 million and $33 million of this amount is reflected in current liabilities which relates primarily to costs associated with obligations related to Hurricanes Katrina and Rita.

7. Debt and Credit Facilities

Debt. Our long-term debt consisted of the following at December 31:

	2007	2006
	(In millions)	
6.0% Debentures due December 2011	$ 86	$ 86
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	300	300
	1,626	1,626
Less:		
Current maturities	—	300
Unamortized discount	23	24
Long-term debt, less current maturities	$ 1,603	$ 1,302

The holders of our $300 million, 7.0% debentures did not exercise their early redemption option, which expired on February 15, 2007. Accordingly, the amount is reflected as long-term debt in our balance sheet at December 31, 2007.

Credit Facilities. In November 2007, El Paso entered into a $1.5 billion credit agreement, which amended and restated its existing $1.75 billion credit agreement. We continue to be an eligible borrower under the $1.5 billion credit agreement and are only liable for amounts we directly borrow. As of December 31, 2007, El Paso had approximately $0.3 billion of letters of credit issued and $0.4 billion of debt outstanding under this facility, none of which was issued or borrowed by us. Our common stock and the common stock of another El Paso subsidiary are pledged as collateral under the credit agreement.

Under El Paso's $1.5 billion credit agreement and our indentures, we are subject to a number of restrictions and covenants. The most restrictive of these include (i) limitations on the incurrence of additional debt, based on a ratio of debt to EBITDA (as defined in the agreements), which shall not exceed 5 to 1; (ii) limitations on the use of proceeds from borrowings; (iii) limitations, in some cases, on transactions with our affiliates; (iv) limitations on the incurrence of liens; and (v) potential limitations on our ability to declare and pay dividends. For the year ended December 31, 2007, we were in compliance with our debt-related covenants.

8. Commitments and Contingencies

Legal Proceedings

Gas Measurement Cases. We and a number of our affiliates were named defendants in actions that generally allege mismeasurement of natural gas volumes and/or heating content resulting in the underpayment of royalties. The first set of cases was filed in 1997 by an individual under the False Claims Act, which have been consolidated for pretrial purposes (In *re: Natural Gas Royalties Qui Tam Litigation,* U.S. District Court for the District of Wyoming). These complaints allege an industry-wide conspiracy to underreport the heating value as well as the volumes of the natural gas produced from federal and Native American lands. In October 2006, the U.S. District Judge issued an order dismissing all claims against all defendants. An appeal has been filed.

Similar allegations were filed in a second set of actions initiated in 1999 in *Will Price, et al. v. Gas Pipelines and Their Predecessors, et al.,* in the District Court of Stevens County, Kansas. The plaintiffs currently seek certification of a class of royalty owners in wells on non-federal and non-Native American lands in Kansas, Wyoming and Colorado. Motions for class certification have been briefed and argued in the proceedings and the parties are awaiting the court's ruling. The plaintiff seeks an unspecified amount of monetary damages in the form of additional royalty payments (along with interest, expenses and punitive damages) and injunctive relief with regard to future gas measurement practices. Our costs and legal exposure related to these lawsuits and claim are not currently determinable.

In addition to the above proceedings, we and our subsidiaries and affiliates are named defendants in numerous lawsuits and governmental proceedings that arise in the ordinary course of our business. For each of these matters, we evaluate the merits of the case, our exposure to the matter, possible legal or settlement strategies and the likelihood of an unfavorable outcome. If we determine that an unfavorable outcome is probable and can be estimated, we establish the necessary accruals. While the outcome of these matters, including those discussed above, cannot be predicted with certainty, and there are still uncertainties related to the costs we may incur, based upon our evaluation and experience to date, we had no accruals for our outstanding legal matters at December 31, 2007. It is possible that new information or future developments could require us to reassess our potential exposure related to these matters and establish our accruals accordingly.

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 on the environment of the disposal or release of specified substances at current and former operating sites. At December 31, 2007, we accrued approximately $10 million for expected remediation costs and associated onsite, offsite and groundwater technical studies and for related environmental legal costs.

Our accrual represents a combination of two estimation methodologies. First, where the most likely outcome can be reasonably estimated, that cost has been accrued. Second, where the most likely outcome cannot be estimated, a range of costs is established and if no one amount in that range is more likely than any other, the lower end of the expected range has been accrued. Our environmental remediation projects are in various stages of completion. Our recorded liabilities reflect our current estimates of amounts we will expend to remediate these sites. 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.

Below is a reconciliation of our accrued liability from January 1, 2007 to December 31, 2007 (in millions):

Balance at January 1, 2007	$ 15
Adjustments for remediation activities	(2)
Payments for remediation activities	(3)
Balance at December 31, 2007	$ 10

For 2008, we estimate that our total remediation expenditures will be approximately $2 million, which will be expended under government directed clean-up plans.

Polychlorinated Biphenyls (PCB) Cost Recoveries. Pursuant to a consent order executed with the United States Environmental Protection Agency in May 1994, we have been conducting remediation activities at certain of our compressor stations associated with the presence of PCBs and other hazardous materials. We have recovered a substantial portion of the environmental costs identified in our PCB remediation project through a surcharge to our customers. An agreement with our customers, approved by the FERC in November 1995, established the surcharge mechanism. The surcharge collection period is currently set to expire in June 2008 with further extensions subject to a filing with the FERC. As of December 31, 2007, we had pre-collected PCB costs of approximately $149 million, which includes interest. This pre-collected amount will be reduced by future eligible costs incurred for the remainder of the remediation project. To the extent actual eligible expenditures are less than the amounts pre-collected, we will refund to our customers the difference, plus carrying charges incurred up to the date of the refunds. At December 31, 2007, our regulatory liability for estimated future refund obligations to our customers was approximately $143 million.

Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) Matters. We have received notice that we could be designated, or have been asked for information to determine whether we could be designated, as a Potentially Responsible Party (PRP) with respect to four active sites under the CERCLA or state equivalents. We have sought to resolve our liability as a PRP at these sites through indemnification by third parties and settlements which provide for payment of our allocable share of remediation costs. As of December 31, 2007, we have estimated our share of the remediation costs at these sites to be between $1 million and $2 million. Because the clean-up costs are estimates and are subject to revision as more information becomes available about the extent of remediation required, and in some cases we have asserted a defense to any liability, our estimates could change. Moreover, liability under the federal CERCLA statute is joint and several, meaning that we could be required to pay in excess of our pro rata share of remediation costs. Our understanding of the financial strength of other PRPs has been considered, where appropriate, in estimating our liabilities. Accruals for these matters are included in the environmental reserve discussed above.

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 and regulations and orders of regulatory agencies, as well as claims for damages to property and the environment or injuries to employees, and 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.

Regulatory Matters

Notice of Inquiry on Pipeline Fuel Retention Policies. In September 2007, the FERC issued a Notice of Inquiry regarding its policy about the in-kind recovery of fuel and lost and unaccounted for gas by natural gas pipeline companies. Under current policy, pipeline companies have options for recovering these costs. For some companies, the tariff states a fixed percentage as a non-negotiable fee-in-kind retained from the volumes tendered for shipment by each shipper. There is also a tracker approach, where the pipeline company's tariff provides for prospective adjustments to the fuel retention rates from time-to-time, but does not include a mechanism to allow the company to reconcile past over or under-recoveries of fuel. Finally, some pipeline companies' tariffs provide for a tracker with a true-up approach, where provisions in the companies' tariff allow for periodic adjustments to the fuel retention rates, and also provide for a true-up of past over and under-recoveries of fuel and lost and unaccounted for gas. In this proceeding, the FERC is seeking comments on whether it should change its current policy and prescribe a uniform method for all pipeline companies to use in recovering these costs. Our tariff currently provides for a fixed percentage recovery basis. At this time, we do not know what impact this proceeding may ultimately have on us.

Notice of Proposed Rulemaking. In October 2007, the Minerals Management Service (MMS) issued a Notice of Proposed Rulemaking for Oil and Gas and Sulphur Operations in the Outer Continental Shelf — Pipelines and Pipeline Rights-of-Way. If adopted, the proposed rules would substantially revise MMS Outer Continental Shelf (OCS) pipeline and rights-of-way (ROW) regulations. The proposed rules would have the effect of: (1) increasing the financial obligations of entities, like us, which have pipelines and pipeline rights-of-way in the OCS; (2) increasing the regulatory requirements imposed on the operation and maintenance of existing pipelines in the OCS; and (3) increasing the requirements and preconditions for obtaining new rights-of-way in the OCS.

Commitments and Purchase Obligations

Capital Commitments. At December 31, 2007, we had capital and investment commitments of approximately $21 million. We have other planned capital and investment projects that are discretionary in nature, with no substantial contractual capital commitments made in advance of the actual expenditures. In addition, we have entered into unconditional purchase obligations for products, services and other capital assets, including a storage agreement with our affiliate, totaling $115 million at December 31, 2007. Our annual obligations under these agreements are $48 million in 2008, $30 million in 2009, $11 million in 2010, $9 million in 2011, $5 million in 2012 and $12 million in total thereafter.

Operating Leases and Other Commercial Commitments. We lease property, facilities and equipment under various operating leases. Minimum future annual rental commitments on our operating leases as of December 31, 2007, were as follows:

Year Ending December 31,	(In millions)
2008	$ 1
2009	1
2010	1
2011	1
Thereafter	2
Total	$ 6

Rental expense on our operating leases for each of the three years ended December 31, 2007, 2006 and 2005 was $2 million, $2 million and $3 million. These amounts include rent allocated to us from El Paso.

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

9. Retirement Benefits

Pension and Retirement Benefits. El Paso maintains a pension plan and a retirement savings plan covering substantially all of its U.S. employees, including our employees. The benefits under the pension plan are determined under a cash balance formula. Under its retirement savings plan, El Paso matches 75 percent of participant basic contributions up to six percent of eligible compensation and can make additional discretionary matching contributions. El Paso is responsible for benefits accrued under its plans and allocates the related costs to its affiliates.

Postretirement Benefits. We provide medical and life insurance benefits for a closed group of retirees who were eligible to retire on December 31, 1996, and did so before July 1, 1997. Medical benefits for this closed group may be subject to deductibles, co-payment provisions, and other limitations and dollar caps on the amount of employer costs. El Paso reserves the right to change these benefits. Employees in this group who retire after July 1, 1997 continue to receive limited postretirement life insurance benefits. Our postretirement benefit plan costs are prefunded to the extent these costs are recoverable through our rates and in 1992, we began recovering through our rates the other postretirement benefits (OPEB) costs. To the extent actual OPEB costs differ from the amounts recovered in rates, a regulatory asset or liability is recorded. We do not expect to make any contributions to our postretirement benefit plan in 2008.

In December 2006, we adopted the recognition provisions of SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans — an Amendment of FASB Statements No. 87, 88, 106, and 132(R),* and began reflecting assets and liabilities related to our postretirement benefit plan based on its funded or unfunded status and reclassified all actuarial deferrals as a component of accumulated other comprehensive income. In March 2007, the FERC issued guidance requiring regulated pipeline companies to recognize a regulatory asset or liability for the amount that would otherwise be recorded in accumulated other comprehensive income under SFAS No. 158, if it is probable that amounts calculated on the same basis as SFAS No. 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions,* would be included in our rates in future periods. Upon adoption of this FERC guidance, we reclassified approximately $3 million from the beginning balance of accumulated other comprehensive income to a regulatory liability, which represented the amount we believe will be included in our future rates.

Change in Accumulated Postretirement Benefit Obligation, Plan Assets and Funded Status. Our benefits are presented and computed as of and for the twelve months ended September 30:

	2007	2006
	(In millions)	
Change in accumulated postretirement benefit obligation:		
Accumulated postretirement benefit obligation at beginning of period	$ 22	$ 24
Interest cost	1	1
Participant contributions	1	1
Actuarial loss	—	(2)
Benefits paid	(2)	(2)
Accumulated postretirement benefit obligation at end of period	$ 22	$ 22
Change in plan assets:		
Fair value of plan assets at beginning of period	$ 23	$ 19
Actual return on plan assets	2	—
Employer contributions	5	5
Participant contributions	1	1
Benefits paid	(2)	(2)
Fair value of plan assets at end of period	$ 29	$ 23
Reconciliation of funded status:		
Fair value of plan assets at September 30	$ 29	$ 23
Less: Accumulated postretirement benefit obligation, end of period	22	22
Funded status at September 30	7	1
Fourth quarter contributions and income	1	1
Net asset at December 31	$ 8	$ 2

Expected Payment of Future Benefits. As of December 31, 2007, we expect the following payments (net of participant contributions) under our plan (in million):

Year Ending December 31,	
2008	$ 2
2009	2
2010	2
2011	2
2012	2
2013-2017	9

Components of Net Benefit Cost. For each of the years ended December 31, the components of net benefit cost are as follows:

	2007	2006	2005
		(In millions)	
Interest cost	$ 1	$ 1	$ 2
Expected return on plan assets	(1)	(1)	(1)
Net postretirement benefit cost	$ —	$ —	$ 1

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 for 2007, 2006 and 2005:

	2007	2006	2005
		(Percent)	
Assumptions related to benefit obligations at September 30:			
Discount rate	6.05	5.50	
Assumptions related to benefit costs at December 31:			
Discount rate	5.50	5.25	5.75
Expected return on plan assets(1)	8.00	8.00	7.50

(1) The expected return on plan assets is a pre-tax rate of return based on our targeted portfolio of investments. Our postretirement benefit plan's investment earnings are subject to unrelated business income tax at a rate of 35%. The expected return on plan assets for our postretirement benefit plan is calculated using the after-tax rate of return.

Actuarial estimates for our postretirement benefits plan assumed a weighted average annual rate of increase in the per capita costs of covered health care benefits of 9.4 percent in 2007, gradually decreasing to 5.0 percent by the year 2015. Changes in our assumed health care cost trend rates do not have a material impact on the amounts reported for our interest costs or our accumulated postretirement benefit obligations.

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 to meet the benefit obligations to participants, retirees and beneficiaries exists. Investment objectives are long-term in nature covering typical market cycles of three to five years. Any shortfall of investment performance compared to investment objectives is the result of general economic and capital market conditions. The following table provides the target and actual asset allocations in our postretirement benefit plan as of September 30:

Asset Category	Target	Actual 2007	Actual 2006
		(Percent)	
Equity securities	65	63	61
Debt securities	35	33	32
Cash and cash equivalents	—	4	7
Total	100	100	100

10. Supplemental Cash Flow Information

The following table contains supplemental cash flow information for each of the three years ended December 31:

	2007	2006	2005
		(In millions)	
Interest paid, net of capitalized interest	$116	$119	$121
Income tax payments (refunds)	121	13	(21)

11. Investment in Unconsolidated Affiliate and Transactions with Affiliates

Investment in Unconsolidated Affiliate

Bear Creek Storage Company (Bear Creek). We have a 50 percent ownership interest in Bear Creek, a joint venture with Southern Gas Storage Company, our affiliate. During 2007, 2006 and 2005, we received $27 million, $17 million and $64 million in dividends from Bear Creek.

Summarized financial information for our proportionate share of Bear Creek as of and for the years ended December 31 is presented as follows:

	2007	2006	2005
		(In millions)	
Operating results data:			
Operating revenues	$19	$20	$18
Operating expenses	8	7	7
Income from continuing operations and net income	13	15	14

	2007	2006
	(In millions)	
Financial position data:		
Current assets	$28	$38
Non-current assets	58	60
Current liabilities	2	—
Equity in net assets	84	98

Transactions with Affiliates

Cash Management Program and Other Notes Receivable. We participate in El Paso's cash management program which matches short-term cash surpluses and needs of participating affiliates, thus minimizing total borrowings from outside sources. El Paso uses the cash management program to settle intercompany transactions between participating affiliates. We have historically advanced cash to El Paso in exchange for an affiliated note receivable that is due upon demand. At December 31, 2007 and 2006, we had notes receivable from El Paso and other affiliates of $582 million and $651 million. The interest rate on these notes at December 31, 2007 and 2006 was 6.5% and 5.3%.

At December 31, 2007 and 2006, we had non-interest bearing notes receivable of $334 million and $336 million from an El Paso affiliate. In addition, we had a variable interest rate note receivable from El Paso of $118 million and $86 million at December 31, 2007 and 2006. Each of these notes is due upon demand. The interest rate on the variable rate note at December 31, 2007 and 2006 was 6.5% and 5.3%.

We do not intend to settle these notes within twelve months and therefore have classified them as non-current on our balance sheets.

Accounts Receivable Sales Program. We sell certain accounts receivable to a qualifying special purpose entity (QSPE) and reflect our subordinated interest in these receivables as accounts receivable — affiliate on our balance sheets. We earn a fee for servicing the receivables and performing all administrative duties for the QSPE. At December 31, 2007 and December 31, 2006, our subordinated beneficial interest in the receivables sold was $61 million and $35 million. The fair value of the fees earned was not material to our financial statements for the years ended December 31, 2007 and 2006.

Income Taxes. El Paso files consolidated U.S. federal and certain state tax returns which include our taxable income. In certain states, we file and pay taxes directly to the state taxing authorities. At December 31, 2007 and 2006, we had federal and state income taxes payable of $13 million and $53 million. The majority of these balances, as well as deferred income taxes and amounts associated with the resolution of unrecognized tax benefits, will become payable to El Paso. See Note 1 for a discussion of our income tax policy.

During 2007, we amended our tax sharing agreement and intercompany tax billing policy with El Paso to clarify the billing of taxes and tax related items to El Paso's subsidiaries. We also settled with El Paso certain tax attributes previously reflected as deferred income taxes in our financial statements for $77 million through El Paso's cash management program. This settlement is reflected as operating activities in our statement of cash flows.

During 2007, El Paso utilized approximately $75 million of our deferred tax assets from net operating loss carryovers. This utilization offset our taxes payable to El Paso.

Other Affiliate Balances. At December 31, 2007 and 2006, we have contractual deposits from our affiliates of $8 million.

Affiliate Revenues and Expenses. We transport gas for El Paso Marketing L.P. in the normal course of our business on the same terms as non-affiliates.

El Paso bills us directly for certain general and administrative costs and allocates a portion of its general and administrative costs to us. In addition to allocations from El Paso, we allocate costs to our pipeline affiliates for their proportionate share of our pipeline services. The allocations from El Paso and the allocations to our affiliates are based on the estimated level of effort devoted to our operations and the relative size of our and their EBIT, gross property and payroll.

We store natural gas in an affiliated storage facility and utilize the pipeline system of an affiliate to transport some of our natural gas in the normal course of our business based on the same terms as non-affiliates.

The following table shows overall revenues and charges from our affiliates for each of the three years ended December 31:

	2007	2006	2005
		(In millions)	
Revenues from affiliates	$21	$22	$25
Operation and maintenance expenses from affiliates	57	56	70
Reimbursements of operating expenses charged to affiliates(1)	45	79	79

(1) Decrease in activity in 2007 is due to El Paso's sale of its subsidiary, ANR Pipeline Company.

12. Supplemental Selected Quarterly Financial Information (Unaudited)

Our financial information by quarter is summarized below. Due to the seasonal nature of our business, information for interim periods may not be indicative of our results of operations for the entire year.

	Quarters Ended				
	March 31	June 30	September 30	December 31	Total
			(In millions)		
2007					
Operating revenues	$226	$ 220	$ 193	$ 223	$862
Operating income	101	85	47	65	298
Net income	55	43	22	33	153
2006					
Operating revenues	$230	$ 194	$ 182	$ 187	$793
Operating income	101	62	40	56	259
Net income	52	29	17	29	127