



Northern Natural Gas Company

**Financial Statements (Unaudited) as of and for the
Quarterly Period Ended June 30, 2017**

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

	As of	
	June 30, 2017	December 31, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 35,205	\$ 48,398
Accounts receivable, net	45,015	75,147
Accounts receivable from affiliates	3,989	8,708
Notes receivable from BHE	315,000	155,000
Transportation and exchange gas receivables	12,324	12,028
Inventories	29,435	28,314
Other current assets	10,314	10,057
Total current assets	451,282	337,652
Property, plant and equipment, net	2,838,039	2,812,523
Regulatory assets	145,681	150,436
Other assets	42,007	40,969
Total assets	\$ 3,477,009	\$ 3,341,580
LIABILITIES AND SHAREHOLDER'S EQUITY		
Current liabilities:		
Accounts payable	\$ 36,395	\$ 44,312
Accounts payable to affiliates	606	1,253
Accrued interest	12,260	12,260
Accrued property, income and other taxes	94,536	55,501
Transportation and exchange gas payables	12,013	10,630
Derivative contracts	14,796	14,025
Other current liabilities	29,906	35,446
Total current liabilities	200,512	173,427
Regulatory liabilities	26,428	25,393
Derivative contracts	43,822	50,507
Asset retirement obligations	33,186	32,676
Long-term debt	795,714	795,478
Deferred income taxes	844,468	832,758
Other long-term liabilities	23,515	21,923
Total liabilities	1,967,645	1,932,162
Commitments and contingencies (Notes 4 and 6)		
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	527,495	427,549
Total shareholder's equity	1,509,364	1,409,418
Total liabilities and shareholder's equity	\$ 3,477,009	\$ 3,341,580

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

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

	Six-Month Periods Ended June 30,	
	2017	2016
Operating revenue:		
Transportation	\$ 310,367	\$ 297,451
Storage	28,556	27,332
Gas, liquids and other sales	22,597	4,936
Total operating revenue	361,520	329,719
Operating costs and expenses:		
Operating and maintenance	94,849	87,095
Cost of gas and liquids sales	23,192	6,947
Depreciation and amortization	38,221	36,806
Taxes, other than income taxes	26,787	27,275
Total operating costs and expenses	183,049	158,123
Operating income	178,471	171,596
Other income (expense):		
Interest expense, net	(19,247)	(19,446)
Interest income	2,011	834
Other, net	4,759	2,506
Total other income (expense)	(12,477)	(16,106)
Income before income tax expense	165,994	155,490
Income tax expense	66,048	61,887
Net income	\$ 99,946	\$ 93,603

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

	<u>Common Stock</u>	<u>Additional Paid-In Capital</u>	<u>Retained Earnings</u>	<u>Total</u>
Balance, December 31, 2015	\$ 1	\$ 981,868	\$ 428,170	\$ 1,410,039
Net income	—	—	93,603	93,603
Dividends on common stock	—	—	(85,000)	(85,000)
Balance, June 30, 2016	<u>\$ 1</u>	<u>\$ 981,868</u>	<u>\$ 436,773</u>	<u>\$ 1,418,642</u>
Balance, December 31, 2016	\$ 1	\$ 981,868	\$ 427,549	\$ 1,409,418
Net income	—	—	99,946	99,946
Balance, June 30, 2017	<u>\$ 1</u>	<u>\$ 981,868</u>	<u>\$ 527,495</u>	<u>\$ 1,509,364</u>

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

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

	Six-Month Periods Ended June 30,	
	2017	2016
Cash flows from operating activities:		
Net income	\$ 99,946	\$ 93,603
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation and amortization	38,221	36,806
Amortization of debt issuance costs	225	235
Deferred income taxes	11,710	33,607
Other, net	1,106	3,103
Changes in other operating assets and liabilities:		
Accounts receivable and other assets	37,007	31,036
Inventories	729	276
Accounts payable and other accrued liabilities	1,479	(288)
Gas balancing activities	(7,687)	(3,535)
Accrued property, income and other taxes	39,035	7,131
Net cash flows from operating activities	221,771	201,974
Cash flows from investing activities:		
Capital expenditures	(72,467)	(60,885)
Purchases of marketable securities	(4,867)	(4,475)
Proceeds from sales of marketable securities	2,370	2,550
Net cash flows from investing activities	(74,964)	(62,810)
Cash flows from financing activities:		
Dividends on common stock	—	(85,000)
Issuance of promissory notes by BHE	(160,000)	—
Net cash flows from financing activities	(160,000)	(85,000)
Net change in cash and cash equivalents	(13,193)	54,164
Cash and cash equivalents at beginning of period	48,398	27,523
Cash and cash equivalents at end of period	\$ 35,205	\$ 81,687

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

Northern Natural Gas Company
Notes to Financial Statements
(Unaudited)

(1) General

Northern Natural Gas Company (the "Company") is an indirect wholly owned subsidiary of Berkshire Hathaway Energy Company ("BHE"), a holding company that owns subsidiaries principally engaged in energy businesses. 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 System consists of 14,700 miles of natural gas pipelines, including 6,300 miles of mainline transmission pipelines and 8,400 miles of branch and lateral pipelines, with a Market Area design capacity of 5.8 billion cubic feet ("Bcf") per day, a Field Area delivery capacity of 1.7 Bcf per day to the Market Area and 1.1 Bcf per day to the West Texas area and over 73 Bcf of firm service and operational storage cycle capacity in five storage facilities. The System is configured with approximately 2,300 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 delivers over 1.0 trillion cubic feet of natural gas to its customers annually.

The Company has no subsidiaries and does not hold a controlling financial interest in any other entity. The unaudited Financial Statements are prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information. Accordingly, they do not include all of the disclosures required by GAAP for annual financial statements. Management believes the unaudited Financial Statements contain all adjustments (consisting only of normal recurring adjustments) considered necessary for the fair presentation of the unaudited Financial Statements as of June 30, 2017 and for the six-month periods ended June 30, 2017 and 2016. The results of operations for the six-month period ended June 30, 2017 are not necessarily indicative of the results to be expected for the full year. The Company has evaluated subsequent events through August 29, 2017, which is the date the unaudited Financial Statements were available to be issued.

The preparation of the unaudited 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 unaudited Financial Statements and the reported amounts of revenue and expenses during the period. Actual results may differ from the estimates used in preparing the unaudited Financial Statements. Note 2 of Notes to Financial Statements included in the Company's audited Financial Statements for the year ended December 31, 2016 describes the most significant accounting policies used in the preparation of the unaudited Financial Statements. There have been no significant changes in the Company's assumptions regarding significant accounting estimates and policies during the six-month period ended June 30, 2017.

(2) New Accounting Pronouncements

In March 2017, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2017-07, which amends FASB Accounting Standards Codification ("ASC") Topic 715, "Compensation - Retirement Benefits." The amendments in this guidance require that an employer disaggregate the service cost component from the other components of net benefit cost and report the service cost component in the same line item as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the statement of operations separately from the service cost component and outside the subtotal of operating income. Additionally, the guidance only allows the service cost component to be eligible for capitalization when applicable. This guidance is effective for interim and annual reporting periods beginning after December 15, 2017 for public entities. For nonpublic entities, this guidance is effective for annual reporting periods beginning after December 15, 2018 and interim reporting periods within annual reporting periods beginning after December 15, 2019. This guidance must be adopted retrospectively for the presentation of the service cost component and the other components of net benefit cost in the statement of operations and prospectively for the capitalization of the service cost component in the balance sheet, with early adoption permitted. The Company plans to adopt this guidance effective January 1, 2018 and is currently evaluating the impact on its Financial Statements and disclosures included within Notes to Financial Statements.

In November 2016, the FASB issued ASU No. 2016-18, which amends FASB ASC Subtopic 230-10, "Statement of Cash Flows - Overall." The amendments in this guidance require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows. This guidance is effective for interim and annual reporting periods beginning after December 15, 2017 for public entities. For nonpublic entities, this guidance is effective for annual reporting periods beginning after December 15, 2018 and interim reporting periods within annual reporting periods beginning after December 15, 2019. This guidance is required to be adopted retrospectively, with early adoption permitted. The Company plans to adopt this guidance effective January 1, 2018 and is currently evaluating the impact on its Financial Statements and disclosures included within Notes to Financial Statements.

In August 2016, the FASB issued ASU No. 2016-15, which amends FASB ASC Topic 230, "Statement of Cash Flows." The amendments in this guidance address the classification of eight specific cash flow issues within the statement of cash flows with the objective of reducing the existing diversity in practice. This guidance is effective for interim and annual reporting periods beginning after December 15, 2017 for public entities. For nonpublic entities, this guidance is effective for annual reporting periods beginning after December 15, 2018 and interim reporting periods within annual reporting periods beginning after December 15, 2019. This guidance is required to be adopted retrospectively, with early adoption permitted. The Company plans to adopt this guidance effective January 1, 2018 and does not believe the adoption of this guidance will have a material impact on its Financial Statements.

In February 2016, the FASB issued ASU No. 2016-02, which creates FASB 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 in 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. This guidance is effective for interim and annual reporting

periods beginning after December 15, 2018 for public entities. For nonpublic entities, this guidance is effective for annual reporting periods beginning after December 15, 2019 and interim reporting periods within annual reporting periods beginning after December 15, 2020. This guidance is required to be adopted using a modified retrospective approach, with early adoption permitted. The Company plans to adopt this guidance effective January 1, 2019 and is currently evaluating the impact on its Financial Statements and disclosures included within Notes to Financial Statements.

In May 2014, the FASB issued ASU No. 2014-09, which creates FASB ASC Topic 606, "Revenue from Contracts with Customers" and supersedes ASC Topic 605, "Revenue Recognition." The guidance replaces industry-specific guidance and establishes a single five-step model to identify and recognize revenue. The core principle of the guidance is that an entity should recognize revenue upon transfer of control of promised goods or services to customers in an amount that reflects the consideration to which an entity expects to be entitled in exchange for those goods or services. Additionally, the guidance requires the entity to disclose further quantitative and qualitative information regarding the nature and amount of revenues arising from contracts with customers, as well as other information about the significant judgments and estimates used in recognizing revenues from contracts with customers. In August 2015, the FASB issued ASU No. 2015-14, which defers the effective date of ASU No. 2014-09 one year. This guidance is effective for interim and annual reporting periods beginning after December 15, 2017 for public entities. For nonpublic entities, this guidance is effective for annual reporting periods beginning after December 15, 2018 and interim reporting periods within annual reporting periods beginning after December 15, 2019, with early adoption permitted. During 2016, the FASB issued several ASUs that clarify the implementation guidance for ASU No. 2014-09 but do not change the core principle of the guidance. This guidance may be adopted retrospectively or under a modified retrospective method where the cumulative effect is recognized at the date of initial application. The Company plans to adopt the guidance effective January 1, 2018 under the modified retrospective method and is currently evaluating the impact on its Financial Statements and disclosures included within Notes to Financial Statements. The Company currently does not expect the timing and amount of revenue currently recognized to be materially different after adoption of the new guidance as a majority of revenue is recognized when the Company has the right to invoice as it corresponds directly with the value to the customer of the Company's performance to date.

(3) 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 \$0.4 million and \$0.5 million for the six-month periods ended June 30, 2017 and 2016, respectively. As of June 30, 2017, 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 \$6.4 million and \$25.5 million, respectively. As of December 31, 2016, 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 \$6.4 million and \$24.9 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.

(4) Risk Management and Hedging Activities

The Company is exposed to the impact of market fluctuations in natural gas prices as supply and demand are impacted by, among many other unpredictable items, weather, market liquidity, customer usage, storage and transportation constraints. The Company does not engage in a material amount of proprietary trading activities.

The Company has established a risk management process that is designed to identify, assess, manage, monitor and report each of the various types of risk involved in its business. To mitigate a portion of its natural gas price risk, the Company uses commodity derivative contracts generally at fixed prices to hedge natural gas for operational and preferred deferred delivery ("PDD") storage, fuel requirements and other transactions. The Company uses natural gas commodity swaps to hedge the margin on forecasted gas sales and purchases required for operational storage balancing purposes and to hedge the margin on anticipated future PDD storage contracts.

For certain designated markets, certain customers pay a fixed price of \$0.09 per decatherm ("dth") of volumes delivered to purchase compressor fuel and system use gas from the Company. The Company estimates it will be required to purchase an annual average of 0.7 Bcf of natural gas through October 2022 to meet these requirements based on an average system requirements factor of 1.0% of volumes delivered. The Company's contracts with these customers provide service through October 2019, with annual renewal options for one customer to continue service through October 2022. As of June 30, 2017, the Company had entered into swap agreements covering the expected contractual requirements through October 2022.

Interest rate risk exists on future debt issuances. The Company manages its interest rate risk by limiting its exposure to variable interest rates primarily through the issuance of fixed-rate long-term debt and by monitoring market changes in interest rates. Additionally, the Company may from time to time enter into interest rate derivative contracts, such as interest rate swaps or locks, to mitigate the Company's exposure to interest rate risk. The Company does not hedge all of its commodity price and interest rate risks, thereby exposing the unhedged portion to changes in market prices.

There have been no significant changes in the Company's accounting policies related to derivatives. Refer to Note 5 for additional information on derivative contracts.

The following table, which reflects master netting arrangements and excludes contracts that have been designated as normal under the normal purchases or normal sales exception afforded by GAAP, summarizes the fair value of the Company's derivative contracts, on a gross basis, and reconciles those amounts to the amounts presented on a net basis on the Balance Sheets (in thousands):

	Derivative Assets		Derivative Liabilities		Total
	Current⁽¹⁾	Current	Noncurrent	Total	
<u>As of June 30, 2017</u>					
Not designated as hedging contracts⁽²⁾:					
Commodity assets	\$ 370	\$ 138	\$ 13	\$ 521	
Commodity liabilities	—	(14,934)	(43,835)	(58,769)	
Total	370	(14,796)	(43,822)	(58,248)	
Total derivatives - net basis⁽³⁾	\$ 370	\$ (14,796)	\$ (43,822)	\$ (58,248)	
<u>As of December 31, 2016</u>					
Not designated as hedging contracts⁽²⁾:					
Commodity assets	\$ —	\$ 502	\$ 59	\$ 561	
Commodity liabilities	—	(14,527)	(50,566)	(65,093)	
Total	—	(14,025)	(50,507)	(64,532)	
Total derivatives - net basis⁽³⁾	\$ —	\$ (14,025)	\$ (50,507)	\$ (64,532)	

- (1) Current derivative assets are included in other current assets on the Balance Sheets.
- (2) The Company's commodity derivatives not designated as hedging contracts are generally included in regulated rates, and as of June 30, 2017 and December 31, 2016, a regulatory asset of \$58.2 million and \$64.5 million, respectively, was recorded related to the net derivative liability of \$58.2 million and \$64.5 million, respectively.
- (3) The net notional amounts of outstanding commodity derivative contracts with fixed price terms that comprise the mark-to-market values included above are 8 million and 9 million dth of natural gas purchases, net, as of June 30, 2017 and December 31, 2016, respectively.

Not Designated as Hedging Contracts

The following table reconciles the beginning and ending balances of the Company's regulatory assets and summarizes the pre-tax gains and losses on open commodity derivative contracts recognized in regulatory assets, as well as amounts reclassified to earnings for the six-month periods ended June 30 (in thousands):

	<u>2017</u>	<u>2016</u>
Beginning balance	\$ 64,532	\$ 74,963
Changes in fair value recognized in regulatory assets	902	1,562
Net gains reclassified to operating revenue	191	—
Net losses reclassified to unamortized contract value regulatory asset	(1,627)	—
Net losses reclassified to cost of gas and liquids sales	(5,750)	(6,663)
Ending balance	<u>\$ 58,248</u>	<u>\$ 69,862</u>

Credit Risk

The Company is exposed to counterparty credit risk associated with wholesale energy supply and marketing activities with other utilities, energy marketing companies, financial institutions and other market participants. Credit risk may be concentrated to the extent the Company's counterparties have similar economic, industry or other characteristics and due to direct or indirect relationships among the counterparties. Before entering into a transaction, the Company analyzes the financial condition of each significant wholesale counterparty, establishes limits on the amount of unsecured credit to be extended to each counterparty and evaluates the appropriateness of unsecured credit limits on an ongoing basis. To further mitigate wholesale counterparty credit risk, the Company enters into netting and collateral arrangements that may include margining and cross-product netting agreements and obtain third-party guarantees, letters of credit and cash deposits. If required, the Company exercises rights under these arrangements, including calling on the counterparty's credit support arrangement.

Collateral and Contingent Features

In accordance with industry practice, certain derivative contracts contain credit support provisions that in part base certain collateral requirements on credit ratings for senior unsecured debt as reported by one or more of the three recognized credit rating agencies. These derivative contracts may either specifically provide bilateral rights to demand cash or other security if credit exposures on a net basis exceed specified rating-dependent threshold levels ("credit-risk-related contingent features") or provide the right for counterparties to demand "adequate assurance," or in some cases terminate the contract, in the event of a material adverse change in creditworthiness. These rights can vary by contract and by counterparty. As of June 30, 2017, the Company's credit ratings from the three recognized credit rating agencies were investment grade.

The aggregate fair value of the Company's derivative contracts in liability positions with specific credit-risk-related contingent features totaled \$58.8 million and \$64.5 million as of June 30, 2017 and December 31, 2016, respectively. If all credit-risk-related contingent features for derivative contracts in liability positions had been triggered as of June 30, 2017 and December 31, 2016, the Company would have been required to post \$58.6 million and \$64.5 million, respectively, of collateral. The Company's collateral requirements could fluctuate considerably due to market price volatility, changes in credit ratings, changes in legislation or regulation, or other factors.

(5) 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 financial 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				Total
	Level 1	Level 2	Level 3	Other⁽¹⁾	
<u>As of June 30, 2017</u>					
Assets:					
Commodity derivatives	\$ —	\$ 521	\$ —	\$ (151)	\$ 370
Money market mutual funds ⁽²⁾	47,652	—	—	—	47,652
Investment funds	7,596	—	—	—	7,596
	<u>\$ 55,248</u>	<u>\$ 521</u>	<u>\$ —</u>	<u>\$ (151)</u>	<u>\$ 55,618</u>
Liabilities - commodity derivatives	<u>\$ —</u>	<u>\$ (58,769)</u>	<u>\$ —</u>	<u>\$ 151</u>	<u>\$ (58,618)</u>
<u>As of December 31, 2016</u>					
Assets:					
Commodity derivatives	\$ —	\$ 561	\$ —	\$ (561)	\$ —
Money market mutual funds ⁽²⁾	67,046	—	—	—	67,046
Investment funds	4,433	—	—	—	4,433
	<u>\$ 71,479</u>	<u>\$ 561</u>	<u>\$ —</u>	<u>\$ (561)</u>	<u>\$ 71,479</u>
Liabilities - commodity derivatives	<u>\$ —</u>	<u>\$ (65,093)</u>	<u>\$ —</u>	<u>\$ 561</u>	<u>\$ (64,532)</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 and crude oil 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. Refer to Note 4 for further discussion regarding the Company's risk management and hedging activities.

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.

(6) Commitments and Contingencies

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 leases 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 established a three-person condemnation panel which issued a report in August 2014, recommending a total award of \$7.3 million. The federal district court issued a decision in February 2015, adopting the condemnation panel's recommendations. The Company filed its appeal of the final condemnation order to the Tenth Circuit Court of Appeals in November 2015. All of the defendants cross-appealed. In July 2017, the Tenth Circuit Court of Appeals reversed the federal district court award requiring the Company to pay for the value of storage gas remaining in the extension area and rejected the appeals of the defendants for additional compensation for storage rights and wells that were converted to observation wells. The Tenth Circuit Court of Appeals also rejected the defendants' request for attorney's fees. The decision reduces the condemnation award by approximately \$6.0 million. The landowner and producer defendants filed requests for rehearing of the Tenth Circuit Court of Appeals decision. If rehearing is not granted, the case will be remanded to the federal district court for final disposition.
- 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 ("District Court") 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 and unjust enrichment claims have been dismissed, but the nuisance claim remains. In May 2016, the court issued an order lifting the stay that had been in place since August 2011. The magistrate established dates for amending pleadings, discovery and expert reports. The trial is set for June 2018.
- 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. In April 2010, the Pratt County State District Court granted the defendants' motion for summary judgment, finding that the Company does not have title to storage gas that has migrated beyond adjoining property. The Company appealed the decision and in

March 2013, the Kansas Supreme Court determined that the Company lost title to storage gas when it migrated and was produced beyond one mile of the storage field certificated boundaries. The case has been remanded for a determination of the Company's recovery of conversion damages from ONEOK and Lumen for storage gas produced 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 2, 2010. The Company filed a motion to modify the summary judgment ruling which was heard in October 2014. In June 2015, the court indicated an order would be entered denying the Company's motion, and that order was issued in July 2017. The Company will appeal the decision to the Kansas Court of Appeals. The proceeds from June 2010 through February 2011 when the wells were shut-in will continue to be held in suspense pending appeal with the Kansas Court of Appeals. The Company has valued these amounts at approximately \$4.7 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 remain stayed.

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.

(7) Other Related Party Transactions

The Company provided gas transportation, storage and other services to MEC totaling \$33.5 million and \$34.1 million for the six-month periods ended June 30, 2017 and 2016, 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 \$2.9 million and \$2.8 million for the six-month periods ended June 30, 2017 and 2016, respectively. MEC also provided electricity and other services to the Company of \$0.4 million and \$0.3 million for the six-month periods ended June 30, 2017 and 2016, respectively. The Company reimbursed MEC \$30.6 million and \$29.5 million for the six-month periods ended June 30, 2017 and 2016, 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 \$1.1 million for each of the six-month periods ended June 30, 2017 and 2016. Income tax transactions with BHE resulted in net payments of \$9.3 million and \$17.2 million for the six-month periods ended June 30, 2017 and 2016, respectively.

As of June 30, 2017 and December 31, 2016, the Company had accounts payable to BHE and certain subsidiaries for intercompany transactions totaling \$0.6 million and \$1.3 million, respectively. The Company also had accounts receivable from affiliates of \$4.0 million and \$8.7 million as of June 30, 2017 and December 31, 2016, 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

\$1.0 million and \$0.8 million for the six-month periods ended June 30, 2017 and 2016, respectively, for these services.

The Company possesses demand promissory notes from BHE. The balance of the demand promissory notes as of June 30, 2017 and December 31, 2016 was \$315.0 million and \$155.0 million, respectively. The notes contain variable interest rates based on 30-day LIBOR plus a fixed spread per annum. Interest income of \$1.8 million and \$0.7 million was recorded for the six-month periods ended June 30, 2017 and 2016, respectively.

(8) Subsequent Events

In July 2017, BHE issued promissory notes to the Company totaling \$25.0 million.