

EL PASO CORP/DE  
Form POS AM  
May 09, 2005

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**As filed with the Securities and Exchange Commission on May 6, 2005**

**Registration No. 333-82412**

**SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

**Post-Effective Amendment No. 1 to Form S-3**

**on**

**Form S-1**

**REGISTRATION STATEMENT**

**UNDER**

**THE SECURITIES ACT OF 1933**

**EL PASO CORPORATION**

*(Exact Name of Registrant As Specified In its Charter)*

**Delaware**

*(State or Other Jurisdiction of  
Incorporation or Organization)*

**El Paso Building**

**1001 Louisiana Street**

**Houston, Texas 77002**

**(713) 420-2600**

*(Address, Including Zip Code, and  
Telephone Number, Including  
Area Code, of Registrant's  
Principal Executive Offices)*

**76-0568816**

*(I.R.S. Employer Identification Number)*

**Robert W. Baker, Esq.**

**El Paso Building**

**1001 Louisiana Street**

**Houston, Texas 77002**

**(713) 420-2600**

*(Name, Address, Including Zip Code,  
and Telephone Number, Including  
Area Code, of Agent For Service)*

***Copies To:***

**Andrews Kurth LLP**

**600 Travis, Suite 4200**

**Houston, Texas 77002**

**Attention: G. Michael O Leary, Esq.**

**(713) 220-4200**

**Approximate date of commencement of proposed sale to the public:** From time to time after the effective date of this Registration Statement, as determined in light of market conditions and other factors.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act of 1933, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act of 1933, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

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If this form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box.

This Registration Statement on Form S-1 constitutes a post-effective amendment to the Company's Registration Statement on Form S-3 (Registration No. 333-82412). The Company is filing this post-effective amendment for the purpose of meeting the requirements of Section 10(a)(3) of the Securities Act of 1933. Pursuant to Rule 401(b) under the Securities Act, the Company is filing this post-effective amendment on Form S-1, as it is currently ineligible to file a registration statement on Form S-3.

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, or until this Registration Statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

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### EXPLANATORY NOTE

On June 26, 2002 we issued 11,500,000 equity security units, or ESUs, of which 5,442,047 ESUs are currently issued and outstanding. Each ESU consists of (a) a purchase contract which obligates the holder to purchase from us, at a purchase price of \$50, shares of our common stock on August 16, 2005 and (b) a senior note with a principal amount of \$50 that is due on August 16, 2005. The issuance of the ESUs, and the issuance pursuant to the purchase contracts of the shares of our common stock on August 16, 2005 or upon the early settlement of the purchase contracts, was originally registered under a shelf registration statement on Form S-3 (Common File No. 333-82412). Due to the late filing of our Annual Report on Form 10-K for the year ended December 31, 2003, under applicable SEC rules we no longer qualify for the use of a registration statement on Form S-3 or for incorporation of information by reference into a prospectus. In order to assure that shares of our common stock issued upon maturity or early settlement of the purchase contracts are so issued under an effective registration statement, we have filed a post-effective amendment on Form S-1 to the registration statement described above. This prospectus is a part of that post-effective amendment and registers the issuance of the shares of our common stock upon the maturity of the purchase contracts on August 16, 2005 or early settlement of such purchase contracts. As we no longer qualify for incorporation of information by reference under applicable SEC rules, no information is incorporated in this prospectus by reference.

### INDUSTRY AND MARKET DATA

We have obtained some industry and market share data from third party sources that we believe to be reliable. In many cases, however, we have made statements in this offering memorandum regarding our industry and our position in the industry based on our experience in the industry and our own investigation of

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market conditions. We cannot assure you that any of these assumptions are accurate or that our assumptions correctly reflect our position in the industry.

Below is a list of terms that are common to our industry and used throughout this document:

|        |  |
|--------|--|
| /d     | = per day  |
| Bbl    | = barrels  |
| BBtu   | = billion British thermal units                  |
| BBtue  | = billion British thermal unit equivalents       |
| Bcf    | = billion cubic feet                             |
| Bcfe   | = billion cubic feet of natural gas equivalents  |
| MBbls  | = thousand barrels                               |
| Mcf    | = thousand cubic feet                            |
| MDth   | = thousand dekatherms                            |
| Mcfe   | = thousand cubic feet of natural gas equivalents |
| Mgal   | = thousand gallons                               |
| MMBbls | = million barrels                                |
| MMBtu  | = million British thermal units                  |
| MMcf   | = million cubic feet                             |
| MMcfe  | = million cubic feet of natural gas equivalents  |
| MMWh   | = thousand megawatt hours                        |
| MTons  | = thousand tons                                  |
| MW     | = megawatt                                       |
| TBtu   | = trillion British thermal units                 |
| Tcfe   | = trillion cubic feet of natural gas equivalents |

When we refer to natural gas and oil in equivalents, we are doing so to compare quantities of oil with quantities of natural gas or to express these different commodities in a common unit. In calculating equivalents, we use a generally recognized standard in which one Bbl of oil is equal to six Mcf of natural gas. Also, when we refer to cubic feet measurements, all measurements are at a pressure of 14.73 pounds per square inch.

When we refer to us, we, our, ours or El Paso, we are describing El Paso Corporation and/or our subsidiaries.

#### **NON-GAAP FINANCIAL MEASURES**

Our management uses EBIT to assess the operating results and effectiveness of our business segments. EBIT and the related ratios presented in this offering memorandum are supplemental measures of our performance that are not required by, or recognized as being in accordance with, GAAP. EBIT should not be considered as an alternative to net income, operating income or any other performance measures derived in accordance with GAAP or as an alternative to cash flow from operating activities as a measure of our operating liquidity. For a reconciliation of our EBIT (by segment) to our consolidated net loss for each of the three years ended December 31, 2004, see Management's Discussion and Analysis of Financial Condition and Results of Operations—Results of Operations.

We define EBIT as net income (loss) adjusted for (1) items that do not impact our income (loss) from continuing operations, such as extraordinary items, discontinued operations and the impact of accounting changes, (2) income taxes, (3) interest and debt expense and (4) distributions on preferred interests of consolidated subsidiaries. Our businesses consist of consolidated operations as well as investments in unconsolidated affiliates. We exclude interest and debt expense and distributions on preferred interests of consolidated subsidiaries from this measure so that investors may evaluate our operating results independently.

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from our financing methods or capital structure. We believe that EBIT is helpful to our investors because it allows them to more effectively evaluate the operating performance of our consolidated businesses and our unconsolidated investments using the same performance measure analyzed internally by our management. EBIT may not be comparable to measurements used by other companies. Additionally, EBIT should be considered in conjunction with net income and other performance measures such as operating income or operating cash flow.

**WHERE YOU CAN FIND MORE INFORMATION**

We file annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy reports, statements or other information we file at the SEC's public reference room at 450 Fifth Street, N.W., Washington, D.C., 20549. Please call the SEC at 1-800-SEC-0330 for further information on the operation of public reference room. Our SEC filings are also available to the public through the web site maintained by the SEC at <http://www.sec.gov>.

This prospectus is part of a registration statement on Form S-1 that we have filed with the SEC. As allowed by SEC rules, this prospectus does not contain all the information you can find in the registration statement or the exhibits filed with the registration statement. Whenever a reference is made in this prospectus to an agreement or other document of El Paso, be aware that such reference is not necessarily complete and that you should refer to the exhibits that are filed with the registration statement for a copy of the agreement or other document. You may review a copy of the registration statement at the SEC's public reference room in Washington, D.C., as well as through the SEC's website as described above. You may also obtain any of the documents referenced in this prospectus from us free of charge, excluding any exhibits to those documents unless the exhibit is specifically incorporated by reference as an exhibit in this prospectus, by requesting them in writing or by telephone from us at the following address:

El Paso Corporation  
Office of Investor Relations  
El Paso Building  
1001 Louisiana Street  
Houston, Texas 77002  
Telephone No.: (713) 420-2600

You should read this prospectus and any prospectus supplement together with the registration statement and the exhibits filed with the registration statement. The information contained in this prospectus speaks only as of its date unless the context specifically indicates otherwise.

We have not authorized any person to give any information or to make any representation that differs from, or add to, the information discussed in this prospectus. Therefore, if anyone gives you different or additional information, you should not rely on it.

**CAUTIONARY STATEMENT REGARDING  
FORWARD-LOOKING STATEMENTS**

This prospectus includes statements that constitute forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. These statements are subject to risks and uncertainties. Forward-looking statements include information concerning possible or assumed future results of operations of us and our affiliates. These statements may relate to, but are not limited to, information or assumptions about earnings per share, capital and other expenditures, dividends, financing plans, capital structure, cash flow, liquidity, pending legal and regulatory proceedings and claims, including environmental matters, future economic performance, operating income, cost savings, management's plans, goals and objectives for future operations and growth. These forward-looking statements generally are accompanied by words such as intend, anticipate, believe, estimate, expect, should or similar expressions. It should be understood that these forward-looking statements are necessarily estimates reflecting the best judgment of our senior management, not guarantees of future performance. They are subject to a number of

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assumptions, risks and uncertainties that could cause actual results to differ materially from those expressed or implied in the forward-looking statements.

Undue reliance should not be placed on forward-looking statements, which speak only as of the date of this prospectus.

For a description of risks relating to us and our business, see **Risk Factors** beginning on page 6 of this prospectus.

All subsequent written and oral forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section and any other cautionary statements that may accompany such forward-looking statements. We do not undertake any obligation to release publicly any revisions to these forward-looking statements to reflect events or circumstances after the date of this document or to reflect the occurrence of unanticipated events, unless the securities laws require us to do so.

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**SUMMARY**

*This summary highlights some basic information from this prospectus to help you understand our business, the purchase contracts and the common stock issuable upon settlement thereof. It does not contain all of the information that is important to you. You should carefully read this prospectus to understand fully the terms of the common stock subject to issuance upon settlement of the purchase contracts, as well as the other considerations that are important to you in making your investment decision. You should pay special attention to the Risk Factors beginning on page 6 of this prospectus and the section entitled Cautionary Statement Regarding Forward-Looking Statements on page iii of this prospectus. For purposes of this prospectus, except where we are describing the terms of the ESUs, purchase contracts and the common stock subject to issuance upon settlement thereof, and unless the context otherwise indicates, when we refer to El Paso, us, we, our, or issuer, we are describing El Paso Corporation, together with its subsidiaries. With respect to any description of the terms of the common stock subject to issuance upon settlement of the purchase contracts, such references refer only to El Paso Corporation, and not to its subsidiaries.*

**Our Business**

We are an energy company originally founded in 1928 in El Paso, Texas. Our business purpose is to provide natural gas and related energy products in a safe, efficient and dependable manner. We own North America's largest natural gas pipeline system and are a large independent natural gas producer. We also own and operate an energy marketing and trading business, a power business, midstream assets and investments, and have an investment in a small telecommunications business. Our power business primarily consists of international assets.

Since the end of 2001, our business activities have largely been focused on maintaining our core businesses of pipelines and production, while attempting to liquidate or otherwise divest of those businesses and operations that were not core to our long-term objectives, or that were not performing consistently with the expectations we had for them at the time we made the investment. Our overall objective during this period has been to reduce debt and improve liquidity, while at the same time investing in our core business activities. Our actions during this period have significantly impacted our financial condition, with the sale of almost \$10 billion of operating assets. These actions have also produced significant financial losses through asset impairments, realized losses on asset sales and diminishment of income producing potential on businesses sold.

In late 2003 and early 2004, we appointed a new chief executive officer and several new members of the executive management team. Following a period of assessment, we announced that our long-term business strategy would principally focus on our core pipeline and production businesses. Our businesses are owned through a complex legal structure of companies that reflect the acquisitions and growth in our business from 1996 to 2001. As part of our long range strategy, we are actively working to reduce the complexity of our corporate structure. See our ownership structure chart on page 70.

We believe that 2004 was a watershed year for us. We were able to meet and exceed a number of the goals established under our 2003 Long Range Plan. As part of our efforts in 2004:

We focused capital investment on our core pipeline and production businesses, where in 2002, 2003 and 2004, we spent 87 percent, 91 percent, and 97 percent of our total capital dollars;

We completed the sale of a number of assets and investments including international production properties, a substantial portion of our general and limited partnership interests in GulfTerra Energy Partners, L.P., a publicly traded limited partnership, a significant portion of our worldwide petroleum markets operations, a significant portion of our domestic power generation operations and our merchant LNG business. Total proceeds from these sales were approximately \$3.3 billion;

We reduced our net debt (debt, net of cash) by \$3.4 billion in 2004, lowering our net debt to \$17.1 billion (debt of \$19.2 billion, less cash and cash equivalents of \$2.1 billion) as of December 31, 2004; and

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We continued our cost-reduction efforts with a goal of achieving \$150 million of savings by the end of 2006.

In 2004 we focused on expanding our pipeline operations and beginning the turnaround of our production business. During the year, we completed major expansions in our pipeline operations, including our Cheyenne Plains project, to provide transmission outlets for natural gas supply in the Rocky Mountains, and we are moving forward on our Seafarer and Cypress projects to fulfill demand for natural gas in the southeastern United States, primarily Florida. Additionally, we continue to work in recontracting capacity on our systems and have been successful to date in these efforts. In our production operations, we instituted a new, more rigorous, risk analysis process which emphasizes strict capital discipline. Over the second half of 2004, this process resulted in a shifting of capital to areas with higher returns and improved drilling results and helped us to begin the stabilization of our domestic production. In addition, we have recently made several strategic acquisitions of production properties in Texas and acquired the interests held by one of the third parties under our net profits interest agreements.

In 2005, we will continue to work to achieve our long-range goals by:

Simplifying our capital structure;

Continuing to focus on expansions in our core pipeline business and completing the turnaround of our production business;

Selling additional assets that we expect will generate proceeds from \$1.8 billion to \$2.2 billion;

Reducing outstanding debt (net of cash) to \$15 billion by the end of 2005; and

Continuing to reduce costs to achieve the cost savings outlined in our Long Range Plan.

For a further description of our business, see the information set forth under the caption **Business** that begins on page 70 of this prospectus.

**The Offering and this Prospectus**

This prospectus relates to the shares of our common stock to be issued upon the maturity on August 16, 2005 or early settlement of the purchase contracts originally issued in connection with our public offering of ESUs on June 26, 2002. The number of shares of our common stock issuable upon settlement of the purchase contract will be (1) 2.0886 shares per purchase contract in the case of early settlement, subject to adjustment upon specified events, or (2) in the case of shares issuable upon maturity of the purchase contracts, will depend on the prior consecutive 20-trading day average closing price of our common stock determined on the third trading day immediately prior to August 16, 2005. The settlement rate will range from 2.0886 shares to 2.5063 shares per purchase contract with the actual rate to be determined based on such average price, subject to adjustment upon specified events. Accordingly, we will issue a minimum of approximately 12 million shares and up to a maximum of approximately 15.2 million shares on the settlement date of the purchase contracts, depending on our average stock price. The aggregate purchase price payable to us under the 5,442,047 ESUs that remain outstanding is approximately \$272.1 million (a purchase price of \$50 is payable in respect of the purchase contract under each ESU). For a further description of the ESUs, the purchase contracts constituting a portion thereof and our common stock, see the information set forth under the captions **Description of the Equity Security Units** and **Description of El Paso Capital Stock** elsewhere in this prospectus. We intend to use the net proceeds from the issuance of our shares of common stock upon maturity of the purchase contracts for general corporate purposes. See **Use of Proceeds**.

This prospectus is part of a post-effective amendment to a registration statement filed with the SEC that has been declared effective. This prospectus has been filed with the SEC because under applicable SEC rules we no longer qualify for use of a registration statement on Form S-3 or for incorporation by reference into a prospectus. For a further explanation, see **Explanatory Note** on page i above.

We may be required to amend or supplement this prospectus at any time prior to August 16, 2005 to add, update or change the information contained in this prospectus. This prospectus does not contain all the



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information you can find in the registration statement or the exhibits filed with the registration statement. You should read this prospectus and any amendment or supplement hereto, together with the registration statement, the exhibits filed with or incorporated by reference into the registration statement and the additional information described under Where You Can Find More Information.

**Recent Developments**

***Preferred Stock Offering***

On April 15, 2005, we completed a private placement of 750,000 shares of our 4.99% Convertible Perpetual Preferred Stock (liquidation preference \$1,000 per share). In connection with the private placement, we entered into a purchase agreement, dated as of April 11, 2005, with the initial purchasers of the preferred stock. The initial purchasers resold the preferred stock to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, and the securities are required to be registered later this year. The gross proceeds to us were approximately \$750 million, and the net proceeds (after deducting the initial purchasers' discounts and commissions and our estimated expenses) were approximately \$722 million. We used approximately \$442 million of the net proceeds of the private placement to prepay our Western Energy Settlement obligations. The remaining net proceeds, along with cash on hand, will be used to redeem the outstanding 8.25% Cumulative Preferred Stock of our subsidiary, El Paso Tennessee Pipeline Co., for approximately \$300 million plus accrued and unpaid dividends. In connection with the prepayment of the Western Energy Settlement obligation, we incurred an additional first quarter 2005 charge of approximately \$59 million, before income taxes, (approximately \$39 million net of income taxes), since the obligation will be paid earlier than originally expected.

***Deep-Shelf Discovery***

On April 4, 2005, we reported that one of our subsidiaries, El Paso Production Company, has tested a recent deep-shelf discovery in the Gulf of Mexico. The West Cameron 75 No. 1 well was tested with almost 14,000 pounds per square inch of flowing wellhead pressure and has anticipated deliverability of approximately 40 million cubic feet per day.

***Sale of Interests in Enterprise Products Partners***

On January 14, 2005, we sold our remaining interests in Enterprise Products Partners L.P. (Enterprise) and Enterprise Products GP, LLC, the general partner of Enterprise, to Enterprise for approximately \$425 million. The transaction includes the sale of our 9.9 percent membership interest in the general partner of Enterprise and approximately 13.5 million common units in Enterprise. Below are pro forma effects of this sale on the historical financial statements as of and for the year ended December 31, 2004. The El Paso Historical amounts in the tables below represent our condensed historical consolidated balance sheet and income statement information and were derived from our 2004 Annual Report on Form 10-K, as amended. The pro forma adjustment amounts represent the historical results and balances related to our interests in Enterprise which were accounted for as an equity investment. The pro forma adjusting entries below reflect (1) the receipt of proceeds of \$425 million from the sale of our remaining 9.9 percent interest in the general partner of Enterprise and 13.5 million Enterprise common units; (2) the elimination of the remaining carrying value of our investment in Enterprise of \$257 million and unamortized non-current deferred gains of \$15 million that were recognized at the time of sale; (3) the recording of a deferred income tax liability of \$64 million; and (4) the recording of a \$183 million gain, net of income taxes of \$64 million (assuming a 35 percent tax rate), associated with the sale.

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**EL PASO CORPORATION**  
**UNAUDITED PRO FORMA CONDENSED CONSOLIDATED BALANCE SHEET**  
**As of December 31, 2004**

|  | <b>El Paso<br/>Historical</b> | <b>Pro Forma<br/>Adjustments</b> | <b>Pro Forma</b> |
|--|-------------------------------|----------------------------------|------------------|
|  | <b>(In millions)</b>          |                                  |                  |
| <b>ASSETS</b>  |                               |                                  |                  |
| Current assets   |                               |                                  |                  |
| Cash and cash equivalents                                      | \$ 2,117                      | \$ 425                           | \$ 2,542         |
| Accounts and notes receivable, net                             | 1,709                         |                                  | 1,709            |
| Other  | 1,806                         |                                  | 1,806            |
| Total current assets   | 5,632                         | 425                              | 6,057            |
| Property, plant and equipment, net                             | 18,812                        |                                  | 18,812           |
| Other assets   |                               |                                  |                  |
| Investments in unconsolidated affiliates                       | 2,614                         | (257)                            | 2,357            |
| Other  | 4,325                         |                                  | 4,325            |
| Total assets   | \$ 31,383                     | \$ 168                           | \$ 31,551        |
| <b>LIABILITIES &amp; STOCKHOLDERS EQUITY</b>                   |                               |                                  |                  |
| Current liabilities  |                               |                                  |                  |
| Accounts payable   | \$ 1,556                      |                                  | \$ 1,556         |
| Short-term financing obligations, including current maturities | 955                           |                                  | 955              |
| Other  | 2,061                         |                                  | 2,061            |
| Total current liabilities                                      | 4,572                         |                                  | 4,572            |
| Long-term debt   | 18,241                        |                                  | 18,241           |
| Other liabilities  |                               |                                  |                  |
| Deferred income taxes  | 1,311                         | 64                               | 1,375            |
| Other  | 3,453                         | (15)                             | 3,438            |
| Commitments and contingencies                                  |                               |                                  |                  |
| Securities of subsidiaries                                     | 367                           |                                  | 367              |
| Stockholders equity  |                               |                                  |                  |
| Common stock   | 1,953                         |                                  | 1,953            |
| Additional paid-in capital                                     | 4,538                         |                                  | 4,538            |
| Accumulated deficit  | (2,855)                       | 119                              | (2,736)          |
| Other  | (197)                         |                                  | (197)            |
| Total stockholders equity                                      | 3,439                         | 119                              | 3,558            |

|   |           |        |           |
|---|-----------|--------|-----------|
| Total liabilities & stockholders equity | \$ 31,383 | \$ 168 | \$ 31,551 |
|---|-----------|--------|-----------|

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**EL PASO CORPORATION**  
**UNAUDITED PRO FORMA CONDENSED CONSOLIDATED STATEMENT OF INCOME**  
**For the Year Ended December 31, 2004**

|  | <b>El Paso<br/>Historical</b> | <b>Pro Forma<br/>Adjustments</b> | <b>Pro Forma</b> |
|--|-------------------------------|----------------------------------|------------------|
|  | <b>(In millions)</b>          |                                  |                  |
| Operating revenues   | \$ 5,874                      | \$                               | \$ 5,874         |
| Operating expenses   |                               |                                  |                  |
| Cost of products and services                                      | 1,363                         |                                  | 1,363            |
| Operation and maintenance  | 1,872                         |                                  | 1,872            |
| Depreciation, depletion and amortization                           | 1,088                         |                                  | 1,088            |
| Loss on long-lived assets  | 1,092                         |                                  | 1,092            |
| Taxes, other than income taxes                                     | 253                           |                                  | 253              |
|  | 5,668                         |                                  | 5,668            |
| Operating income   | 206                           |                                  | 206              |
| Earnings from unconsolidated affiliates                            | 559                           | (6)                              | 553              |
| Other income, net  | 90                            |                                  | 90               |
| Interest and debt expense  | (1,607)                       |                                  | (1,607)          |
| Distributions on preferred interests of consolidated subsidiaries  | (25)                          |                                  | (25)             |
| Loss before income taxes   | (777)                         | (6)                              | (783)            |
| Income taxes   | 25                            | 2                                | 27               |
| Loss from continuing operations                                    | \$ (802)                      | \$ (4)                           | \$ (806)         |
| Basic and diluted loss per common share from continuing operations | \$ (1.25)                     | \$ (0.01)                        | \$ (1.26)        |
| Basic and diluted average common shares outstanding                | 639                           |                                  | 639              |

**Risk Factors**

**An investment in our common stock involves risks that a potential investor should carefully evaluate prior to making an investment in the common stock. See Risk Factors beginning on page 6.**

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**RISK FACTORS**

*Before you invest in our common stock, you should consider the risks, uncertainties and factors that may adversely affect us that are discussed below.*

**Risks Related to Our Business**

***Our operations are subject to operational hazards and uninsured risks.***

Our operations are subject to the inherent risks normally associated with those operations, including pipeline ruptures, explosions, pollution, release of toxic substances, fires and adverse weather conditions, and other hazards, each of which could result in damage to or destruction of our facilities or damages to persons and property. In addition, our operations face possible risks associated with acts of aggression on our domestic and foreign assets. If any of these events were to occur, we could suffer substantial losses.

While we maintain insurance against many of these risks to the extent and in amounts that we believe are reasonable, our financial condition and operations could be adversely affected if a significant event occurs that is not fully covered by insurance.

***The success of our pipeline business depends, in part, on factors beyond our control.***

Most of the natural gas and natural gas liquids we transport and store are owned by third parties. As a result, the volume of natural gas and natural gas liquids involved in these activities depends on the actions of those third parties, and is beyond our control. Further, the following factors, most of which are beyond our control, may unfavorably impact our ability to maintain or increase current throughput, to renegotiate existing contracts as they expire, or to remarket unsubscribed capacity on our pipeline systems:

service area competition;

expiration and/or turn back of significant contracts;

changes in regulation and action of regulatory bodies;

future weather conditions;

price competition;

drilling activity and availability of natural gas supplies;

decreased availability of conventional gas supply sources and the availability and timing of other gas supply sources, such as LNG;

increased availability or popularity of alternative energy sources such as hydroelectric power;

increased cost of capital;

opposition to energy infrastructure development, especially in environmentally sensitive areas;

adverse general economic conditions;

expiration and/or renewal of existing interests in real property, including real property on Native American lands, and

unfavorable movements in natural gas and liquids prices.

***The revenues of our pipeline businesses are generated under contracts that must be renegotiated periodically.***

Substantially all of our pipeline subsidiaries' revenues are generated under contracts which expire periodically and must be renegotiated and extended or replaced. We cannot assure you that we will be able to extend or replace these contracts when they expire or that the terms of any renegotiated contracts will be as favorable as the existing contracts.

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In particular, our ability to extend and/or replace contracts could be adversely affected by factors we cannot control, including:

competition by other pipelines, including the proposed construction by other companies of additional pipeline capacity or LNG terminals in markets served by our interstate pipelines;

changes in state regulation of local distribution companies, which may cause them to negotiate short-term contracts or turn back their capacity when their contracts expire;

reduced demand and market conditions in the areas we serve;

the availability of alternative energy sources or gas supply points; and

regulatory actions.

If we are unable to renew, extend or replace these contracts or if we renew them on less favorable terms, we may suffer a material reduction in our revenues, earnings and cash flows.

***Fluctuations in energy commodity prices could adversely affect our pipeline businesses.***

Revenues generated by our transmission, storage, and processing contracts depend on volumes and rates, both of which can be affected by the prices of natural gas and natural gas liquids. Increased prices could result in a reduction of the volumes transported by our customers, such as power companies who, depending on the price of fuel, may not dispatch gas-fired power plants. Increased prices could also result from industrial plant shutdowns or load losses to competitive fuels as well as local distribution companies' loss of customer base. We also experience earnings volatility when the amount of gas utilized in operations differs from amounts we receive for that purpose. The success of our transmission, storage and processing operations is subject to continued development of additional oil and natural gas reserves and our ability to access additional suppliers from interconnecting pipelines to offset the natural decline from existing wells connected to our systems. A decline in energy prices could precipitate a decrease in these development activities and could cause a decrease in the volume of reserves available for transmission, storage and processing through our systems or facilities. We retain a fixed percentage of natural gas transported for use as fuel and to replace lost and unaccounted for gas, and we are at risk for the difference between the retained amount and actual gas consumed or lost and unaccounted. Pricing volatility may also impact the value of under or over recoveries of this retained gas. If natural gas prices in the supply basins connected to our pipeline systems are higher on a delivered basis to our off-system markets than delivered prices from other natural gas producing regions, our ability to compete with other transporters may be negatively impacted. Fluctuations in energy prices are caused by a number of factors, including:

regional, domestic and international supply and demand;

availability and adequacy of transportation facilities;

energy legislation;

federal and state taxes, if any, on the sale or transportation of natural gas and natural gas liquids;

abundance of supplies of alternative energy sources; and

political unrest among oil producing countries.

***Natural gas and oil prices are volatile. A substantial decrease in natural gas and oil prices could adversely affect the financial results of our exploration and production business.***

Our future financial condition, revenues, results of operations, cash flows and future rate of growth depend primarily upon the prices we receive for our natural gas and oil production. Natural gas and oil prices historically have

been volatile and are likely to continue to be volatile in the future, especially given current

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world geopolitical conditions. The prices for natural gas and oil are subject to a variety of additional factors that are beyond our control. These factors include:

the level of consumer demand for, and the supply of, natural gas and oil;

commodity processing, gathering and transportation availability;

the level of imports of, and the price of, foreign natural gas and oil;

the ability of the members of the Organization of Petroleum Exporting Countries to agree to and maintain oil price and production controls;

domestic governmental regulations and taxes;

the price and availability of alternative fuel sources;

the availability of pipeline capacity;

weather conditions;

market uncertainty;

political conditions or hostilities in natural gas and oil producing regions;

worldwide economic conditions; and

decreased demand for the use of natural gas and oil because of market concerns about global warming or changes in governmental policies and regulations due to climate change initiatives.

Further, because approximately 82 percent of our proved reserves at December 31, 2004 were natural gas reserves, we are substantially more sensitive to changes in natural gas prices than we are to changes in oil prices. Declines in natural gas and oil prices would not only reduce revenue, but could reduce the amount of natural gas and oil that we can produce economically and, as a result, could adversely affect the financial results of our production business. Changes in natural gas and oil prices can have a significant impact on the calculation of our full cost ceiling test. A significant decline in natural gas and oil prices could result in a downward revision of our reserves and a write-down of the carrying value of our natural gas and oil properties, which could be substantial, and would negatively impact our net income and stockholders' equity.

***The success of our natural gas and oil exploration and production businesses is dependent, in part, on factors that are beyond our control.***

In addition to prices, the performance of our natural gas and oil exploration and production businesses is dependent, in part, upon a number of factors that we cannot control, including:

the results of future drilling activity;

our ability to identify and precisely locate prospective geologic structures and to drill and successfully complete wells in those structures in a timely manner;

our ability to expand our leased land positions in desirable areas, which often are subject to intensely competitive conditions;

increased competition in the search for and acquisition of reserves;

future drilling, production and development costs, including drilling rig rates and oil field services costs;

future tax policies, rates, and drilling or production incentives by state, federal, or foreign governments;

increased federal or state regulations, including environmental regulations, that limit or restrict the ability to drill natural gas or oil wells, reduce operational flexibility, or increase capital and operating costs;

decreased demand for the use of natural gas and oil because of market concerns about global warming or changes in governmental policies and regulations due to climate change initiatives;

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declines in production volumes, including those from the Gulf of Mexico; and

continued access to sufficient capital to fund drilling programs to develop and replace a reserve base with rapid depletion characteristics.

***Our natural gas and oil drilling and producing operations involve many risks and may not be profitable.***

Our operations are subject to all the risks normally incident to the operation and development of natural gas and oil properties and the drilling of natural gas and oil wells, including well blowouts, cratering and explosions, pipe failure, fires, formations with abnormal pressures, uncontrollable flows of natural gas, oil, brine or well fluids, release of contaminants into the environment and other environmental hazards and risks. The nature of the risks is such that some liabilities could exceed our insurance policy limits, or, as in the case of environmental fines and penalties, cannot be insured. As a result, we could incur substantial costs that could adversely affect our future results of operations, cash flows or financial condition.

In addition, in our drilling operations we are subject to the risk that we will not encounter commercially productive reservoirs. New wells drilled by us may not be productive, or we may not recover all or any portion of our investment in those wells. Drilling for natural gas and oil can be unprofitable, not only because of dry holes but wells that are productive may not produce sufficient net reserves to return a profit at then realized prices after deducting drilling, operating and other costs.

***Estimating our reserves, production and future net cash flow is difficult.***

Estimating quantities of proved natural gas and oil reserves is a complex process that involves significant interpretations and assumptions. It requires interpretations of available technical data and various estimates, including estimates based upon assumptions relating to economic factors, such as future commodity prices, production costs, severance and excise taxes, capital expenditures and workover and remedial costs, and the assumed effect of governmental regulation. As a result, our reserve estimates are inherently imprecise. Also, the use of a 10 percent discount factor for estimating the value of our reserves, as prescribed by the SEC, may not necessarily represent the most appropriate discount factor, given actual interest rates and risks to which our production business or the natural gas and oil industry, in general, are subject. Any significant variations from the interpretations or assumptions used in our estimates or changes of conditions could cause the estimated quantities and net present value of our reserves to differ materially.

Our reserve data represents an estimate. You should not assume that the present values referred to in this report represent the current market value of our estimated natural gas and oil reserves. The timing of the production and the expenses from development and production of natural gas and oil properties will affect both the timing of actual future net cash flows from our proved reserves and their present value. Changes in the present value of these reserves could cause a write-down in the carrying value of our natural gas and oil properties, which could be substantial, and would negatively affect our net income and stockholders' equity.

As of December 31, 2004, approximately 29 percent of our estimated proved reserves were undeveloped. Recovery of undeveloped reserves requires significant capital expenditures and successful drilling operations. The reserve data assumes that we can and will make these expenditures and conduct these operations successfully, but future events, including commodity price changes, may cause these assumptions to change. In addition, estimates of proved undeveloped reserves and proved but non-producing reserves are subject to greater uncertainties than estimates of proved producing reserves.

***The success of our power activities depends, in part, on many factors beyond our control.***

The success of our remaining domestic and international power projects could be adversely affected by factors beyond our control, including:

alternative sources and supplies of energy becoming available due to new technologies and interest in self generation and cogeneration;

increases in the costs of generation, including increases in fuel costs;

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uncertain regulatory conditions resulting from the ongoing deregulation of the electric industry in the United States and in foreign jurisdictions;

our ability to negotiate successfully, and enter into advantageous power purchase and supply agreements;

the possibility of a reduction in the projected rate of growth in electricity usage as a result of factors such as regional economic conditions, excessive reserve margins and the implementation of conservation programs;

risks incidental to the operation and maintenance of power generation facilities;

the inability of customers to pay amounts owed under power purchase agreements;

the increasing price volatility due to deregulation and changes in commodity trading practices; and

over-capacity of generation in markets served by the power plants we own or in which we have an interest.

***Our use of derivative financial instruments could result in financial losses.***

Some of our subsidiaries use futures, swaps and option contracts traded on the New York Mercantile Exchange, over-the-counter options and price and basis swaps with other natural gas merchants and financial institutions. To the extent we have positions that are not designated or qualify as hedges, changes in commodity prices, interest rates, volatility, correlation factors, the liquidity of the market could cause our revenues, net income and cash requirements to be volatile.

We could incur financial losses in the future as a result of volatility in the market values of the energy commodities we trade, or if one of our counterparties fails to perform under a contract. The valuation of these financial instruments involves estimates. Changes in the assumptions underlying these estimates can occur, changing our valuation of these instruments and potentially resulting in financial losses. To the extent we hedge our commodity price exposure and interest rate exposure, we forego the benefits we would otherwise experience if commodity prices were to increase, or interest rates were to change. The use of derivatives also requires the posting of cash collateral with our counterparties which can impact our working capital (current assets and liabilities) when commodity prices or interest rates change. For additional information concerning our derivative financial instruments, see Management Discussion and Analysis of Financial Condition and Results of Operations Quantitative and Qualitative Disclosures About Market Risk and note 10 to our Consolidated Financial Statements.

***Our businesses are subject to the risk of payment defaults by our counterparties.***

We frequently extend credit to our counterparties following the performance of credit analysis. Despite performing this analysis, we are exposed to the risk that we may not be able to collect amounts owed to us. Although in many cases we have collateral to secure the counterparty's performance, it could be inadequate and we could suffer credit losses.

***Our foreign operations and investments involve special risks.***

Our activities in areas outside the United States, including material investment exposure in our power, pipeline and production projects in Brazil and Pakistan, are subject to the risks inherent in foreign operations, including: loss of revenue, property and equipment as a result of hazards such as expropriation, nationalization, wars, insurrection and other political risks;

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the effects of currency fluctuations and exchange controls, such as devaluation of foreign currencies and other economic problems; and

changes in laws, regulations and policies of foreign governments, including those associated with changes in the governing parties.

### ***Retained liabilities associated with businesses that we have sold could exceed our estimates.***

We have sold a significant number of assets over the years, including the sale of many assets since 2001. Pursuant to various purchase and sale agreements relating to businesses and assets that we have divested, we have either retained certain liabilities or indemnified certain purchasers against liabilities that they might incur in the future. These liabilities in many cases relate to breaches of warranties, environmental, tax, litigation, personal injury and other representations that we have provided. Although we believe that we have established appropriate reserves for these liabilities, we could be required to accrue additional reserves in the future and these amounts could be material. In addition, as we exit businesses, we have experienced substantial reductions and turnover in our workforce that previously supported the ownership and operation of such assets. There is the risk that such reductions and turnover in our workforce could result in errors or mistakes in managing the businesses that we are exiting prior to closing. There is also the risk that such reductions could result in errors or mistakes in managing the retained liabilities after closing, including the lack of any historical knowledge with regard to such assets and businesses in managing the liabilities or defending any associated litigation.

### **Risks Related to Legal and Regulatory Matters**

#### ***Ongoing litigation and investigations related to our financial statements associated with our reserve estimates and hedges could significantly adversely affect our business.***

In 2004, we restated our historical financial statements as a result of a downward revision of our natural gas and oil reserves and because of the manner in which we applied the accounting rules related to many of our historical hedges, primarily those associated with hedges of our anticipated natural gas production. As a result of this reduction in reserve estimates, several class action lawsuits were filed against us and several of our subsidiaries. The reserve revisions are also the subject of investigations by the SEC and the U.S. Attorney and the hedging matters are also the subject of an investigation by the U.S. Attorney and may become the subject of a separate inquiry by the SEC, any of which could result in significant fines against us. These investigations and lawsuits, and possible future claims based on these same facts, may further negatively impact our credit ratings and place further demands on our liquidity. We cannot provide assurance at this time that the effects and results of these or other investigations or of the class action lawsuits will not be material to our financial conditions, results of operations and liquidity.

#### ***The agencies that regulate our pipeline businesses and their customers affect our profitability.***

Our pipeline businesses are regulated by the FERC, the U.S. Department of Transportation, and various state and local regulatory agencies. Regulatory actions taken by those agencies have the potential to adversely affect our profitability. In particular, the FERC regulates the rates our pipelines are permitted to charge their customers for their services. In setting authorized rates of return in a few recent FERC decisions, the FERC has utilized a proxy group of companies that includes local distribution companies that are not faced with as much competition or risks as interstate pipelines. The inclusion of these companies creates downward pressure on approved tariff rates. If our pipelines' tariff rates were reduced in a future proceeding, if our pipelines' volume of business under their currently permitted rates was decreased significantly, or if our pipelines were required to substantially discount the rates for their services because of competition or because of regulatory pressure, the profitability of our pipeline businesses could be reduced.

In addition, increased regulatory requirements relating to the integrity of our pipelines requires additional spending in order to maintain compliance with these requirements. Any additional requirements that are enacted could significantly increase the amount of these expenditures.

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Further, state agencies that regulate our pipelines local distribution company customers could impose requirements that could impact demand for our pipelines services.

***Costs of environmental liabilities, regulations and litigation could exceed our estimates.***

Our operations are subject to various environmental laws and regulations. These laws and regulations obligate us to install and maintain pollution controls and to clean up various sites at which regulated materials may have been disposed of or released. Some of these sites have been designated as Superfund sites by the EPA under the Comprehensive Environmental Response, Compensation and Liability Act. We are also party to legal proceedings involving environmental matters pending in various courts and agencies, including matters relating to methyl butyl ether found in water supplies and the clean up of, or exposure to, hazardous substances.

Compliance with environmental laws and regulations can require significant costs, such as costs of installing and maintaining pollution controls and clean-up and damages, including natural resources damages, arising out of contaminated properties, and the failure to comply with environmental laws and regulations may result in fines and penalties being imposed. It is not possible for us to estimate reliably the amount and timing of all future expenditures related to environmental matters because of:

the uncertainties in estimating pollution control and clean up costs;

the discovery of new sites or information;

the uncertainty in quantifying liability under environmental laws that impose joint and several liability on all potentially responsible parties;

the nature of environmental laws and regulations; and

potential changes in environmental laws and regulations, including changes in the interpretation and enforcement thereof.

Although we believe we have established appropriate reserves for liabilities, including clean up costs, we could be required to set aside additional reserves in the future due to these uncertainties, and these amounts could be material. For additional information concerning our environmental matters, see Business Legal Proceedings, and note 17 to our Consolidated Financial Statements.

***Costs of litigation matters and other contingencies could exceed our estimates.***

We are involved in various lawsuits in which we or our subsidiaries have been sued. We also have other contingent liabilities and exposures. Although we believe we have established appropriate reserves for these liabilities, we could be required to set aside additional reserves in the future and these amounts could be material. For additional information concerning our litigation matters and other contingent liabilities, see note 17 to our Consolidated Financial Statements.

***Our system of internal controls ensure the accuracy or completeness of our disclosures and a loss of public confidence in the quality of our internal controls or disclosures could have a negative impact on us.***

Section 404 of the Sarbanes-Oxley Act of 2002, requires us to provide an annual report on our internal controls over financial reporting, including an assessment as to whether or not our internal controls over financial reporting are effective. We are also required to have our auditors attest to our assessment and to opine on the effectiveness of our internal controls over financial reporting. Based upon such review, we concluded that as of December 31, 2004 we did not maintain effective internal control over financial reporting. We identified several deficiencies in internal control over financial reporting that management has concluded constitute material weaknesses. Although we have taken steps to remediate some of these deficiencies, additional steps must be taken to remediate the remaining control deficiencies. If we are unable to remediate our identified internal control deficiencies over financial reporting by the end of 2005, or we identify additional deficiencies in our internal controls over financial reporting, we could be subjected to additional regulatory



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scrutiny, future delays in filing our financial statements and suffer a loss of public confidence in the reliability of our financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles, which could have a negative impact on our liquidity, access to capital markets, financial condition and the market value of our common stock.

In addition to the risk of not completing the remediation of all deficiencies in our internal controls over financial reporting, we do not expect that our disclosure controls and procedures or our internal controls over financial reporting will prevent all mistakes, errors and fraud. Any system of internal controls, no matter how well designed or implemented, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. The design of a control system must reflect the fact that the benefits of controls must be considered relative to their costs. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Therefore, any system of internal controls is subject to inherent limitations, including the possibility that controls may be circumvented or overridden, that judgments in decision-making can be faulty, and that misstatements due to mistakes, errors or fraud may occur and may not be detected. Also, while we document our assumptions and review financial disclosures with the Audit Committee of our Board of Directors, the regulations and literature governing our disclosures are complex and reasonable persons may disagree as to their application to a particular situation or set of facts. In addition, the applicable regulations and literature are relatively new. As a result, they are potentially subject to change in the future, which could include changes in the interpretation of the existing regulations and literature as well as the issuance of more detailed rules and procedures.

**Risks Related to Our Liquidity**

***We have significant debt and below investment grade credit ratings, which have impacted and will continue to impact our financial condition, results of operations and liquidity.***

We have significant debt of approximately \$19 billion as of December 31, 2004 and have significant debt service and debt maturity obligations. The ratings assigned to our senior unsecured indebtedness are below investment grade, currently rated Caa1 by Moody's Investor Service (Moody's) and CCC+ by Standard & Poor's. These ratings have increased our cost of capital and our operating costs, particularly in our trading operations, and could impede our access to capital markets. Moreover, we must retain greater liquidity levels to operate our business than if we had investment grade credit ratings. Our debt maturities as of December 31, 2004 for 2005, 2006 and 2007 are \$948 million, \$1,155 million and \$835 million, respectively. If our ability to generate or access capital becomes significantly restrained, our financial condition and future results of operations could be significantly adversely affected. See note 15 to our Consolidated Financial Statements, for a further discussion of our debt.

***We may not achieve all of the objectives set forth in our Long-Range Plan in a timely manner or at all.***

Our ability to achieve the objectives of our Long-Range Plan, as well as the timing of their achievement, if at all, is subject, in part, to factors beyond our control. These factors include (1) our ability to raise cash from asset sales, which may be impacted by our ability to locate potential buyers in a timely fashion and obtain a reasonable price, (2) our ability to manage our working capital, (3) our ability to generate additional cash by improving the performance of our pipeline and production operations, (4) our ability to exit the power and trading businesses in the manner and within the time period we expect, (5) our ability to significantly reduce debt, and (6) our ability to preserve sufficient cash flow to service our debt and other obligations. If we fail to achieve in a timely manner the targets of our Long-Range Plan, our liquidity or financial position could be materially adversely affected. In addition, it is possible that any of the asset sales contemplated by our Long-Range Plan could be at prices that are below our current book value for the assets, which could result in losses that could be substantial.

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***A breach of the covenants applicable to our debt and other financing obligations could affect our ability to borrow funds and could accelerate our debt and other financing obligations and those of our subsidiaries.***

Our debt and other financing obligations contain restrictive covenants and cross-acceleration provisions, which become more restrictive over time. A breach of any of these covenants could preclude us or our subsidiaries from issuing letters of credit and from borrowing under our \$3 billion credit agreement, and could accelerate our long-term debt and other financing obligations and those of our subsidiaries. If this were to occur, we may not be able to repay such debt and other financing obligations upon such acceleration.

Our \$3 billion credit agreement is collateralized by our equity interests in Tennessee Gas Pipeline Company, ANR Pipeline Company, El Paso Natural Gas Company, Colorado Interstate Gas Company, Wyoming Interstate Company Ltd., Southern Gas Storage Company and ANR Storage Company. A breach of the covenants under the \$3 billion agreement could permit the lender to exercise their rights to the collateral, and we could be required to liquidate these interests.

***Our ability to access capital markets is limited to private placements or filing new registration statements as a result of the restatement of our historical financial results.***

In 2004, we restated our historical financial statements as a result of a downward revision of our natural gas and oil reserves and because of the manner in which we applied the accounting rules related to our hedges of our natural gas production and certain other derivatives. As a result of the time required to complete these revisions, our 2003 Form 10-K and our 2004 Forms 10-Q were not filed in a timely manner. As a result, until January 2006, our ability to access approximately \$926 million of capacity under our existing shelf registration statement without filing additional disclosure information with the SEC is restricted. The additional disclosure requirements, and any related review by the SEC, could be expensive and impede our ability to access capital in a timely fashion. If our ability to access capital becomes significantly restrained, our financial condition and future results of operations could be significantly adversely affected.

***We are subject to financing and interest rate exposure risks.***

Our future success depends on our ability to access capital markets and obtain financing at cost effective rates. Our ability to access financial markets and obtain cost-effective rates in the future are dependent on a number of factors, many of which we cannot control, including changes in:

our credit ratings;

interest rates;

the structured and commercial financial markets;

market perceptions of us or the natural gas and energy industry;

changes in tax rates due to new tax laws;

our stock price; and

changes in market prices for energy.

**Risks Related to Our Common Stock**

***You will bear the entire risk of a decline in the price of our common stock.***

The market value of the shares of our common stock you will receive on the stock purchase date may be materially different from the effective price per share paid by you on the settlement date under the applicable purchase contracts. If the average trading price of our common stock on the settlement date under the applicable purchase contracts is less than \$19.95 per share, you will, on the settlement date, be required to purchase shares of common stock at a loss. Accordingly, a holder of ESUs assumes the entire risk that the market value of our common stock may decline. Any such decline could be substantial.



**Table of Contents*****You will receive only a portion of any appreciation in our common stock price.***

The aggregate market value of the shares of our common stock you will receive on the settlement date under the applicable purchase contracts generally will exceed the stated amount of \$50 only if the average closing price per share of our common stock over the applicable 20-trading day period preceding settlement equals or exceeds \$23.94, which we refer to as the threshold appreciation price. Therefore, during the period prior to the settlement date, an investment in the ESUs affords less opportunity for equity appreciation than a direct investment in our common stock. If the average closing price of our common stock exceeds \$19.95, which we refer to as the reference price, but falls below the threshold appreciation price, you will realize no equity appreciation on the common stock for the period during which you own the purchase contract.

***The trading price of our common stock and the general level of interest rates and our creditworthiness will directly affect the trading price for the ESUs.***

It is impossible to predict whether the price of our common stock or interest rates will rise or fall. Our creditworthiness, operating results and prospects and economic, financial and other factors will affect the trading prices of our common stock. In addition, market conditions can affect the capital markets generally, in turn affecting the price of our common stock. These conditions may include the level of, and fluctuations in, the trading prices of stocks generally and sales of substantial amounts of our common stock in the market after the offering of the ESUs or the perception that those sales could occur. Fluctuations in interest rates may affect the relative value of our common stock subject to issuance upon settlement of the purchase contracts.

***You may suffer dilution of our common stock issuable upon settlement of your purchase contract.***

The number of shares of our common stock issuable upon settlement of your purchase contract is subject to adjustment only for stock splits and combinations, stock dividends and other specified transactions described in this prospectus. See Description of the Equity Security Units Anti-dilution Adjustments for more information. The number of shares of our common stock issuable upon settlement of each purchase contract is not subject to adjustment for other events, such as employee stock option grants, offerings of common stock for cash, or in connection with acquisitions or other transactions, any of which may adversely affect the price of our common stock. The terms of the ESUs do not restrict our ability to offer common stock in the future or to engage in other transactions that could dilute our common stock. Moreover, we have no obligation to consider the interests of the holders of the ESUs in engaging in any such offering or transaction.

***The price of our common stock may fluctuate significantly, which may make it difficult for you to resell the common stock issuable upon settlement of the purchase contracts, when you want or at prices you find attractive.***

The price of our common stock on the New York Stock Exchange constantly changes. We expect that the market price of our common stock will continue to fluctuate. Because common stock is issuable upon settlement of the purchase contracts, volatility or depressed prices for our common stock could have similar effect on the trading price of the ESUs. Holders of ESUs who receive common stock upon settlement of the purchase contracts will also be subject to the risk of volatility and depressed prices.

***Our corporate documents and Delaware law contain provisions that could discourage, delay or prevent a change in control of our company even if some stockholders might consider such a development favorable, which may adversely affect the price of our common stock.***

Provisions in our amended and restated certificate of incorporation and amended and restated by-laws may discourage, delay or prevent a merger or acquisition involving us that our stockholders may consider favorable. For example, our amended and restated certificate of incorporation authorizes our board of directors to issue shares of preferred stock to which special rights are attached, including voting and dividend rights.

We are also subject to the anti-takeover provisions of Section 203 of the Delaware General Corporation Law. Under these provisions, if anyone becomes an interested stockholder, we may not enter into a business combination with that person for three years without special approval, which could discourage a

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third party from making a takeover offer and could delay or prevent a change of control. For purposes of Section 203, interested stockholder means, generally, someone owning 15% or more of our outstanding voting stock or an affiliate of ours that owned 15% or more of our outstanding voting stock during the past three years, subject to certain exceptions as described in Section 203.

Upon a change in control as defined in our existing credit facilities, the lenders under such existing credit facilities will have the right to require us to repay all of our outstanding obligations under the facility. In addition, the holders of certain series of indebtedness of certain of our subsidiaries will have the right upon the occurrence of a change of control as defined in such indebtedness or the indenture relating thereto, subject to certain conditions, to require us to repurchase their notes at a price equal to 100% or 101% of their principal amount, plus accrued and unpaid interest to the date of repurchase.

**USE OF PROCEEDS**

We will receive an aggregate of approximately \$272.1 million upon settlement of the purchase contracts, which we will use for general corporate purposes.

**Table of Contents****SELECTED FINANCIAL DATA**

The following historical selected financial data excludes certain of our international natural gas and oil production operations and our petroleum markets and coal mining businesses, which are presented as discontinued operations in our financial statements for all periods. The selected financial data below should be read together with Management's Discussion and Analysis of Financial Condition and Results of Operations beginning on page 19 of this prospectus and Financial Statements beginning on page F-1 of this prospectus. These selected historical results are not necessarily indicative of results to be expected in the future.

**As of or for the Year Ended December 31,**

|  | <b>2004</b>   | <b>2003</b>             | <b>2002</b>          | <b>2001</b> | <b>2000(3)</b> |
|--|---|-------------------------|----------------------|-------------|----------------|
|  |   | <b>(Restated)(1)(2)</b> | <b>(Restated)(1)</b> |             |                |
|  | <b>(In millions, except per common share amounts)</b> |                         |                      |             |                |
| <b>Operating Results Data:</b>   |   |                         |                      |             |                |
| Operating revenues   | \$ 5,874  | \$ 6,668                | \$ 6,881             | \$ 10,186   | \$ 6,179       |
| Income (loss) from continuing operations available to common stockholders(4) | \$ (802)  | \$ (605)                | \$ (1,242)           | \$ (223)    | \$ 481         |
| Net income (loss)  | \$ (948)  | \$ (1,928)              | \$ (1,875)           | \$ (447)    | \$ 665         |
| Basic income (loss) per common share from continuing operations              | \$ (1.25)   | \$ (1.01)               | \$ (2.22)            | \$ (0.44)   | \$ 0.98        |
| Diluted income (loss) per common share from continuing operations            | \$ (1.25)   | \$ (1.01)               | \$ (2.22)            | \$ (0.44)   | \$ 0.95        |
| Cash dividends declared per common share(5)                                  | \$ 0.16   | \$ 0.16                 | \$ 0.87              | \$ 0.85     | \$ 0.82        |
| Basic average common shares outstanding                                      | 639   | 597                     | 560                  | 505         | 494            |
| Diluted average common shares outstanding                                    | 639   | 597                     | 560                  | 505         | 506            |
| <b>Financial Position Data:</b>  |   |                         |                      |             |                |
| Total assets(6)  | \$ 31,383   | \$ 36,942               | \$ 41,923            | \$ 44,271   | \$ 43,992      |
| Long-term financing obligations(7)   | 18,241  | 20,275                  | 16,106               | 12,840      | 11,206         |
| Securities of subsidiaries(7)  | 367   | 447                     | 3,420                | 4,013       | 3,707          |
| Stockholders' equity   | 3,439   | 4,352                   | 5,749                | 6,666       | 6,145          |

- (1) During the completion of the financial statements for the year ended December 31, 2004, we identified an error in the manner in which we had originally adopted the provisions of SFAS No. 141, *Business Combinations*, and SFAS No. 142, *Goodwill and Other Intangible Assets*, in 2002. Upon adoption of these standards, we incorrectly adjusted the cost of investments in unconsolidated affiliates and the cumulative effect of change in accounting principle for the excess of our share of the affiliates' fair value of the net assets over their original cost, which we believed was negative goodwill. The amount originally recorded as a cumulative effect of accounting change was \$154 million and related to our investments in Citrus Corporation, Portland Natural Gas, several Australian investments and an investment in the Korea Independent Energy Corporation. We subsequently determined that

the amounts we adjusted were not negative goodwill, but rather amounts that should have been allocated to the long-lived assets underlying our investments. As a result, we were required to restate our 2002 financial statements to reverse the amount we recorded as a cumulative effect of an accounting change on January 1, 2002. This adjustment also impacted a deferred tax adjustment and an unrealized loss we recorded on our Australian investments during 2002, requiring a further restatement of that year. The restatements also affected the investment, deferred tax liability and stockholders' equity balances we reported as of December 31, 2002 and 2003. See Notes to Consolidated Financial Statements, Note 1 for a further discussion of the restatements.

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- (2) We also identified an error in the manner in which we had originally reported certain of our income taxes associated with our discontinued Canadian exploration and production operations for the year ended December 31, 2003. We incorrectly included approximately \$82 million of deferred tax benefits in continuing operations in the fourth quarter of 2003 that should have been reflected in discontinued operations. As a result, we were required to restate our 2003 financial statements, and related quarterly financial information, to reclassify this amount from continuing operations to discontinued operations. This restatement did not impact our reported net loss or balance sheet amounts as of and for the year ended December 31, 2003. See Notes to Consolidated Financial Statements, Note 1 for a further discussion of the restatement.
- (3) These amounts are derived from unaudited financial statements. Such amounts were restated in 2003 for the accounting impact of adjustments to our historical reserve estimates.
- (4) We incurred losses of \$1.1 billion in 2004, \$1.2 billion in 2003 and \$0.9 billion in 2002 related to impairments of assets and equity investments as well as restructuring charges related to industry changes and the related realignment of our businesses in response to those changes. In 2003, we also entered into an agreement in principle to settle claims associated with the western energy crisis of 2000 and 2001. This settlement resulted in charges of \$104 million in 2003 and \$899 million in 2002, both before income taxes. In addition, we incurred ceiling test charges of \$5 million, \$5 million and \$1,895 million in 2003, 2002 and 2001 on our full cost natural gas and oil properties. During 2001, we merged with The Coastal Corporation and incurred costs and asset impairments related to this merger that totaled approximately \$1.5 billion. For further discussions of events affecting comparability of our results in 2004, 2003 and 2002, see Notes to Consolidated Financial Statements, Notes 2 through 5.
- (5) Cash dividends declared per share of common stock represent the historical dividends declared by El Paso for all periods presented.
- (6) Decreases in 2002, 2003 and 2004 were a result of asset sales activities during these periods. See Notes to Consolidated Financial Statements, Note 3.
- (7) The increases in total long-term financing obligations in 2002 and 2003 was a result of the consolidations of our Chaparral and Gemstone power investments, the restructuring of other financing transactions, and the reclassification of securities of subsidiaries as a result of our adoption of SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity*, during 2003.

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**MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL  
CONDITION AND RESULTS OF OPERATIONS**

Our Management's Discussion and Analysis includes forward-looking statements that are subject to risks and uncertainties. Actual results may differ substantially from the statements we make in this section due to a number of factors that are discussed beginning on page 6.

**Overview**

Our business purpose is to provide natural gas and related energy products in a safe, efficient and dependable manner. We own North America's largest natural gas pipeline system and are a large independent natural gas producer. We also own and operate an energy marketing and trading business, a power business, midstream assets and investments, and have an investment in a small telecommunications business. Our power business primarily consists of international assets.

Since the end of 2001, our business activities have largely been focused on maintaining our core businesses of pipelines and production, while attempting to liquidate or otherwise divest of those businesses and operations that were not core to our long-term objectives, or that were not performing consistently with the expectations we had for them at the time we made the investment. Our overall objective during this period has been to reduce debt and improve liquidity, while at the same time invest in our core business activities. Our actions during this period have significantly impacted our financial condition, with the sale of almost \$10 billion of operating assets. These actions have also resulted in significant financial losses through asset impairments, realized losses on asset sales and reduction of income from the businesses sold.

We believe that 2004 was a watershed year for us. We were able to meet and exceed a number of the goals established under our 2003 Long Range Plan. As part of our efforts in 2004:

We focused capital investment on our core pipeline and production businesses, where in 2002, 2003 and 2004, we spent 87 percent, 91 percent, and 97 percent of our total capital dollars;

We completed the sale of a number of assets and investments including international production properties, a substantial portion of our general and limited partnership interests in GulfTerra, a significant portion of our worldwide petroleum markets operations, a significant portion of our domestic power generation operations and our merchant LNG business. Total proceeds from these sales were approximately \$3.3 billion;

We reduced our net debt (debt, net of cash) by \$3.4 billion in 2004, lowering our net debt to \$17.1 billion as of December 31, 2004; and

We continued our cost-reduction efforts with a goal of achieving \$150 million of savings by the end of 2006. As noted above, in 2004, we focused on expanding our pipeline operations and beginning the turnaround of our production business. During the year, we completed major expansions in our pipeline operations, including our Cheyenne Plains project to provide transmission outlets for natural gas supply in the Rocky Mountains, and we are moving forward on our Seafarer and Cypress projects to fulfill demand for natural gas in the southeastern United States, primarily Florida. Additionally, we continue to work in recontracting capacity on our systems and have been successful to date in these efforts. In our production operations, we instituted a new, more rigorous, risk analysis process which emphasizes strict capital discipline. Over the second half of 2004, this process resulted in a shifting of capital to areas with higher returns, improved drilling results and helped us to begin the stabilization of our domestic production. In addition, we have recently made several strategic acquisitions of production properties in Texas. In 2005, we will continue to work to achieve our long-range goals by:

Simplifying our capital structure;

Continuing to focus on expansions in our core pipeline business and completing the turnaround of our production business;



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Selling additional assets that we expect will generate proceeds from \$1.8 billion to \$2.2 billion;

Reducing outstanding debt (net of cash) to \$15 billion by the end of 2005; and

Continuing to reduce costs to achieve the cost savings outlined in our plan.

**Capital Resources and Liquidity**

We rely on cash generated from our internal operations as our primary source of liquidity, as well as available credit facilities, project and bank financings, proceeds from asset sales and the issuance of long-term debt, preferred securities and equity securities. From time to time, we have also used structured financing transactions that are sometimes referred to as off-balance sheet arrangements. We expect that our future funding for working capital needs, capital expenditures, long-term debt repayments, dividends and other financing activities will continue to be provided from some or all of these sources, although we do not expect to use off-balance sheet arrangements to the same degree in the future. Each of our existing and projected sources of cash are impacted by operational and financial risks that influence the overall amount of cash generated and the capital available to us. For example, cash generated by our business operations may be impacted by, among other things, changes in commodity prices, demands for our commodities or services, success in recontracting existing contracts, drilling success and competition from other providers or alternative energy sources. Collateral demands or recovery of cash posted as collateral are impacted by natural gas prices, hedging levels and the credit quality of us and our counterparties. Cash generated by future asset sales may depend on the condition and location of the assets and the number of interested buyers. In addition, our future liquidity will be impacted by our ability to access capital markets which may be restricted due to our credit ratings, general market conditions, and by limitations on our ability to access our existing shelf registration statement as further discussed in note 15 to our Consolidated Financial Statements. For a further discussion of risks that can impact our liquidity, see **Risk Factors** beginning on page 6.

Our subsidiaries are a significant potential source of liquidity to us and they participate in our cash management program to the extent they are permitted under their financing agreements and indentures. Under the cash management program, depending on whether a participating subsidiary has short-term cash surpluses or requirements, we either provide cash to them or they provide cash to us.

During 2004, we took additional steps to reduce our overall debt obligations. These actions included entering into a new \$3 billion credit agreement and selling entities with substantial debt obligations as follows (in millions):

|  |               |
|--|---------------|
| Debt obligations as of December 31, 2003 | \$ 21,732     |
| Principal amounts borrowed(1)            | 1,513         |
| Repayment of principal(2)                | (3,370)       |
| Sale of entities(3)                      | (887)         |
| Other                                    | 208           |
| <br>Total debt as of December 31, 2004   | <br>\$ 19,196 |

(1) Includes proceeds from a \$1.25 billion term loan under our new \$3 billion credit agreement.

(2) Includes \$850 million of repayments under our previous \$3 billion revolving credit facility.

(3) Consists of \$815 million of debt related to Utility Contract Funding and \$72 million of debt related to Mohawk River Funding IV.

For a further discussion of our long-term debt, other financing obligations and other credit facilities, see note 15 to our Consolidated Financial Statements.



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As of December 31, 2004, we had available liquidity as follows (in billions):

|   |               |
|---|---------------|
| Available cash  | \$ 1.8        |
| Available capacity under our \$3 billion credit agreement | 0.6           |
| <b>Net available liquidity at December 31, 2004</b>       | <b>\$ 2.4</b> |

In addition to our available liquidity, we expect to generate significant operating cash flow in 2005. We will supplement this operating cash flow with proceeds from asset sales, which we expect will range from \$1.8 billion to \$2.2 billion over the next 12 to 24 months (of which \$0.7 billion has already closed through March 25, 2005). We will also utilize proceeds from our financing activities as needed. In March 2005, we completed a \$200 million financing at CIG. The proceeds will be used to refinance \$180 million of bonds at CIG that will mature in June 2005 and for other general purposes.

In 2005 we expect to spend between \$1.6 billion and \$1.7 billion on capital investments mainly in our core pipeline and production businesses. We have also spent approximately \$0.3 billion on acquisitions in our natural gas and oil operations in 2005, and may make additional acquisitions during 2005. As of December 31, 2004, our contractual debt maturities for 2005 and 2006 were approximately \$0.6 billion and \$1.3 billion. Additionally, we had approximately \$0.8 billion of zero-coupon debentures that have a stated maturity of 2021, but contain an option whereby the holders can require us to redeem the obligations in February 2006. We currently expect the holders to exercise this right, which combined with our contractual maturities could require us to retire up to \$2.1 billion of debt in 2006. So far, in 2005 we have prepaid approximately \$0.7 billion of our Euro denominated debt originally scheduled to mature in March 2006 and \$0.2 billion of our zero-coupon debentures. As a result of these prepayments, we have reduced our 2006 expected maturities to approximately \$1.2 billion which will give us greater financial flexibility next year.

Finally, in 2005 we may also prepay a number of other obligations including derivative positions in our marketing and trading operations and possibly amounts outstanding for the Western Energy Settlement, among other items. These prepayments could total approximately \$1.1 billion. Of this amount, we have already prepaid approximately \$240 million of obligations through the transfer of derivative contracts to Constellation Power in March 2005, in connection with the sale of Cedar Brakes I and II.

Our net available liquidity includes our \$3 billion credit agreement. As of December 31, 2004, we had borrowed \$1.25 billion as a term loan and issued approximately \$1.2 billion of letters of credit under this agreement. The availability of borrowings under this credit agreement and our ability to incur additional debt is subject to various conditions as further described in note 15 to our Consolidated Financial Statements, which we currently meet. These conditions include compliance with the financial covenants and ratios required by those agreements, absence of default under the agreements, and continued accuracy of the representations and warranties contained in the agreements. The financial coverage ratios under our \$3 billion credit agreement change over time. However, these covenants currently require our Debt to Consolidated EBITDA not to exceed 6.5 to 1 and our ratio of Consolidated EBITDA to interest expense and dividends to be equal to or greater than 1.6 to 1, each as defined in the credit agreement. As of December 31, 2004, our ratio of Debt to Consolidated EBITDA was 4.85 to 1 and our ratio of Consolidated EBITDA to interest expense and dividends was 1.93 to 1.

Our \$3 billion credit agreement is collateralized by our equity interests in TGP, EPNG, ANR, CIG, WIC, Southern Gas Storage Company, and ANR Storage Company. Based upon a review of the covenants contained in our indentures and our other financing obligations, acceleration of the outstanding amounts under the credit agreement could constitute an event of default under some of our other debt agreements. If there was an event of default and the lenders under the credit agreement were to exercise their rights to the collateral, we could be required to liquidate our interests in these entities that collateralize the credit agreement. Additionally, we would be unable to obtain cash from our pipeline subsidiaries through our cash management program in an event of default under some of our subsidiaries indentures. Finally, three of our subsidiaries have indentures associated with their public debt that contain \$5 million

cross-acceleration provisions.

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We believe we will be able to meet our ongoing liquidity and cash needs through the combination of available cash and borrowings under our \$3 billion credit agreement. We also believe that the actions we have taken to date will allow us greater financial flexibility for the remainder of 2005 and into 2006 than we had in 2004. However, a number of factors could influence our liquidity sources, as well as the timing and ultimate outcome of our ongoing efforts and plans. These factors are discussed in detail beginning on page 13.

**Table of Contents****Overview of Cash Flow Activities for 2004 Compared to 2003**

For the years ended December 31, 2004 and 2003, our cash flows are summarized as follows:

|  | 2004     | 2003<br>(Restated) |
|--|----------|--------------------|
| (In billions)  |          |                    |
| <b>Cash inflows</b>  |          |                    |
| <i>Continuing operating activities</i>                           |          |                    |
| Net loss before discontinued operations                          | \$ (0.8) | \$ (0.6)           |
| Non-cash income adjustments                                      | 2.4      | 1.8                |
| Payment on Western Energy Settlement                             | (0.6)    |                    |
| Change in assets and liabilities                                 | 0.1      | 1.1                |
|  | 1.1      | 2.3                |
| <i>Continuing investing activities</i>                           |          |                    |
| Net proceeds from the sale of assets and investments             | 1.9      | 2.5                |
| Net proceeds from restricted cash                                | 0.6      |                    |
| Other  | 0.1      |                    |
|  | 2.6      | 2.5                |
| <i>Continuing financing activities</i>                           |          |                    |
| Net proceeds from the issuance of long-term debt                 | 1.3      | 3.6                |
| Borrowings under long-term credit facility                       |          | 0.5                |
| Proceeds from the issuance of common stock                       | 0.1      | 0.1                |
| Net discontinued operations activity                             | 1.0      | 0.4                |
|  | 2.4      | 4.6                |
| Total cash inflows   | \$ 6.1   | \$ 9.4             |
| <b>Cash outflows</b>   |          |                    |
| <i>Continuing investing activities</i>                           |          |                    |
| Additions to property, plant, and equipment                      | \$ 1.8   | \$ 2.4             |
| Net cash paid to acquire Chaparral and Gemstone                  |          | 1.1                |
| Net payments of restricted cash                                  |          | 0.5                |
| Other  |          | 0.1                |
|  | 1.8      | 4.1                |
| <i>Continuing financing activities</i>                           |          |                    |
| Payments to retire long-term debt and redeem preferred interests | 2.5      | 4.1                |
| Payments of revolving credit facilities                          | 0.9      | 1.2                |
| Dividends paid to common stockholders                            | 0.1      | 0.2                |
| Other  | 0.1      |                    |
|  | 3.6      | 5.5                |

|                     |        |          |
|---------------------|--------|----------|
| Total cash outflows | 5.4    | 9.6      |
| Net change in cash  | \$ 0.7 | \$ (0.2) |

**Table of Contents****Cash From Continuing Operating Activities**

Overall, cash generated from continuing operating activities decreased by \$1.2 billion largely due to a payment of \$0.6 billion related to the principal litigation under the Western Energy Settlement in 2004 and higher cash recovered from margin deposits in 2003. We recovered \$0.7 billion of cash in 2003 from our margin deposits by substituting letters of credit for cash on deposit as compared to \$0.1 billion recovered in 2004.

**Cash From Continuing Investing Activities**

For the year ended December 31, 2004, net cash provided by our continuing investing activities was \$0.8 billion. During the year, we received net proceeds of approximately \$0.9 billion from sales of our domestic power assets as well as \$1.0 billion from the sales of our general and limited partnership interests in GulfTerra and various other Field Services assets. We also released restricted cash of \$0.6 billion out of escrow, which was paid to the settling parties to the Western Energy Settlement as discussed above.

Our 2004 capital expenditures included the following (in billions):

|  |            |
|--|------------|
| Production exploration, development and acquisition expenditures       | \$ 0.7     |
| Pipeline expansion, maintenance and integrity projects                 | 1.0        |
| Other (primarily power projects)                                       | 0.1        |
| <br>Total capital expenditures and net additions to equity investments | <br>\$ 1.8 |

In 2005, we expect our total capital expenditures, including acquisitions, to be approximately \$1.9 billion, divided approximately equally between our Production and Pipelines segments. In 2004, our Production segment received funds of approximately \$110 million from third parties under net profits interest agreements. In March 2005, we purchased all of the interests held by one of the parties to these agreements for \$62 million. See Supplemental Financial Information, under the heading Supplemental Natural Gas and Oil Operations (Unaudited), for a further discussion of these agreements.

In September 2004, we incurred significant damage to sections of our offshore pipeline facilities due to Hurricane Ivan. Cost estimates are currently in the \$80 million to \$95 million range with damage assessment still in progress. We expect insurance reimbursement with the exception of a \$2 million deductible for this event; however the timing of such reimbursements may occur later than the capital expenditures on the damaged facilities which may increase our net capital expenditures for 2005.

In January 2005, we sold our remaining interests in Enterprise and its general partner for \$425 million. We also sold our membership interest in two subsidiaries that own and operate natural gas gathering systems and the Indian Springs processing facility to Enterprise for \$75 million. During 2005, we will continue to divest, where appropriate, our non-core assets based on our long-term business strategy, including additional power assets in Asia and other countries (see Business and note 3 to our Consolidated Financial Statements, for a further discussion of these divestitures and the asset divestitures of our discontinued operations). The timing and extent of these additional sales will be based on the level of market interest and based upon obtaining the necessary approvals.

**Cash From Continuing Financing Activities**

Net cash used in our continuing financing activities was \$1.2 billion for the year ended December 31, 2004. During 2004, our significant financing cash inflows included \$1.25 billion borrowed as a term loan under our new \$3 billion credit agreement. We also had \$1.0 billion of cash contributed by our discontinued operations. Of the amount contributed by our discontinued operations, \$0.2 billion was generated from operations, \$1.2 billion was received as proceeds from the sales of our Eagle Point and Aruba refineries and our international production operations, primarily in western Canada, and \$0.4 billion was used to repay long-term debt related to the Aruba refinery.

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Our significant financing cash outflows included net repayments of \$0.9 billion on our previous \$3 billion revolving credit facilities during 2004, prior to entering into our new \$3 billion credit agreement. We also made \$2.5 billion of payments to retire third party long-term debt and redeem preferred interests as we continued in our efforts to reduce our overall debt obligations under our Long-Range Plan. See note 15 to our Consolidated Financial Statements, for further detail of our financing activities.

**Contractual Obligations and Off-Balance Sheet Arrangements**

In the course of our business activities, we enter into a variety of financing arrangements and contractual obligations. The following discusses those contingent obligations, often referred to as off-balance sheet arrangements. We also present aggregated information on our contractual cash obligations, some of which are reflected in our financial statements, such as short-term and long-term debt and other accrued liabilities; other obligations, such as operating leases; and capital commitments are not reflected in our financial statements.

**Off-Balance Sheet Arrangements and Related Liabilities**

***Guarantees***

We are involved in various joint ventures and other ownership arrangements that sometimes require additional financial support in the form of financial and performance guarantees. In a financial guarantee, we are obligated to make payments if the guaranteed party fails to make payments under, or violates the terms of, the financial arrangement. In a performance guarantee, we provide assurance that the guaranteed party will execute on the terms of the contract. If they do not, we are required to perform on their behalf. For example, if the guaranteed party is required to deliver natural gas to a third party and then fails to do so, we would be required to either deliver that natural gas or make payments to the third party equal to the difference between the contract price and the market value of the natural gas. We also periodically provide indemnification arrangements related to assets or businesses we have sold. These arrangements include indemnifications for income taxes, the resolution of existing disputes, environmental matters, and necessary expenditures to ensure the safety and integrity of the assets sold.

We evaluate our guarantees and indemnity arrangements at the time they are entered into and in each period thereafter to determine whether a liability exists and, if so, if it can be estimated. We record accruals when both these criteria are met. As of December 31, 2004, we had accrued \$70 million related to these arrangements. As of December 31, 2004, we also had approximately \$40 million of financial and performance guarantees and indemnification arrangements not otherwise reflected in our financial statements.

**Table of Contents****Contractual Obligations**

The following table summarizes our contractual obligations as of December 31, 2004, for each of the years presented (all amounts are undiscounted):

|   | 2005            | 2006            | 2007            | 2008            | 2009            | Thereafter       | Total            |
|---|-----------------|-----------------|-----------------|-----------------|-----------------|------------------|------------------|
| <b>(In millions)</b>  |                 |                 |                 |                 |                 |                  |                  |
| <b>Long-term financing obligations:(1)</b>                        |                 |                 |                 |                 |                 |                  |                  |
| Principal   | \$ 948          | \$ 1,155        | \$ 835          | \$ 733          | \$ 2,637        | \$ 13,031        | \$ 19,339        |
| Interest  | 1,356           | 1,330           | 1,257           | 1,191           | 1,127           | 11,762           | 18,023           |
| Western Energy Settlement(2)                                      | 44              | 44              | 44              | 44              | 44              | 634              | 854              |
| Other contractual liabilities(3)                                  | 31              | 47              | 23              | 22              | 5               | 32               | 160              |
| Operating leases(4)   | 79              | 66              | 51              | 43              | 40              | 163              | 442              |
| <b>Other contractual commitments and purchase obligations:(5)</b> |                 |                 |                 |                 |                 |                  |                  |
| Tolling, transportation and storage(6)                            | 178             | 144             | 131             | 127             | 122             | 779              | 1,481            |
| Commodity purchases(7)  | 30              | 28              | 28              | 17              | 10              | 36               | 149              |
| Other(8)  | 151             | 36              | 14              | 15              | 5               | 3                | 224              |
| <b>Total contractual obligations</b>                              | <b>\$ 2,817</b> | <b>\$ 2,850</b> | <b>\$ 2,383</b> | <b>\$ 2,192</b> | <b>\$ 3,990</b> | <b>\$ 26,440</b> | <b>\$ 40,672</b> |

(1) See Notes to Consolidated Financial Statements, Note 15.

(2) See Notes to Consolidated Financial Statements, Note 17.

(3) Includes contractual, environmental and other obligations included in other noncurrent liabilities in our balance sheet. Excludes expected contributions to our pension and other postretirement benefit plans of \$68 million in 2005 and \$209 million for the four year period ended December 31, 2009, because these expected contributions are not contractually required.

(4) See Notes to Consolidated Financial Statements, Note 17.

(5) Other contractual commitments and purchase obligations are defined as legally enforceable agreements to purchase goods or services that have fixed or minimum quantities and fixed or minimum variable price provisions, and that detail approximate timing of the underlying obligations.

(6) These are commitments for demand charges on our tolling arrangements and for firm access to natural gas transportation and storage capacity.

(7) Includes purchase commitments for natural gas and power.

(8) Includes commitments for drilling and seismic activities in our production operations and various other maintenance, engineering, procurement and construction contracts, as well as service and license agreements, used by our other operations.

**Commodity-based Derivative Contracts**

We utilize derivative financial instruments in hedging activities, power contract restructuring activities and in our historical energy trading activities. In the tables below, derivatives designated as hedges primarily consist of instruments used to hedge natural gas production. Derivatives from power contract restructuring activities relate to power purchase and sale agreements that arose from our activities in that business and other commodity-based derivative contracts relate to our historical energy trading activities as well as other derivative contracts not designated as hedges.

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The following table details the fair value of our commodity-based derivative contracts by year of maturity and valuation methodology as of December 31, 2004:

| Source of Fair Value  | Maturity<br>Less<br>Than<br>1 Year | Maturity<br>1 to 3<br>Years | Maturity<br>4 to 5<br>Years | Maturity<br>6 to 10<br>Years | Maturity<br>Beyond<br>10 Years | Total<br>Fair<br>Value |
|---|------------------------------------|-----------------------------|-----------------------------|------------------------------|--------------------------------|------------------------|
| <b>(In millions)</b>  |                                    |                             |                             |                              |                                |                        |
| <b>Derivatives designated as hedges</b>                           |                                    |                             |                             |                              |                                |                        |
| Assets  | \$ 92                              | \$ 33                       | \$                          | \$                           | \$                             | \$ 125                 |
| Liabilities   | (416)                              | (222)                       | (14)                        | (9)                          |                                | (661)                  |
| Total derivatives designated as hedges                            | (324)                              | (189)                       | (14)                        | (9)                          |                                | (536)                  |
| <b>Assets from power contract restructuring derivatives(1)(2)</b> |                                    |                             |                             |                              |                                |                        |
|   | 105                                | 199                         | 151                         | 210                          |                                | 665                    |
| <b>Other commodity-based derivatives</b>                          |                                    |                             |                             |                              |                                |                        |
| <b>Exchange-traded positions(3)</b>                               |                                    |                             |                             |                              |                                |                        |
| Assets  | 19                                 | 220                         | 76                          |                              |                                | 315                    |
| Liabilities   | (107)                              | (1)                         |                             |                              |                                | (108)                  |
| <b>Non-exchange traded positions(2)</b>                           |                                    |                             |                             |                              |                                |                        |
| Assets  | 431                                | 271                         | 186                         | 166                          | 46                             | 1,100                  |
| Liabilities(1)  | (372)                              | (448)                       | (267)                       | (230)                        | (51)                           | (1,368)                |
| Total other commodity-based derivatives                           | (29)                               | 42                          | (5)                         | (64)                         | (5)                            | (61)                   |
| Total commodity-based derivatives                                 | \$ (248)                           | \$ 52                       | \$ 132                      | \$ 137                       | \$ (5)                         | \$ 68                  |

- (1) Includes \$259 million of intercompany derivatives that eliminate in consolidation and have no impact on our consolidated assets and liabilities from price risk management activities.
- (2) In March 2005, we sold our Cedar Brakes I and II subsidiaries and their related restructured power contracts, which had a fair value of \$596 million as of December 31, 2004. In connection with this sale, we also assigned or terminated other commodity-based derivatives that had a fair value loss of \$240 million as of December 31, 2004.
- (3) Exchange-traded positions are traded on active exchanges such as the New York Mercantile Exchange, the International Petroleum Exchange and the London Clearinghouse.

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The following is a reconciliation of our commodity-based derivatives for the years ended December 31, 2004 and 2003.

|  | <b>Derivatives<br/>Designated<br/>as<br/>Hedges</b> | <b>Derivatives<br/>from<br/>Power<br/>Contract<br/>Restructuring<br/>Activities</b> | <b>Other<br/>Commodity-<br/>Based<br/>Derivatives</b> | <b>Total<br/>Commodity-<br/>Based<br/>Derivatives</b> |
|--|---|---|---|---|
| <b>(In millions)</b>   |   |   |   |   |
| Fair value of contracts outstanding at<br>December 31, 2002                              | \$ (21)   | \$ 968  | \$ (525)  | \$ 422  |
| Fair value of contract settlements<br>during the period                                  | 15  | (405)   | 602   | 212   |
| Change in fair value of contracts  | (25)  | 140   | (477)   | (362)   |
| Original fair value of contracts<br>consolidated as a result of Chaparral<br>acquisition |   | 1,222   |   | 1,222   |
| Option premiums received, net  |   |   | (88)  | (88)  |
| Net change in contracts outstanding<br>during the period                                 | (10)  | 957   | 37  | 984   |
| Fair value of contracts outstanding at<br>December 31, 2003                              | (31)  | 1,925   | (488)   | 1,406   |
| Fair value of contract settlements<br>during the period                                  | 49  | (1,132)(1)  | 284   | (799)   |
| Change in fair value of contracts  | 38  | (128)(2)  | (513)(3)  | (603)   |
| Other commodity-based derivatives<br>designated as hedges                                | (592)   |   | 592   |   |
| Option premiums paid, net  |   |   | 64  | 64  |
| Net change in contracts outstanding<br>during the period                                 | (505)   | (1,260)   | 427   | (1,338)   |
| Fair value of contracts outstanding at<br>December 31, 2004                              | \$ (536)  | \$ 665  | \$ (61)   | \$ 68   |

(1) Includes \$861 million and \$75 million of derivative contracts sold in conjunction with the sales of Utility Contract Funding and Mohawk River Funding IV in 2004. See Notes to Consolidated Financial Statements, Notes 3 and 5 for additional information on these sales.

(2)

In the fourth quarter of 2004, we recorded a \$227 million charge associated with the sale of our Cedar Brakes I and II subsidiaries and their related restructured power contracts. See Notes to Consolidated Financial Statements, Notes 3 and 5 for additional information on this sale.

- (3) In the second quarter of 2004, we reclassified a \$69 million liability from our Western Energy Settlement obligation to our price risk management activities.

The fair value of contract settlements during the period represents the estimated amounts of derivative contracts settled through physical delivery of a commodity or by a claim to cash as accounts receivable or payable. The fair value of contract settlements also includes physical or financial contract terminations due to counterparty bankruptcies and the sale or settlement of derivative contracts through early termination or through the sale of the entities that own these contracts. The change in fair value of contracts during the year represents the change in value of contracts from the beginning of the period, or the date of their origination or acquisition, until their settlement, early termination or, if not settled or terminated, until the end of the period. During 2003, in conjunction with our acquisition of Chaparral, we consolidated a number of derivative contracts. The majority of the value of these contracts was for power purchase agreements and power supply agreements related to power contract restructuring activities conducted by Chaparral.

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In December 2004, we designated a number of our other commodity-based derivative contracts in our Marketing and Trading segment as hedges of our 2005 and 2006 natural gas production. As a result, we reclassified this amount to derivatives designated as hedges beginning in the fourth quarter of 2004. The combination of these positions and our Production segment's other hedges will result in us receiving the following prices on our natural gas production:

|              | <b>Volume</b><br>(TBtu) | <b>Hedge Price(1)</b><br>(per MMBtu) | <b>Cash Price</b><br>(per MMBtu) |
|--------------|-------------------------|--------------------------------------|----------------------------------|
| 2005         | 132                     | \$ 6.75                              | \$ 3.74(2)                       |
| 2006         | 86                      | \$ 6.34                              | \$ 4.01(2)                       |
| 2007         | 5                       | \$ 3.56                              | \$ 3.56                          |
| 2008 to 2012 | 21                      | \$ 3.67                              | \$ 3.67                          |

- (1) Our Production segment will record revenues related to these natural gas volumes at this price in their operating results.
- (2) The difference between our Production segment's hedge price and the cash price we will receive upon settlement of the derivative transactions was previously recorded as losses in our Marketing and Trading segment.

To stabilize the company's pricing outlook for 2005 to 2007, our Marketing and Trading segment entered into additional contracts that provide a floor price on a portion of our unhedged production in 2005, 2006 and 2007 and a ceiling price on a portion of our unhedged 2006 production. These contracts, which are reported on a mark-to-market basis, will result in us receiving the following cash prices on our natural gas production:

|      | <b>Floor Price(1)</b><br>(per MMBtu) | <b>Floor Volume</b><br>(TBtu) | <b>Ceiling Price(2)</b><br>(per MMBtu) | <b>Ceiling Volume</b><br>(TBtu) |
|------|--------------------------------------|-------------------------------|--|---------------------------------|
| 2005 | \$ 6.00                              | 60                            |  |                                 |
| 2006 | \$ 6.00                              | 120                           | \$ 9.50                                | 60                              |
| 2007 | \$ 6.00                              | 30                            |  |                                 |

- (1) The floor price is the minimum cash price to be received under the option contract.
- (2) The ceiling price is the maximum cash price to be received under the option contract.

**Results of Operations****Overview**

Since 2001, we have experienced tremendous change in our businesses. Prior to this time, we had grown through mergers and acquisitions and internal growth initiatives, and at the same time had incurred significant amounts of debt and other obligations. In late 2001, driven by the bankruptcy of a number of energy sector participants, followed by increased scrutiny of our debt levels and credit rating downgrades of our debt and the debt of many of our competitors, our focus changed to improving liquidity, paying down debt, simplifying our capital structure, reducing our cost of capital, resolving substantial contingencies and returning to our core natural gas businesses. Accordingly, our operating results during the three year period from 2002 to 2004 have been substantially impacted by a number of

significant events, such as asset sales, significant legal settlements and ongoing business restructuring efforts as part of this change in focus.

As of December 31, 2004, our operating business segments were Pipelines, Production, Marketing and Trading, Power and Field Services. These segments provide a variety of energy products and services. They are managed separately and each requires different technology and marketing strategies. Our businesses are divided into two primary business lines: regulated and non-regulated. Our regulated business includes our Pipelines segment, while our non-regulated business includes our Production, Marketing and Trading, Power and Field Services segments.

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Our management uses EBIT to assess the operating results and effectiveness of our business segments. We define EBIT as net income (loss) adjusted for (i) items that do not impact our income (loss) from continuing operations, such as extraordinary items, discontinued operations and the impact of accounting changes, (ii) income taxes, (iii) interest and debt expense and (iv) distributions on preferred interests of consolidated subsidiaries.

Our businesses consist of consolidated operations as well as investments in unconsolidated affiliates. We exclude interest and debt expense and distributions on preferred interests of consolidated subsidiaries so that investors may evaluate our operating results independently from our financing methods or capital structure. We believe EBIT is helpful to our investors because it allows them to more effectively evaluate the operating performance of both our consolidated businesses and our unconsolidated investments using the same performance measure analyzed internally by our management. EBIT may not be comparable to measurements used by other companies. Additionally, EBIT should be considered in conjunction with net income and other performance measures such as operating income or operating cash flow.

Below is a reconciliation of our EBIT (by segment) to our consolidated net loss for each of the three years ended December 31:

|   | 2004     | 2003          | 2002          |
|---|----------|---------------|---------------|
|   |          | (Restated)(1) | (Restated)(1) |
|   |          | (In millions) |               |
| <i>Regulated Business</i>   |          |               |               |
| Pipelines   | \$ 1,331 | \$ 1,234      | \$ 828        |
| <i>Non-regulated Businesses</i>                                   |          |               |               |
| Production  | 734      | 1,091         | 808           |
| Marketing and Trading   | (547)    | (809)         | (1,977)       |
| Power   | (569)    | (28)          | 12            |
| Field Services  | 120      | 133           | 289           |
| Segment EBIT  | 1,069    | 1,621         | (40)          |
| <i>Corporate and other</i>  | (214)    | (852)         | (387)         |
| Consolidated EBIT   | 855      | 769           | (427)         |
| Interest and debt expense   | (1,607)  | (1,791)       | (1,297)       |
| Distributions on preferred interests of consolidated subsidiaries | (25)     | (52)          | (159)         |
| Income taxes  | (25)     | 469           | 641           |
| Loss from continuing operations                                   | (802)    | (605)         | (1,242)       |
| Discontinued operations, net of income taxes                      | (146)    | (1,314)       | (425)         |
| Cumulative effect of accounting changes, net of income taxes      |          | (9)           | (208)         |
| Net loss  | \$ (948) | \$ (1,928)    | \$ (1,875)    |

- (1) See Notes to Consolidated Financial Statements, Note 1 for a discussion of the restatements of our 2002 and 2003 financial statements. The restatement of our 2002 financial statements affected our Pipelines segment results and the amounts reported as a cumulative effect of accounting change in 2002. The restatement of our 2003 financial

statements affected the classification of income taxes between continuing and discontinued operations, and therefore the results reported as continuing versus discontinued for that period.

As we refocused our activities on our core businesses by divesting of non-core businesses and restructuring our organization, we incurred losses and incremental costs in each year. During this period, we also resolved significant legal contingencies. These items are described in the table below. For a more detailed

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discussion of these factors and other items impacting our financial performance, see the individual segment and other results included in Notes to Consolidated Financial Statements, Notes 3 through 5, and 21.

**Operating Segments**

| <b>Pipelines</b> | <b>Production</b> | <b>Marketing<br/>and<br/>Trading</b> | <b>Power</b> | <b>Field<br/>Services</b> | <b>Corporate &amp;<br/>Other</b> |
|------------------|-------------------|--------------------------------------|--------------|---------------------------|----------------------------------|
|------------------|-------------------|--------------------------------------|--------------|---------------------------|----------------------------------|

**(In millions)**

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