WILLIAMS COMPANIES INC
Form 10-Q
November 01, 2018

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549
FORM 10-Q
(Mark One)
þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2018
or
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____________ to _____________
Commission file number 1-4174
THE WILLIAMS COMPANIES, INC.
(Exact name of registrant as specified in its charter)

DELAWARE	73-0569878
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
ONE WILLIAMS CENTER TULSA, OKLAHOMA	74172-0172
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (918) 573-2000
NO CHANGE

(Former name, former address and former fiscal year, if changed since last report.)
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer þ	Accelerated filer ¨	Non-accelerated filer ¨	Smaller reporting company ¨	Emerging growth company ¨
		(Do not check if a smaller reporting company)		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.) Yes ¨ No þ

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Shares Outstanding at October 29, 2018
Common Stock, $1 par value	1,210,542,031

The Williams Companies, Inc.
Index

	Page
Part I. Financial Information	
Item 1. Financial Statements	
Consolidated Statement of Income – Three and Nine Months Ended September 30, 2018 and 2017	6
Consolidated Statement of Comprehensive Income – Three and Nine Months Ended September 30, 2018 and 2017	7
Consolidated Balance Sheet – September 30, 2018 and December 31, 2017	8
Consolidated Statement of Changes in Equity – Nine Months Ended September 30, 2018	9
Consolidated Statement of Cash Flows – Nine Months Ended September 30, 2018 and 2017	10
Notes to Consolidated Financial Statements	11
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	46
Item 3. Quantitative and Qualitative Disclosures About Market Risk	71
Item 4. Controls and Procedures	71
Part II. Other Information	71
Item 1. Legal Proceedings	71
Item 1A. Risk Factors	73
Item 6. Exhibits	74

The reports, filings, and other public announcements of The Williams Companies, Inc. (Williams) may contain or incorporate by reference statements that do not directly or exclusively relate to historical facts. Such statements are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (Exchange Act). These forward-looking statements relate to anticipated financial performance, management's plans and objectives for future operations, business prospects, outcome of regulatory proceedings, market conditions, and other matters. We make these forward-looking statements in reliance on the safe harbor protections provided under the Private Securities Litigation Reform Act of 1995.

All statements, other than statements of historical facts, included in this report that address activities, events or developments that we expect, believe or anticipate will exist or may occur in the future, are forward-looking statements. Forward-looking statements can be identified by various forms of words such as "anticipates," "believes," "seeks," "could," "may," "should," "continues," "estimates," "expects," "forecasts," "intends," "might," "goals," "objectives," "potential," "projects," "scheduled," "will," "assumes," "guidance," "outlook," "in-service date," or other similar expressions. forward-looking statements are based on management's beliefs and assumptions and on information currently available to management and include, among others, statements regarding:

- Levels of dividends to Williams stockholders;
- Future credit ratings of Williams and its affiliates;
- Amounts and nature of future capital expenditures;
- Expansion and growth of our business and operations;

- Expected in-service dates for capital projects;
- Financial condition and liquidity;
- Business strategy;
- Cash flow from operations or results of operations;
- Seasonality of certain business components;
- Natural gas and natural gas liquids prices, supply, and demand;
- Demand for our services.

Forward-looking statements are based on numerous assumptions, uncertainties and risks that could cause future events or results to be materially different from those stated or implied in this report. Many of the factors that will determine these results are beyond our ability to control or predict. Specific factors that could cause actual results to differ from results contemplated by the forward-looking statements include, among others, the following:

- Whether we are able to pay current and expected levels of dividends;
- Whether we will be able to effectively execute our financing plan;
- Availability of supplies, market demand, and volatility of prices;
- Inflation, interest rates, and general economic conditions (including future disruptions and volatility in the global credit markets and the impact of these events on customers and suppliers);
- The strength and financial resources of our competitors and the effects of competition;
- Whether we are able to successfully identify, evaluate and timely execute investment opportunities;
- Our ability to acquire new businesses and assets and successfully integrate those operations and assets into existing businesses as well as successfully expand our facilities, and to consummate asset sales on acceptable terms;
- Development and rate of adoption of alternative energy sources;
- The impact of operational and developmental hazards and unforeseen interruptions;
- The impact of existing and future laws (including, but not limited to, the Tax Cuts and Job Acts of 2017 and Colorado Proposition 112), regulations, the regulatory environment, environmental liabilities, and litigation, as well as our ability to obtain necessary permits and approvals, and achieve favorable rate proceeding outcomes;
- Our costs and funding obligations for defined benefit pension plans and other postretirement benefit plans;
- Changes in maintenance and construction costs;

2

- Changes in the current geopolitical situation;
- Our exposure to the credit risk of our customers and counterparties;
- Risks related to financing, including restrictions stemming from debt agreements, future changes in credit ratings as determined by nationally recognized credit rating agencies, and the availability and cost of capital;
- The amount of cash distributions from and capital requirements of our investments and joint ventures in which we participate;
- Risks associated with weather and natural phenomena, including climate conditions and physical damage to our facilities;
- Acts of terrorism, cybersecurity incidents, and related disruptions;
- Additional risks described in our filings with the Securities and Exchange Commission (SEC).

Given the uncertainties and risk factors that could cause our actual results to differ materially from those contained in any forward-looking statement, we caution investors not to unduly rely on our forward-looking statements. We disclaim any obligations to and do not intend to update the above list or announce publicly the result of any revisions to any of the forward-looking statements to reflect future events or developments.

In addition to causing our actual results to differ, the factors listed above and referred to below may cause our intentions to change from those statements of intention set forth in this report. Such changes in our intentions may also cause our results to differ. We may change our intentions, at any time and without notice, based upon changes in such factors, our assumptions, or otherwise.

Because forward-looking statements involve risks and uncertainties, we caution that there are important factors, in addition to those listed above, that may cause actual results to differ materially from those contained in the forward-looking statements. For a detailed discussion of those factors, see Part I, Item 1A. Risk Factors in our Annual Report on Form 10-K filed with the SEC on February 22, 2018, as supplemented by the disclosure in Part II, Item 1A. Risk Factors in this Quarterly Report on Form 10-Q.

DEFINITIONS

The following is a listing of certain abbreviations, acronyms, and other industry terminology that may be used throughout this Form 10-Q.

Measurements:
Barrel: One barrel of petroleum products that equals 42 U.S. gallons
Bcf: One billion cubic feet of natural gas
Bcf/d: One billion cubic feet of natural gas per day
British Thermal Unit (Btu): A unit of energy needed to raise the temperature of one pound of water by one degree Fahrenheit
Dekatherms (Dth): A unit of energy equal to one million British thermal units
Mbbls/d: One thousand barrels per day
Mdth/d: One thousand dekatherms per day
MMcf/d: One million cubic feet per day
MMdth: One million dekatherms or approximately one trillion British thermal units
MMdth/d: One million dekatherms per day
Tbtu: One trillion British thermal units
Consolidated Entities:
Cardinal: Cardinal Gas Services, L.L.C.
Constitution: Constitution Pipeline Company, LLC
Gulfstar One: Gulfstar One LLC
Northwest Pipeline: Northwest Pipeline LLC
Transco: Transcontinental Gas Pipe Line Company, LLC
WPZ: Williams Partners L.P. Effective August 10, 2018, we completed our merger with WPZ, pursuant to which we acquired all outstanding common units of WPZ held by others and Williams continued as the surviving entity.
Partially Owned Entities: Entities in which we do not own a 100 percent ownership interest and which, as of September 30, 2018, we account for as an equity-method investment, including principally the following:
Aux Sable: Aux Sable Liquid Products LP
Caiman II: Caiman Energy II, LLC
Discovery: Discovery Producer Services LLC
Gulfstream: Gulfstream Natural Gas System, L.L.C.
Jackalope: Jackalope Gas Gathering Services, L.L.C.
Laurel Mountain: Laurel Mountain Midstream, LLC
OPPL: Overland Pass Pipeline Company LLC
RMM: Rocky Mountain Midstream Holdings LLC
UEOM: Utica East Ohio Midstream LLC

Government and Regulatory:
EPA: Environmental Protection Agency
FERC: Federal Energy Regulatory Commission
SEC: Securities and Exchange Commission
Other:
ETE Merger Agreement: Merger Agreement and Plan of Merger of Williams with Energy Transfer Equity, L.P and certain of its affiliates
Fractionation: The process by which a mixed stream of natural gas liquids is separated into constituent products, such as ethane, propane, and butane
GAAP: U.S. generally accepted accounting principles
IDR: Incentive distribution right
LNG: Liquefied natural gas; natural gas which has been liquefied at cryogenic temperatures
MVC: Minimum volume commitment
NGLs: Natural gas liquids; natural gas liquids result from natural gas processing and crude oil refining and are used as petrochemical feedstocks, heating fuels, and gasoline additives, among other applications
NGL margins: NGL revenues less any applicable Btu replacement cost, plant fuel, and third-party transportation and fractionation
RGP Splitter: Refinery grade propylene splitter
Throughput: The volume of product transported or passing through a pipeline, plant, terminal, or other facility
WPZ Merger: The August 10, 2018 merger transactions pursuant to which we acquired all outstanding common units of WPZ held by others, merged WPZ into Williams, and Williams continued as the surviving entity

PART I – FINANCIAL INFORMATION

The Williams Companies, Inc.
Consolidated Statement of Income
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(Millions, except per-share amounts)			
Revenues:				
Service revenues	$1,371	$1,310	$4,062	$3,853
Service revenues – commodity consideration (Note 2)	121	—	316	—
Product sales	811	581	2,104	1,950
Total revenues	2,303	1,891	6,482	5,803
Costs and expenses:				
Product costs	790	504	2,039	1,620
Processing commodity expenses (Note 2)	30	—	91	—
Operating and maintenance expenses	389	403	1,134	1,166
Depreciation and amortization expenses	425	433	1,290	1,308
Selling, general, and administrative expenses	174	138	436	452
Gain on sale of Geismar Interest (Note 4)	—	(1,095)	—	(1,095)
Impairment of certain assets (Note 12)	—	1,210	66	1,236
Other (income) expense – net	(6)	24	24	34
Total costs and expenses	1,802	1,617	5,080	4,721
Operating income (loss)	501	274	1,402	1,082
Equity earnings (losses)	105	115	279	347
Other investing income (loss) – net (Note 5)	2	4	74	278
Interest incurred	(286)	(275)	(856)	(842)
Interest capitalized	16	8	38	24
Other income (expense) – net	52	23	99	124
Income (loss) before income taxes	390	149	1,036	1,013
Provision (benefit) for income taxes	190	24	297	126
Net income (loss)	200	125	739	887
Less: Net income (loss) attributable to noncontrolling interests	71	92	323	400
Net income (loss) attributable to The Williams Companies, Inc.	129	33	416	487
Preferred stock dividends (Note 11)	—	—	—	—
Net income (loss) available to common stockholders	$129	$33	$416	$487
Amounts attributable to The Williams Companies, Inc.:				
Basic earnings (loss) per common share:				
Net income (loss)	$.13	$.04	$.47	$.59
Weighted-average shares (thousands)	1,023,587	826,779	893,706	825,925
Diluted earnings (loss) per common share:				
Net income (loss)	$.13	$.04	$.46	$.59
Weighted-average shares (thousands)	1,026,504	829,368	896,322	828,150
Cash dividends declared per common share	$.34	$.30	$1.02	$.90

See accompanying notes.

6

The Williams Companies, Inc.
Consolidated Statement of Comprehensive Income
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(Millions)			
Net income (loss)	$200	$125	$739	$887
Other comprehensive income (loss):				
Cash flow hedging activities:				
Net unrealized gain (loss) from derivative instruments, net of taxes of $3 and $6 in 2018, and $2 and $1 in 2017	(5)	(9)	(19)	(5)
Reclassifications into earnings of net derivative instruments (gain) loss, net of taxes of ($2) and ($3) in 2018, and $1 and $1 in 2017	7	2	10	—
Pension and other postretirement benefits:				
Amortization of prior service cost (credit) included in net periodic benefit cost (credit), net of taxes of $1 and $2 in 2017	—	—	—	(2)
Net actuarial gain (loss) arising during the year, net of taxes of ($0) and ($1) in 2018	—	—	4	—
Amortization of actuarial (gain) loss and net actuarial loss from settlements included in net periodic benefit cost (credit), net of taxes of ($3) and ($5) in 2018, and ($2) and ($7) in 2017	4	4	14	13
Other comprehensive income (loss)	6	(3)	9	6
Comprehensive income (loss)	206	122	748	893
Less: Comprehensive income (loss) attributable to noncontrolling interests	72	89	321	398
Comprehensive income (loss) attributable to The Williams Companies, Inc.	$134	$33	$427	$495

See accompanying notes.

The Williams Companies, Inc.
Consolidated Balance Sheet
(Unaudited)

	September 30, 2018	December 31, 2017
	(Millions, except per-share amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	$42	$ 899
Trade accounts and other receivables (net of allowance of $9 at September 30, 2018 and $9 at December 31, 2017)	883	976
Inventories	153	113
Assets held for sale (Note 4)	664	7
Other current assets and deferred charges	242	184
Total current assets	1,984	2,179
Investments	7,427	6,552
Property, plant, and equipment	39,953	39,513
Accumulated depreciation and amortization	(11,279)	(11,302)
Property, plant, and equipment – net	28,674	28,211
Intangible assets – net of accumulated amortization	8,324	8,791
Regulatory assets, deferred charges, and other	744	619
Total assets	$47,153	$ 46,352
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	$739	$ 978
Liabilities held for sale (Note 4)	49	—
Accrued liabilities	1,117	1,167
Commercial paper	823	—
Long-term debt due within one year	33	501
Total current liabilities	2,761	2,646
Long-term debt	21,409	20,434
Deferred income tax liabilities	1,648	3,147
Regulatory liabilities, deferred income, and other	4,376	3,950
Contingent liabilities (Note 13)		
Equity:		
Stockholders' equity:		
Preferred stock (Note 11)	35	—
Common stock ($1 par value; 1,470 million shares authorized at September 30, 2018 and 960 million shares authorized at December 31, 2017; 1,245 million shares issued at September 30, 2018 and 861 million shares issued at December 31, 2017)	1,245	861
Capital in excess of par value	24,680	18,508
Retained deficit	(9,018)	(8,434)
Accumulated other comprehensive income (loss)	(291)	(238)
Treasury stock, at cost (35 million shares of common stock)	(1,041)	(1,041)
Total stockholders' equity	15,610	9,656
Noncontrolling interests in consolidated subsidiaries	1,349	6,519
Total equity	16,959	16,175
Total liabilities and equity	$47,153	$ 46,352

See accompanying notes.

The Williams Companies, Inc.
Consolidated Statement of Changes in Equity
(Unaudited)

	The Williams Companies, Inc., Stockholders								
	Preferred Stock	Common Stock	Capital in Excess of Par Value	Retained Deficit	AOCI*	Treasury Stock	Total Stockholders' Equity	Noncontrolling Interests	Total Equity
	(Millions)								
Balance – December 31, 2017	$—	$ 861	$ 18,508	$ (8,434)	$ (238)	$ (1,041)	$ 9,656	$ 6,519	$ 16,175
Adoption of ASC 606 (Note 1)	—	—	—	(84)	—	—	(84)	(37)	(121)
Adoption of ASU 2018-02 (Note 1)	—	—	—	61	(61)	—	—	—	—
Net income (loss)	—	—	—	416	—	—	416	323	739
Other comprehensive income (loss)	—	—	—	—	11	—	11	(2)	9
WPZ Merger (Note 1)	—	382	6,112	—	(3)	—	6,491	(4,629)	1,862
Issuance of preferred stock (Note 11)	35	—	—	—	—	—	35	—	35
Cash dividends – common stock	—	—	—	(974)	—	—	(974)	—	(974)
Dividends and distributions to noncontrolling interests	—	—	—	—	—	—	—	(598)	(598)
Stock-based compensation and related common stock issuances	—	1	48	—	—	—	49	—	49
Sales of limited partner units of Williams Partners L.P.	—	—	—	—	—	—	—	46	46
Changes in ownership of consolidated subsidiaries, net	—	—	14	—	—	—	14	(18)	(4)
Contributions from noncontrolling interests	—	—	—	—	—	—	—	13	13
Deconsolidation of subsidiary (Note 3)	—	—	—	—	—	—	—	(267)	(267)
Other	—	1	(2)	(3)	—	—	(4)	(1)	(5)
Net increase (decrease) in equity	35	384	6,172	(584)	(53)	—	5,954	(5,170)	784
Balance – September 30, 2018	$ 35	$ 1,245	$ 24,680	$ (9,018)	$ (291)	$ (1,041)	$ 15,610	$ 1,349	$ 16,959

* Accumulated Other Comprehensive Income (Loss)
See accompanying notes.

9

The Williams Companies, Inc.
Consolidated Statement of Cash Flows
(Unaudited)

	Nine Months Ended September 30,	
	2018	2017
	(Millions)	
OPERATING ACTIVITIES:		
Net income (loss)	$739	$887
Adjustments to reconcile to net cash provided (used) by operating activities:		
Depreciation and amortization	1,290	1,308
Provision (benefit) for deferred income taxes	351	99
Equity (earnings) losses	(279)	(347)
Distributions from unconsolidated affiliates	507	602
Net (gain) loss on disposition of equity-method investments	—	(269)
Gain on sale of Geismar Interest (Note 4)	—	(1,095)
Impairment of and net (gain) loss on sale of assets	64	1,225
Amortization of stock-based awards	43	61
Cash provided (used) by changes in current assets and liabilities:		
Accounts and notes receivable	75	118
Inventories	(39)	(23)
Other current assets and deferred charges	(44)	(11)
Accounts payable	(76)	47
Accrued liabilities	(62)	(161)
Other, including changes in noncurrent assets and liabilities	(238)	(210)
Net cash provided (used) by operating activities	2,331	2,231
FINANCING ACTIVITIES:		
Proceeds from (payments of) commercial paper – net	821	(93)
Proceeds from long-term debt	3,745	3,013
Payments of long-term debt	(3,201)	(5,475)
Proceeds from issuance of common stock	15	2,130
Common dividends paid	(974)	(744)
Dividends and distributions paid to noncontrolling interests	(552)	(636)
Contributions from noncontrolling interests	13	15
Payments for debt issuance costs	(26)	(14)
Other – net	(46)	(87)
Net cash provided (used) by financing activities	(205)	(1,891)
INVESTING ACTIVITIES:		
Property, plant, and equipment:		
Capital expenditures (1)	(2,659)	(1,700)
Dispositions – net	(2)	(27)
Contributions in aid of construction	395	253
Proceeds from sale of businesses, net of cash divested	—	2,056
Proceeds from dispositions of equity-method investments	—	200
Purchases of and contributions to equity-method investments	(803)	(103)
Other – net	86	(17)
Net cash provided (used) by investing activities	(2,983)	662
Increase (decrease) in cash and cash equivalents	(857)	1,002

Cash and cash equivalents at beginning of year	899	170
Cash and cash equivalents at end of period	$42	$1,172

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(1) Increases to property, plant, and equipment	$(2,482)	$(1,826)
Changes in related accounts payable and accrued liabilities	(177)	126
Capital expenditures	$(2,659)	$(1,700)

See accompanying notes.

The Williams Companies, Inc.
Notes to Consolidated Financial Statements
(Unaudited)

Note 1 – General, Description of Business, and Basis of Presentation

General

Our accompanying interim consolidated financial statements do not include all the notes in our annual financial statements and, therefore, should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2017, in Exhibit 99.1 of our Form 8-K dated May 3, 2018. The accompanying unaudited financial statements include all normal recurring adjustments and others that, in the opinion of management, are necessary to present fairly our interim financial statements.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

Unless the context clearly indicates otherwise, references in this report to “Williams,” “we,” “our,” “us,” or like terms refer to The Williams Companies, Inc. and its subsidiaries. Unless the context clearly indicates otherwise, references to “Williams,” “we,” “our,” and “us” include the operations in which we own interests accounted for as equity-method investments that are not consolidated in our financial statements. When we refer to our equity investees by name, we are referring exclusively to their businesses and operations.

WPZ Merger

On August 10, 2018, we completed our merger with Williams Partners L.P. (WPZ), pursuant to which we acquired all of the approximately 256 million publicly held outstanding common units of WPZ in exchange for 382 million shares of our common stock (WPZ Merger). Williams continued as the surviving entity. The WPZ Merger was accounted for as a non-cash equity transaction resulting in increases to Common stock of $382 million, Capital in excess of par value of $6.112 billion, and Regulatory assets, deferred charges, and other of $33 million and decreases to Accumulated other comprehensive income (loss) of $3 million, Noncontrolling interests in consolidated subsidiaries of $4.629 billion, and Deferred income tax liabilities of $1.829 billion in the Consolidated Balance Sheet. Prior to the completion of the WPZ Merger and pursuant to its distribution reinvestment program, WPZ had issued 1,230,657 common units to the public in 2018 associated with reinvested distributions of $46 million.

Financial Repositioning

In January 2017, we entered into agreements with WPZ, wherein we permanently waived the general partner’s incentive distribution rights and converted our 2 percent general partner interest in WPZ to a noneconomic interest in exchange for 289 million newly issued WPZ common units. Pursuant to this agreement, we also purchased approximately 277 thousand WPZ common units for $10 million. Additionally, we purchased approximately 59 million common units of WPZ at a price of $36.08586 per unit in a private placement transaction, funded with proceeds from our equity offering. According to the terms of this agreement, concurrent with WPZ’s quarterly distributions in February 2017 and May 2017, we paid additional consideration totaling $56 million to WPZ for these units.

Description of Business

We are a Delaware corporation whose common stock is listed and traded on the New York Stock Exchange. Our operations are located principally in the United States. Prior to the WPZ Merger, we had one reportable segment, Williams Partners. Beginning in the third-quarter 2018, consistent with the manner in which our chief operating decision maker evaluates performance and allocates resources, our operations are now presented within the following reportable segments: Northeast G&P, Atlantic-Gulf, and West. Prior period segment disclosures have been recast for the new segment presentation.

Notes (Continued)

Northeast G&P is comprised of our midstream gathering and processing businesses in the Marcellus Shale region primarily in Pennsylvania, New York, and West Virginia and the Utica Shale region of eastern Ohio, as well as a 66 percent interest in Cardinal Gas Services, L.L.C. (Cardinal) (a consolidated entity), a 62 percent equity-method investment in Utica East Ohio Midstream, LLC, a 69 percent equity-method investment in Laurel Mountain Midstream, LLC, a 58 percent equity-method investment in Caiman Energy II, LLC, and Appalachia Midstream Services, LLC, which owns equity-method investments with an approximate average 66 percent interest in multiple gathering systems in the Marcellus Shale (Appalachia Midstream Investments).

Atlantic-Gulf is comprised of our interstate natural gas pipeline, Transcontinental Gas Pipe Line Company, LLC (Transco), and significant natural gas gathering and processing and crude oil production handling and transportation assets in the Gulf Coast region, including a 51 percent interest in Gulfstar One LLC (Gulfstar One) (a consolidated entity), which is a proprietary floating production system, and various petrochemical and feedstock pipelines in the Gulf Coast region, as well as a 50 percent equity-method investment in Gulfstream Natural Gas System, L.L.C., a 41 percent interest in Constitution Pipeline Company, LLC (Constitution) (a consolidated entity), which is developing a pipeline project (see Note 3 – Variable Interest Entities), and a 60 percent equity-method investment in Discovery Producer Services LLC.

West is comprised of our interstate natural gas pipeline, Northwest Pipeline LLC (Northwest Pipeline), and our gathering, processing, and treating operations in New Mexico, Colorado, and Wyoming, as well as the Barnett Shale region of north-central Texas, the Eagle Ford Shale region of south Texas, the Haynesville Shale region of northwest Louisiana, and the Mid-Continent region which includes the Anadarko, Arkoma, Delaware, and Permian basins. This segment also includes our natural gas liquid (NGL) and natural gas marketing business, storage facilities, an undivided 50 percent interest in an NGL fractionator near Conway, Kansas, and a 50 percent equity-method investment in Overland Pass Pipeline, LLC, a 50 percent interest in Jackalope Gas Gathering Services, L.L.C. (Jackalope) (an equity-method investment following deconsolidation as of June 30, 2018), a 43 percent equity-method investment in Rocky Mountain Midstream Holdings LLC (RMM), and our previously owned 50 percent equity-method investment in the Delaware basin gas gathering system (DBJV) in the Mid-Continent region (see Note 5 – Investing Activities).

All remaining business activities, including our former Williams Olefins, L.L.C., a wholly owned subsidiary which owned our 88.5 percent undivided interest in the Geismar, Louisiana, olefins plant (Geismar Interest) (see Note 4 – Divestitures and Assets Held for Sale), as well as corporate activities, are included in Other.

Basis of Presentation

Significant risks and uncertainties

We may monetize assets that are not core to our strategy which could result in impairments of certain equity-method investments, property, plant, and equipment, and intangible assets. Such impairments could potentially be caused by indications of fair value implied through the monetization process or, in the case of asset dispositions that are part of a broader asset group, the impact of the loss of future estimated cash flows.

Proposition 112

On November 6, 2018, citizens of Colorado will vote on Proposition 112, a ballot measure that could significantly increase setback distances from occupied structures or other vulnerable areas, as defined or designated, for any new oil and gas development in the state, critically restricting or banning such activities. If the measure is approved, it could still be subject to modification or amendment by the Colorado legislature. An unfavorable outcome could adversely impact the operations, and ultimately the value, of our businesses and investments in Colorado, notably our recent investment in RMM (see Note 5 – Investing Activities).

FERC Income Tax Policy Revision

On March 15, 2018, the Federal Energy Regulatory Commission (FERC) issued a revised policy statement (the March 15 Statement) regarding the recovery of income tax costs in rates of natural gas pipelines. The FERC found that an impermissible double recovery results from granting a Master Limited Partnership (MLP) pipeline

12

Notes (Continued)

both an income tax allowance and a return on equity pursuant to the discounted cash flow methodology. As a result, the FERC will no longer permit an MLP pipeline to recover an income tax allowance in its cost of service. The FERC further stated it will address the application of this policy to non-MLP partnership forms as those issues arise in subsequent proceedings. One of the benefits of the recent WPZ Merger is to allow our FERC-regulated pipelines to continue to recover an income tax allowance in their cost of service rates.

On July 18, 2018, the FERC issued an order dismissing the requests for rehearing and clarification of the revised policy statement. In addition, the FERC provided guidance that an MLP pipeline (or other pass-through entity) no longer recovering an income tax allowance pursuant to the revised policy may eliminate previously accumulated deferred income taxes (ADIT) from its cost of service instead of flowing these ADIT balances to ratepayers. This guidance, if implemented, would significantly mitigate the impact of the March 15 Statement. However, the FERC stated that the revised policy statement and such guidance do not establish a binding rule but are instead expressions of general policy intent designed to provide guidance by notifying entities of the course of action the FERC intends to follow in future adjudications. To the extent the FERC addresses these issues in future proceedings, it will consider any arguments regarding not only the application of the revised policy to the facts of the case, but also any arguments regarding the underlying validity of the policy itself. The FERC's guidance on ADIT likely will be challenged by customers and state commissions, which would result in a long period of revenue uncertainty for pipelines eliminating ADIT from their cost of service. The WPZ Merger has the additional benefit of eliminating this uncertainty.

On March 15, 2018, the FERC also issued a Notice of Proposed Rulemaking proposing a filing process that will allow it to determine which natural gas pipelines may be collecting unjust and unreasonable rates in light of the recent reduction in the corporate income tax rate in the Tax Cuts and Jobs Act (Tax Reform) and the revised policy statement. On July 18, 2018, the FERC issued a Final Rule, retaining the filing requirement and reaffirming the options that pipelines have to either reflect the reduced tax rate or explain why no rate change is necessary. The FERC also clarified that a natural gas company organized as a pass-through entity and all of whose income or losses are consolidated on the federal income tax return of its corporate parent is considered to be subject to the federal corporate income tax and is thus eligible for a tax allowance. We believe this Final Rule and the previously discussed WPZ Merger allow for the continued recovery of income tax allowances in Transco's and Northwest Pipeline's rates. Further, Transco's August 31, 2018 general rate case filing reflects a tax allowance based on this clarification, and the FERC's September 28, 2018 order in the rate case proceeding finds that Transco is exempt from the Final Rule's Form 501-G filing requirement. In addition, on October 19, 2018, Northwest Pipeline filed a petition requesting that the FERC waive its Form 501-G filing requirement under this Final Rule because the reduction in the corporate income tax in Tax Reform is already addressed in its settlement.

On March 15, 2018, the FERC also issued a Notice of Inquiry seeking comments on the additional impacts of Tax Reform on jurisdictional rates, particularly whether, and if so how, the FERC should address changes relating to ADIT amounts after the corporate income tax rate reduction and bonus depreciation rules, as well as whether other features of Tax Reform require FERC action. We are evaluating the impact of these developments on our interstate natural gas pipelines and currently expect any associated impacts would be prospective and determined through subsequent rate proceedings. We also continue to monitor developments that may impact our regulatory liabilities resulting from Tax Reform. It is reasonably possible that future tariff-based rates collected by our interstate natural gas pipelines may be adversely impacted.

Accounting standards issued and adopted

During the first quarter of 2018, we early adopted Accounting Standards Update (ASU) 2018-02 "Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income" (ASU 2018-02). As a result of Tax Reform lowering the federal income tax rate, the tax effects of items within accumulated other comprehensive income may not reflect the appropriate tax rate. ASU 2018-02 allows for the reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from Tax Reform. The adoption of ASU 2018-02 resulted in the reclassification of $61

million from Accumulated other comprehensive income (loss) to Retained deficit on our Consolidated Balance Sheet.

Notes (Continued)

Effective January 1, 2018, we adopted ASU 2017-12 “Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities” (ASU 2017-12). ASU 2017-12 applies to entities that elect hedge accounting in accordance with Accounting Standards Codification (ASC) 815. The ASU affects both the designation and measurement guidance for hedging relationships and the presentation of hedging results. ASU 2017-12 was applied using a modified retrospective approach for cash flow and net investment hedges existing at the date of adoption and prospectively for the presentation and disclosure guidance. The adoption of ASU 2017-12 did not have a significant impact on our consolidated financial statements.

Effective January 1, 2018, we adopted ASU 2017-07 “Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost” (ASU 2017-07). ASU 2017-07 requires employers to report the service cost component of net benefit cost in the same line item or items as other compensation costs arising from employee services. The other components of net benefit cost must be presented in the income statement separately from the service cost component and outside Operating income (loss). Only the service cost component is now eligible for capitalization when applicable. The presentation aspect of ASU 2017-07 must be applied retrospectively and the capitalization requirement prospectively. In accordance with this adoption, we have conformed the prior year presentation, which resulted in increases of $3 million and $9 million to Operating and maintenance expenses with corresponding decreases to Operating income (loss) and increases of $3 million and $9 million to Other income (expense) – net below Operating income (loss) in the Consolidated Statement of Income for the three- and nine-month periods ended September 30, 2017, respectively.

Effective January 1, 2018, we adopted ASU 2016-15 “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments” (ASU 2016-15). Among other things, ASU 2016-15 permits an accounting policy election to classify distributions received from equity-method investees using either the cumulative earnings approach or the nature of distribution approach. We have elected to apply the nature of distribution approach and have retrospectively conformed the prior year presentation within the Consolidated Statement of Cash Flows in accordance with ASU 2016-15. For the period ended September 30, 2017, amounts previously presented as Distributions from unconsolidated affiliates in excess of cumulative earnings within Investing Activities are now presented as part of Distributions from unconsolidated affiliates within Operating Activities, resulting in an increase to Net cash provided (used) by operating activities of $394 million with a corresponding reduction in Net cash provided (used) by investing activities.

In May 2014, the Financial Accounting Standards Board (FASB) issued ASU 2014-09 establishing ASC Topic 606, “Revenue from Contracts with Customers” (ASC 606). ASC 606 establishes a comprehensive new revenue recognition model designed to depict the transfer of goods or services to a customer in an amount that reflects the consideration the entity expects to be entitled to receive in exchange for those goods or services and requires significantly enhanced revenue disclosures. In August 2015, the FASB issued ASU 2015-14 “Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date” (ASU 2015-14). Per ASU 2015-14, the standard became effective for interim and annual reporting periods beginning after December 15, 2017.

We adopted the provisions of ASC 606 effective January 1, 2018, utilizing the modified retrospective transition method for all contracts with customers, which included applying the provisions of ASC 606 beginning January 1, 2018, to all contracts not completed as of that date with the cumulative effect of applying the standard for periods prior to January 1, 2018, as an adjustment to Total equity, net of tax, upon adoption. As a result of our adoption, the cumulative impact to our Total equity, net of tax, at January 1, 2018, was a decrease of $121 million in the Consolidated Balance Sheet.

For each revenue contract type, we conducted a formal contract review process to evaluate the impact of ASC 606. The adjustment to Total equity upon adoption of ASC 606 is primarily comprised of the impact to the timing of recognition of deferred revenue (contract liabilities) associated with certain contracts which underwent modifications in periods prior to January 1, 2018. Under the provisions of ASC 606, when a contract modification does not increase both the scope and price of the contract, and the remaining goods and services are distinct from the goods and services

transferred prior to the modification, the modification is treated as a termination of the existing contract and the creation of a new contract. ASC 606 requires that the transaction price, including any remaining contract liabilities from the old contract, be allocated to the performance obligations over the term of the new contract. The contract modification adjustments are partially offset by the impact of changes to the timing of recognizing revenue which is subject to the constraint on

estimates of variable consideration of certain contracts. The constraint of variable consideration will result in the acceleration of revenue recognition and corresponding de-recognition of contract liabilities for certain contracts (as compared to the previous revenue recognition model) as a result of our assessment that it is probable such recognition would not result in a significant revenue reversal in the future. Additionally, under ASC 606, our revenues will increase in situations where we receive noncash consideration, which exists primarily in certain of our gas processing contracts where we receive commodities as full or partial consideration for services provided. This increase in revenues will be offset by a similar increase in costs and expenses when the commodities received are subsequently sold. Financial systems and internal controls necessary for adoption were implemented effective January 1, 2018. (See Note 2 – Revenue Recognition.)

Accounting standards issued but not yet adopted

In June 2016, the FASB issued ASU 2016-13 “Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments” (ASU 2016-13). ASU 2016-13 changes the impairment model for most financial assets and certain other instruments. For trade and other receivables, held-to-maturity debt securities, loans, and other instruments, entities will be required to use a new forward-looking “expected loss” model that generally will result in the earlier recognition of allowances for losses. The guidance also requires increased disclosures. ASU 2016-13 is effective for interim and annual periods beginning after December 15, 2019. Early adoption is permitted. The standard requires varying transition methods for the different categories of amendments. Although we do not expect ASU 2016-13 to have a significant impact, it could impact our trade receivables as the related allowance for credit losses will be recognized earlier under the expected loss model.

In February 2016, the FASB issued ASU 2016-02 “Leases (Topic 842)” (ASU 2016-02). ASU 2016-02 establishes a comprehensive new lease accounting model. ASU 2016-02 modifies the definition of a lease, requires a dual approach to lease classification similar to current lease accounting, and causes lessees to recognize operating leases on the balance sheet as a lease liability measured as the present value of the future lease payments with a corresponding right-of-use asset, with an exception for leases with a term of one year or less. Additional disclosures will also be required regarding the amount, timing, and uncertainty of cash flows arising from leases. In January 2018, the FASB issued ASU 2018-01 “Leases (Topic 842): Land Easement Practical Expedient for Transition to Topic 842” (ASU 2018-01). Per ASU 2018-01, land easements and rights-of-way are required to be assessed under ASU 2016-02 to determine whether the arrangements are or contain a lease. ASU 2018-01 permits an entity to elect a transition practical expedient to not apply ASU 2016-02 to land easements that exist or expired before the effective date of ASU 2016-02 and that were not previously assessed under the previous lease guidance in ASC Topic 840 “Leases.”

In July 2018, the FASB issued ASU 2018-11 “Leases (Topic 842): Targeted Improvements” (ASU 2018-11). Prior to ASU 2018-11, a modified retrospective transition was required for financing or operating leases existing at or entered into after the beginning of the earliest comparative period presented in the financial statements. ASU 2018-11 allows entities an additional transition method to the existing requirements whereby an entity could adopt the provisions of ASU 2016-02 by recognizing a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption without adjustment to the financial statements for periods prior to adoption. ASU 2018-11 also allows a practical expedient that permits lessors to not separate non-lease components from the associated lease component if certain conditions are present. ASU 2016-02 is effective for interim and annual periods beginning after December 15, 2018. Early adoption is permitted. We will adopt ASU 2016-02 effective January 1, 2019.

We are in the process of finalizing our review of contracts to identify leases based on the modified definition of a lease and identifying changes to our internal controls to support management in the accounting for and disclosure of leasing activities upon adoption of ASU 2016-02. We implemented a financial lease accounting system to assist management in the accounting for leases upon adoption. While we are still in the process of completing our implementation evaluation of ASU 2016-02, we currently believe the most significant changes to our financial statements relate to the recognition of a lease liability and offsetting right-of-use asset in our Consolidated Balance Sheet for operating leases. We are also evaluating ASU 2016-02’s available practical expedients on adoption, which

we generally expect to elect.

Notes (Continued)

Note 2 – Revenue Recognition

Customers in our gas pipeline businesses are comprised of public utilities, municipalities, gas marketers and producers, intrastate pipelines, direct industrial users, and electrical generators. Customers in our midstream businesses are comprised of oil and natural gas producer counterparties. Customers for our product sales are comprised of public utilities, gas marketers, and direct industrial users.

A performance obligation is a promise in a contract to transfer a distinct good or service (or integrated package of goods or services) to the customer. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue, when, or as, the performance obligation is satisfied. A performance obligation is distinct if the service is separately identifiable from other items in the integrated package of services and if a customer can benefit from it on its own or with other resources that are readily available to the customer. An integrated package of services typically represents a single performance obligation if the services are contained within the same contract or within multiple contracts entered into in contemplation with one another that are highly interdependent or highly interrelated, meaning each of the services is significantly affected by one or more of the other services in the contract. Service revenue contracts from our gas pipeline and midstream businesses contain a series of distinct services, with the majority of our contracts having a single performance obligation that is satisfied over time as the customer simultaneously receives and consumes the benefits provided by our performance. Most of our product sales contracts have a single performance obligation with revenue recognized at a point in time when the products have been sold and delivered to the customer.

Certain customers reimburse us for costs we incur associated with construction of property, plant, and equipment utilized in our operations. For our rate-regulated gas pipeline businesses that apply ASC 980. "Regulated Operations" (Topic 980), we follow FERC guidelines with respect to reimbursement of construction costs. FERC tariffs only allow for cost reimbursement and are non-negotiable in nature; thus, the construction activities do not represent an ongoing major and central operation of our gas pipeline businesses and are not within the scope of ASC 606. Accordingly, cost reimbursements are treated as a reduction to the cost of the constructed asset. For our midstream businesses, reimbursement and service contracts with customers are viewed together as providing the same commercial objective, as we have the ability to negotiate the mix of consideration between reimbursements and amounts billed over time. Accordingly, we generally re