NISOURCE INC/DE
Form 10-Q
May 04, 2007

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended March 31, 2007
or

o **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 001-16189
NiSource Inc.
(Exact name of registrant as specified in its charter)

Delaware	35-2108964
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
801 East 86th Avenue Merrillville, Indiana	46410
(Address of principal executive offices)	(Zip Code)

(877) 647-5990
(Registrant s telephone number, including area code)

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 o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.
Large accelerated filerþ Accelerated filer o Non-accelerated filer o
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes o No þ
Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date: Common Stock, $0.01 Par Value: 274,066,018 outstanding at April 30, 2007.

NISOURCE INC.
FORM 10-Q QUARTERLY REPORT
FOR THE QUARTER ENDED MARCH 31, 2007
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DEFINED TERMS

The following is a list of frequently used abbreviations or acronyms that are found in this report:

NiSource Subsidiaries and Affiliates

Bay State	Bay State Gas Company
Capital Markets	NiSource Capital Markets, Inc.
CER	Columbia Energy Resources, Inc.
CNR	Columbia Natural Resources, Inc.
Columbia	Columbia Energy Group
Columbia Deep Water	Columbia Deep Water Service Company
Columbia Energy Services	Columbia Energy Services Corporation
Columbia Gulf	Columbia Gulf Transmission Company
Columbia of Kentucky	Columbia Gas of Kentucky, Inc.
Columbia of Maryland	Columbia Gas of Maryland, Inc.
Columbia of Ohio	Columbia Gas of Ohio, Inc.
Columbia of Pennsylvania	Columbia Gas of Pennsylvania, Inc.
Columbia of Virginia	Columbia Gas of Virginia, Inc.
Columbia Transmission	Columbia Gas Transmission Corporation
CORC	Columbia of Ohio Receivables Corporation
Crossroads Pipeline	Crossroads Pipeline Company
Granite State Gas	Granite State Gas Transmission, Inc.
Hardy Storage	Hardy Storage Company, L.L.C.
Kokomo Gas	Kokomo Gas and Fuel Company
Lake Erie Land	Lake Erie Land Company
Millennium	Millennium Pipeline Company, L.P.
NDC Douglas Properties	NDC Douglas Properties, Inc.
NiSource	NiSource Inc.
NiSource Corporate Services	NiSource Corporate Services Company
NiSource Development Company	NiSource Development Company, Inc.
NiSource Finance	NiSource Finance Corp.
Northern Indiana	Northern Indiana Public Service Company
Northern Indiana Fuel and Light	Northern Indiana Fuel and Light Company
Northern Utilities	Northern Utilities, Inc.
NRC	NIPSCO Receivables Corporation
PEI	PEI Holdings, Inc.
TPC	EnergyUSA-TPC Corp.
Transcom	Columbia Transmission Communications Corporation
Whiting Clean Energy	Whiting Clean Energy, Inc.
Whiting Leasing	Whiting Leasing LLC

Abbreviations

AFUDC	Allowance for funds used during construction
APB No. 25	Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees
BBA	British Banker Association
Bcf	Billion cubic feet
Board	Board of Directors
BP	BP Amoco p.l.c.
CAIR	Clean Air Interstate Rule

CAMR	Clean Air Mercury Rule
Day 2	Began April 1, 2005 and refers to the operational control of the energy markets by MISO, including the dispatching of wholesale electricity and generation, managing transmission constraints, and managing the day-ahead, real-time and financial transmission rights markets
DOT	United States Department of Transportation
Dth	dekatherms
ECRM	Environmental Cost Recovery Mechanism

DEFINED TERMS (continued)

ECT	Environmental cost tracker
EER	Environmental Expense Recovery
EERM	Environmental Expense Recovery Mechanism
Empire	Empire State Pipeline
EPA	United States Environmental Protection Agency
EPS	Earnings per share
ESA	Energy Sales Agreement
FAC	Fuel adjustment clause
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
FIN 47	FASB Interpretation No. 47, Accounting for Conditional Asset Retirement Obligations
FIN 48	FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an interpretation of SFAS No. 109
FIP	federal implementation plan
FTRs	Financial Transmission Rights
gwh	Gigawatt hours
IBM	International Business Machines Corp.
IDEM	Indiana Department of Environmental Management
IURC	Indiana Utility Regulatory Commission
LDCs	Local distribution companies
LIBOR	London InterBank Offered Rate
MISO	Midwest Independent Transmission System Operator
Mitchell Station	Dean H. Mitchell Generating Station
MMDth	Million dekatherms
mw	Megawatts
NAAQS	National Ambient Air Quality Standards
NOx	Nitrogen oxide
NYMEX	New York Mercantile Exchange
OUCC	Indiana Office of Utility Consumer Counselor
PCB	Polychlorinated biphenyls
Piedmont	Piedmont Natural Gas Company, Inc.
PPS	Price Protection Service
PUCO	Public Utilities Commission of Ohio
SEC	Securities and Exchange Commission
SFAS	Statement of Financial Accounting Standards
SFAS No. 71	Statement of Financial Accounting Standards No. 71, Accounting for the Effects of Certain Types of Regulation
SFAS No. 123	Statement of Financial Accounting Standards No. 123, Share-Based Payment
SFAS No. 123R	Statement of Financial Accounting Standards No. 123R, Share-Based Payment
SFAS No. 133	Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities, as amended
SFAS No. 143	Statement of Financial Accounting Standards No. 143, Accounting for Asset Retirement Obligations

SFAS No. 157	Statement of Financial Accounting Standards No. 157, Fair Value Measurements
SFAS No. 158	Statement of Financial Accounting Standards No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans
SFAS No. 159	Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115
SIP	State Implementation Plan
SO2	Sulfur dioxide
VaR	Value-at-risk and instrument sensitivity to market factors

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PART I

ITEM 1. FINANCIAL STATEMENTS

NiSource Inc.

Statements of Consolidated Income (unaudited)

Three Months Ended March 31, *(in millions, except per share amounts)*	**2007**	2006
Net Revenues		
Gas Distribution	**$ 1,899.3**	$ 1,998.2
Gas Transportation and Storage	**347.8**	320.6
Electric	**325.9**	305.7
Other	**320.7**	348.0
Gross Revenues	**2,893.7**	2,972.5
Cost of Sales (excluding depreciation and amortization)	**1,831.2**	1,991.7
Total Net Revenues	**1,062.5**	980.8
Operating Expenses		
Operation and maintenance	**385.9**	372.3
Depreciation and amortization	**139.0**	136.8
Impairment and gain on sale of assets	**2.9**	0.9
Other taxes	**101.6**	103.0
Total Operating Expenses	**629.4**	613.0
Equity Earnings (Loss) in Unconsolidated Affiliates	**1.5**	(0.2)
Operating Income	**434.6**	367.6
Other Income (Deductions)		
Interest expense, net	**(98.6)**	(95.3)
Dividend requirement on preferred stock of subsidiaries		(1.1)
Other, net	**(2.8)**	(3.4)
Total Other Income (Deductions)	**(101.4)**	(99.8)
Income From Continuing Operations Before Income Taxes and Cumulative Effect of Change in Accounting Principle	**333.2**	267.8
Income Taxes	**124.1**	94.8
Income from Continuing Operations Before Cumulative Effect of Change in Accounting Principle	**209.1**	173.0
Income (Loss) from Discontinued Operations net of taxes	**1.0**	(0.5)
Gain on Disposition of Discontinued Operations net of taxes	**6.6**	
Income Before Change in Accounting Principle	**216.7**	172.5

Cumulative Effect of Change in Accounting Principle net of taxes				0.4
Net Income	**$**	**216.7**	$	172.9
Basic Earnings Per Share ($)				
Continuing operations	**$**	**0.76**	$	0.63
Discontinued operations		**0.03**		
Basic Earnings Per Share	**$**	**0.79**	$	0.63
Diluted Earnings Per Share ($)				
Continuing operations	**$**	**0.76**	$	0.63
Discontinued operations		**0.03**		
Diluted Earnings Per Share	**$**	**0.79**	$	0.63
Dividends Declared Per Common Share	**$**	**0.46**	$	0.46
Basic Average Common Shares Outstanding (millions)		**273.6**		272.3
Diluted Average Common Shares (millions)		**274.8**		273.1

The accompanying Notes to Consolidated Financial Statements are an integral part of these unaudited statements.

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ITEM 1. FINANCIAL STATEMENTS (continued)
NiSource Inc.
Condensed Consolidated Balance Sheets (unaudited)

(in millions)	**March 31, 2007**	December 31, 2006
ASSETS		
Property, Plant and Equipment		
Utility Plant	**$ 17,333.8**	$ 17,194.9
Accumulated depreciation and amortization	**(7,939.8)**	(7,850.0)
Net utility plant	**9,394.0**	9,344.9
Other property, at cost, less accumulated depreciation	**346.9**	349.6
Net Property, Plant and Equipment	**9,740.9**	9,694.5
Investments and Other Assets		
Assets of discontinued operations and assets held for sale	**36.5**	43.0
Unconsolidated affiliates	**66.1**	59.6
Other investments	**112.3**	116.1
Total Investments and Other Assets	**214.9**	218.7
Current Assets		
Cash and cash equivalents	**102.2**	33.1
Restricted cash	**61.2**	142.5
Accounts receivable (less reserve of $64.8 and $42.1, respectively)	**954.0**	866.3
Gas inventory	**96.5**	550.5
Underrecovered gas and fuel costs	**195.6**	163.2
Materials and supplies, at average cost	**89.7**	89.0
Electric production fuel, at average cost	**62.3**	63.9
Price risk management assets	**128.6**	237.7
Exchange gas receivable	**274.0**	252.3
Regulatory assets	**210.0**	272.7
Prepayments and other	**87.2**	111.7
Total Current Assets	**2,261.3**	2,782.9
Other Assets		
Price risk management assets	**36.4**	49.9
Regulatory assets	**1,030.0**	1,127.3
Goodwill	**3,677.3**	3,677.3

Intangible assets	**432.3**	435.7
Deferred charges and other	**162.1**	170.2
Total Other Assets	**5,338.1**	5,460.4
Total Assets	**$ 17,555.2**	$ 18,156.5

The accompanying Notes to Consolidated Financial Statements are an integral part of these unaudited statements.

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Condensed Consolidated Balance Sheets (unaudited) (continued)

(in millions, except share amounts)	**March 31, 2007**	December 31, 2006
CAPITALIZATION AND LIABILITIES		
Capitalization		
Common Stockholders Equity		
Common stock $0.01 par value, 400,000,000 shares authorized; 273,919,093 and 273,654,180 shares issued and outstanding, respectively	$ **2.7**	$ 2.7
Additional paid-in capital	**4,001.1**	3,998.3
Retained earnings	**1,096.0**	1,012.9
Accumulated other comprehensive income	**50.2**	20.9
Treasury stock	**(22.7)**	(21.2)
Total Common Stockholders Equity	**5,127.3**	5,013.6
Long-term debt, excluding amounts due within one year	**5,153.1**	5,146.2
Total Capitalization	**10,280.4**	10,159.8
Current Liabilities		
Current portion of long-term debt	**90.1**	93.3
Short-term borrowings	**620.0**	1,193.0
Accounts payable	**659.5**	713.1
Dividends declared	**63.1**	
Customer deposits	**110.4**	108.4
Taxes accrued	**335.0**	196.0
Interest accrued	**101.2**	107.1
Overrecovered gas and fuel costs	**63.3**	126.7
Price risk management liabilities	**35.4**	259.4
Exchange gas payable	**361.7**	396.6
Deferred revenue	**39.3**	55.9
Regulatory liabilities	**42.6**	40.7
Accrued liability for postretirement and postemployment benefits	**4.7**	4.7
Other accruals	**696.1**	526.3
Total Current Liabilities	**3,222.4**	3,821.2
Other Liabilities and Deferred Credits		
Price risk management liabilities	**22.5**	38.2
Deferred income taxes	**1,544.9**	1,553.7
Deferred investment tax credits	**59.5**	61.5
Deferred credits	**117.0**	119.3

Deferred revenue	**22.0**	21.9
Accrued liability for postretirement and postemployment benefits	**654.9**	799.5
Liabilities of discontinued operations and liabilities held for sale	**9.8**	11.9
Regulatory liabilities and other removal costs	**1,293.4**	1,253.8
Asset retirement obligations	**133.3**	131.6
Other noncurrent liabilities	**195.1**	184.1
Total Other Liabilities and Deferred Credits	**4,052.4**	4,175.5
Commitments and Contingencies		
Total Capitalization and Liabilities	**$ 17,555.2**	$ 18,156.5

The accompanying Notes to Consolidated Financial Statements are an integral part of these unaudited statements.

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Statements of Consolidated Cash Flows (unaudited)

Three Months Ended March 31, *(in millions)*	**2007**	2006
Operating Activities		
Net income	**$ 216.7**	$ 172.9
Adjustments to reconcile net income to net cash from continuing operations:		
Depreciation and amortization	**139.0**	136.8
Net changes in price risk management assets and liabilities	**5.5**	10.2
Deferred income taxes and investment tax credits	**1.6**	(40.5)
Deferred revenue	**(16.5)**	(26.0)
Stock compensation expense	**1.1**	1.3
Gain on sale of assets	**(0.3)**	(1.6)
Loss on impairment of assets	**3.2**	2.5
Cumulative effect of change in accounting principle, net of taxes		(0.4)
Income from unconsolidated affiliates	**(3.3)**	(1.0)
Gain on disposition of discontinued operations net of taxes	**(6.6)**	
Loss (Income) from discontinued operations net of taxes	**(1.0)**	0.5
Amortization of discount/premium on debt	**1.8**	2.0
AFUDC Equity	**(0.8)**	
Changes in assets and liabilities:		
Accounts receivable	**(103.2)**	110.2
Inventories	**707.2**	442.1
Accounts payable	**(34.3)**	(340.6)
Customer deposits	**2.0**	2.7
Taxes accrued	**129.8**	151.6
Interest accrued	**(0.7)**	19.1
(Under) Overrecovered gas and fuel costs	**(95.8)**	319.7
Exchange gas receivable/payable	**(60.3)**	(126.0)
Other accruals	**(97.2)**	(81.2)
Prepayments and other current assets	**24.5**	9.9
Regulatory assets/liabilities	**18.7**	(19.1)
Postretirement and postemployment benefits	**(57.7)**	(6.0)
Deferred credits	**(3.0)**	2.3
Deferred charges and other noncurrent assets	**2.0**	(5.2)
Other noncurrent liabilities	**7.2**	(7.3)
Net Operating Activities from Continuing Operations	**779.6**	728.9
Net Operating Activities from Discontinued Operations	**0.4**	0.1
Net Cash Flows from Operating Activities	**780.0**	729.0
Investing Activities		
Capital expenditures	**(152.1)**	(123.2)
Proceeds from disposition of assets	**1.5**	3.9
Restricted cash	**81.3**	(21.8)
Other investing activities	**(2.9)**	12.9

Net Cash Flows used for Investing Activities	**(72.2)**	(128.2)
Financing Activities		
Retirement of long-term debt	**(4.1)**	(0.5)
Change in short-term debt	**(572.2)**	(518.7)
Issuance of common stock	**2.1**	1.0
Acquisition of treasury stock	**(1.5)**	(5.9)
Dividends paid common stock	**(63.0)**	(62.7)
Net Cash Flows used for Financing Activities	**(638.7)**	(586.8)
Increase in cash and cash equivalents	**69.1**	14.0
Cash and cash equivalents at beginning of year	**33.1**	69.4
Cash and cash equivalents at end of period	**$ 102.2**	$ 83.4
Supplemental Disclosures of Cash Flow Information		
Cash paid for interest	**$ 100.6**	$ 75.9
Interest capitalized	**3.1**	1.6
Cash paid for income taxes	**3.4**	4.2

The accompanying Notes to Consolidated Financial Statements are an integral part of these unaudited statements.

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements

1. Basis of Accounting Presentation

The accompanying unaudited consolidated financial statements for NiSource reflect all normal recurring adjustments that are necessary, in the opinion of management, to present fairly the results of operations in accordance with generally accepted accounting principles in the United States of America.

The accompanying financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in NiSource s Annual Report on Form 10-K for the fiscal year ended December 31, 2006. Income for interim periods may not be indicative of results for the calendar year due to weather variations and other factors.

2. Recent Accounting Pronouncements

Recently Adopted Accounting Pronouncements

SFAS No. 158 Employers Accounting for Defined Benefit Pension and Other Postretirement Plans. In September 2006, the FASB issued SFAS No. 158 to improve existing reporting for defined benefit postretirement plans by requiring employers to recognize in the statement of financial position the overfunded or underfunded status of a defined benefit postretirement plan, among other changes. In the fourth quarter of 2006, NiSource adopted the provisions of SFAS No. 158 requiring employers to recognize in the statement of financial position the overfunded or underfunded status of a defined benefit postretirement plan, measured as the difference between the fair value of the plan assets and the benefit obligation. On January 1, 2007, NiSource adopted the SFAS No. 158 measurement date provisions requiring employers to measure plan assets and benefit obligations as of the fiscal year-end. The pre-tax impact of adopting the SFAS No. 158 measurement date provisions increased deferred charges and other assets by $9.4 million, decreased regulatory assets by $89.6 million, decreased retained earnings by $11.3 million, increased accumulated other comprehensive income by $5.3 million and decreased accrued liabilities for postretirement and postemployment benefits by $74.2 million. NiSource also recorded a reduction in deferred income taxes of approximately $2.6 million. In addition, 2007 expense for pension and postretirement benefits will reflect the updated measurement date valuations.

With the adoption of SFAS No. 158 NiSource determined that for certain rate-regulated subsidiaries the future recovery of pension and other postretirement plans costs is probable in accordance with the requirements of SFAS No. 71. These rate-regulated subsidiaries recorded regulatory assets and liabilities that would otherwise have been recorded to accumulated other comprehensive income.

Refer to Note 10, Pension and Other Postretirement Benefits, in the Notes to Consolidated Financial Statements for additional information.

FIN 48 Accounting for Uncertainty in Income Taxes. In June 2006, the FASB issued FIN 48 to reduce the diversity in practice associated with certain aspects of the recognition and measurement requirements related to accounting for income taxes. Specifically, this interpretation requires that a tax position meet a more-likely-than-not recognition threshold for the benefit of an uncertain tax position to be recognized in the financial statements and requires that benefit to be measured at the largest amount of benefit that is greater than 50% likely of being realized upon ultimate settlement. When determining whether a tax position meets the more-likely-than-not recognition threshold, it is to be based on whether it is probable of being sustained on audit by the appropriate taxing authorities, based solely on the technical merits of the position. Additionally, FIN 48 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006.

On January 1, 2007, NiSource adopted the provisions of FIN 48. As a result of the implementation of FIN 48, NiSource recognized a charge of $0.8 million to the opening balance of retained earnings. Refer to Note 9, Income Taxes, in the Notes to Consolidated Financial Statements for additional information.

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

SFAS No. 123 (revised 2004) Share-Based Payment. Effective January 1, 2006, NiSource adopted SFAS No. 123R using the modified prospective transition method. SFAS No. 123R requires measurement of compensation cost for all stock-based awards at fair value on the date of grant and recognition of compensation over the service period for awards expected to vest. In accordance with the modified prospective transition method, NiSource s consolidated financial statements for prior periods have not been restated to reflect, and do not include, the impact of SFAS No. 123R. Prior to the adoption of SFAS No. 123R, NiSource applied the intrinsic value method of APB No. 25 for awards granted under its stock-based compensation plans and complied with the disclosure requirements of SFAS No. 123.

When it adopted SFAS No. 123R in the first quarter of 2006, NiSource recognized a cumulative effect of change in accounting principle of $0.4 million, net of income taxes, which reflected the net cumulative impact of estimating future forfeitures in the determination of period expense, rather than recording forfeitures when they occur as previously permitted. Other than the requirement for expensing stock options, outstanding share-based awards will continue to be accounted for substantially as they are currently. Refer to Note 12, Stock Options and Awards, in the Notes to Consolidated Financial Statements for additional information.

Recently Issued Accounting Pronouncements

SFAS No. 157 Fair Value Measurements. In September 2006, the FASB issued SFAS No. 157 to define fair value, establish a framework for measuring fair value and to expand disclosures about fair value measurements. NiSource is currently reviewing the provisions of SFAS No. 157 to determine the impact it may have on its Consolidated Financial Statements and Notes to Consolidated Financial Statements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and should be applied prospectively, with limited exceptions.

SFAS No. 159 The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115. In February 2007, the FASB issued SFAS No. 159 which permits entities to choose to measure certain financial instruments at fair value that are not currently required to be measured at fair value. Upon adoption, a cumulative adjustment will be made to beginning retained earnings for the initial fair value option remeasurement. Subsequent unrealized gains and losses for fair value option items will be reported in earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007 and should not be applied retrospectively, except as permitted for certain conditions for early adoption. NiSource is currently reviewing the provisions of SFAS No. 159 to determine whether to elect fair value measurement for any of its financial assets or liabilities when it adopts this standard in 2008.

3. Earnings Per Share

Basic EPS is computed by dividing income available to common stockholders by the weighted-average number of shares of common stock outstanding for the period. The weighted average shares outstanding for diluted EPS include the incremental effects of the various long-term incentive compensation plans. The numerator in calculating both basic and diluted EPS for each period is reported net income. The computation of diluted average common shares follows:

Three Months Ended March 31, *(in thousands)*	**2007**	2006
Denominator		
Basic average common shares outstanding	**273,594**	272,342
Dilutive potential common shares		
Nonqualified stock options	**376**	50
Shares contingently issuable under employee stock plans	**636**	572
Shares restricted under employee stock plans	**163**	119
Diluted Average Common Shares	**274,769**	273,083

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

4. Restructuring Activities

During the second quarter of 2005, NiSource Corporate Services reached a definitive agreement with IBM under which IBM will provide a broad range of business transformation and outsourcing services to NiSource. The service and outsourcing agreement is for ten years with a transition period that ended on December 31, 2006. As of March 31, 2007, 872 employees were terminated as a result of the agreement with IBM. During the first quarter of 2007, no employees were terminated as a result of the agreement with IBM.

In the fourth quarter of 2005, NiSource announced a plan to reduce its executive ranks by approximately 15% to 20% of the top-level executive group. As of March 31, 2007, the employment of 13 employees was terminated as a result of the executive initiative, of whom 1 employee was terminated during the first quarter of 2007. In part, this reduction has come through anticipated attrition and consolidation of basic positions.

In previous years, NiSource implemented restructuring initiatives to streamline its operations and realize efficiencies as a result of the acquisition of Columbia. As of March 31, 2007, 1,566 employees were terminated, of whom no employees were terminated during the first quarter of 2007. Of the $3.3 million remaining restructuring liability from the Columbia merger and related initiatives, $3.0 million is related to facility exit costs.

Restructuring reserve by restructuring initiative:

(in millions)	Balance at December 31, 2006	Benefits Paid	Adjustments	Balance at March 31, 2007
Outsourcing initiative	$ 2.1	$	$	$ 2.1
Executive initiative	1.2	(0.3)		0.9
Columbia merger and related initiatives	3.8	(0.7)	0.2	3.3
Total	$ 7.1	$ (1.0)	$ 0.2	$ 6.3

5. Discontinued Operations and Assets Held for Sale

The assets and liabilities of discontinued operations and held for sale on the Condensed Consolidated Balance Sheet at March 31, 2007 were:

(in millions)	NDC Douglas Properties	NiSource Corporate Services	NiSource Development Company	Lake Erie Land	Columbia Transmission	Total
Assets of discontinued operations and held for sale						
Property, plant and equipment, net	$ 8.8	$ 9.5	$ 1.8	$ 2.9	$ 12.4	$ 35.4
Other assets	1.1					1.1
Assets of discontinued operations and held for sale	9.9	9.5	1.8	2.9	12.4	36.5

Liabilities of discontinued operations and held for sale												
Debt		(8.0)										(8.0)
Other liabilities		(1.8)										(1.8)
Liabilities of discontinued operations and held for sale	$	(9.8)	$		$		$		$		$	(9.8)

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

The assets and liabilities of discontinued operations and held for sale on the Condensed Consolidated Balance Sheet at December 31, 2006 were:

(in millions)	NDC Douglas Properties	NiSource Corporate Services	NiSource Development Company	Lake Erie Land	Columbia Transmission	Total
Assets of discontinued operations and held for sale						
Property, plant and equipment, net	$ 10.4	$ 12.7	$ 1.8	$ 4.3	$ 12.4	$ 41.6
Other assets	1.2			0.2		1.4
Assets of discontinued operations and held for sale	11.6	12.7	1.8	4.5	12.4	43.0
Liabilities of discontinued operations and held for sale						
Accounts payable	(0.4)					(0.4)
Debt	(10.0)					(10.0)
Other liabilities	(1.5)					(1.5)
Liabilities of discontinued operations and held for sale	$ (11.9)	$	$	$	$	$ (11.9)

Assets classified as discontinued operations or held for sale are no longer depreciated.

NDC Douglas Properties, a subsidiary of NiSource Development Company, is in the process of exiting some of its low income housing investments. Two of these investments were disposed of during 2006 and three other investments are expected to be sold or disposed of during 2007. NiSource has accounted for the investments to be sold as assets and liabilities of discontinued operations.

NiSource Corporate Services is in the process of selling its Marble Cliff facility. Impairment losses of $3.2 million and $2.5 million were recognized in the first quarters of 2007 and 2006, respectively, due to the current book value exceeding the estimated fair value of the facility. NiSource has accounted for this facility as assets held for sale.

NiSource Development Company is in the process of selling the former headquarters of Northern Indiana. NiSource has accounted for this facility as assets held for sale.

In March 2005, Lake Erie Land, wholly owned by NiSource began accounting for the operations of the Sand Creek Golf Club as discontinued operations. In June 2006, the assets of the Sand Creek Golf Club, valued at $11.9 million, and additional properties were sold to a private real estate development group. An after-tax loss of $0.2 million was recorded in June 2006. As a result of the June 2006 transaction, property estimated to be sold to the private developer during the next twelve months has been recorded as assets held for sale.

Columbia Transmission is in the process of selling certain facilities that are non-core to the operation of the pipeline system. NiSource has accounted for the assets of these facilities as assets held for sale.

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

Results from discontinued operations from NDC Douglas Properties low income housing investments, the golf course assets of Lake Erie Land and reserve changes for NiSource s former exploration and production subsidiary, CER, and Transcom are provided in the following table:

Three Months Ended March 31, *(in millions)*	2007	2006
Revenues from Discontinued Operations	$ 0.6	$ 1.4
Loss from discontinued operations	1.5	(0.8)
Income tax expense (benefit)	0.5	(0.3)
Income (Loss) from Discontinued Operations net of taxes	$ 1.0	$ (0.5)
Gain on Disposition of Discontinued Operations net of taxes	$ 6.6	$

Results from Discontinued Operations for the first quarter of 2007 includes a $7.5 million reduction, net of taxes, in the liability for unrecognized tax benefits and $0.9 million in related interest, net of taxes, associated with the issuance of additional income tax guidance in the first quarter of 2007.

6. Asset Retirement Obligations

NiSource accounts for its asset retirement obligations in accordance with SFAS No. 143 and FIN 47. Certain costs of removal that have been, and continue to be, included in depreciation rates and collected in the service rates of the rate-regulated subsidiaries are classified as regulatory liabilities and other removal costs on the Consolidated Balance Sheets.

For the three months ended March 31, 2007, NiSource accrued $1.7 million of accretion, of which $0.2 million was expensed and $1.5 million was recorded as a regulatory asset. For the three months ended March 31, 2006, NiSource accrued $1.8 million of accretion, of which $0.3 million was expensed and $1.5 million was recorded as a regulatory asset.

7. Regulatory Matters

Gas Distribution Operations Regulatory Matters

Significant Rate Developments. On February 1, 2007, Columbia of Kentucky filed a base rate case requesting an increase in rates of $12.6 million, or approximately 8%. Included in the filing is a request for approval of an accelerated main replacement cost recovery mechanism, in order to facilitate replacement of certain parts of Columbia of Kentucky s natural gas distribution system. Also, included are proposals to help offset the effects of recent usage declines and increased customer attrition. Hearings are expected to be held in the third quarter of 2007, with new rates expected to be in effect by the fourth quarter.

In mid 2006, Northern Indiana filed a petition which simplifies gas distribution rates, stabilizes revenues and provides for energy efficiency funding. Northern Indiana filed its detailed case in this proceeding in January 2007, based upon lengthy and detailed discussion with stakeholders. Following a February 27, 2007 evidentiary hearing, Northern Indiana filed an unopposed Form of Order, with the IURC on March 9, 2007. Northern Indiana expects a final order in the second quarter of 2007.

Cost Recovery and Trackers. A significant portion of the distribution companies revenue is related to the recovery of gas costs, the review and recovery of which occurs via standard regulatory proceedings. All states require periodic review of actual gas procurement activity to determine prudence and to permit the recovery of prudently incurred costs related to the supply of gas for customers. NiSource distribution companies have historically been found prudent in the procurement of gas supplies to serve customers.

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

Certain operating costs of the NiSource distribution companies are significant, recurring in nature, and generally outside the control of the distribution companies. Some states allow the recovery of such costs via cost tracking mechanisms. Such tracking mechanisms allow for abbreviated regulatory proceedings in order for the distribution companies to implement charges and recover appropriate costs. Tracking mechanisms allow for more timely recovery of such costs as compared with more traditional cost recovery mechanisms. Examples of such mechanisms include gas cost recovery adjustment mechanisms, tax riders, and bad debt recovery mechanisms. Gas Distribution Operations revenue is increased by the implementation and recovery of costs via such tracking mechanisms.

Comparability of Gas Distribution Operations line item operating results is impacted by these regulatory trackers that allow for the recovery in rates of certain costs such as bad debt expenses. Increases in the expenses that are the subject of trackers result in a corresponding increase in net revenues and therefore have essentially no impact on total operating income results.

Certain types of natural gas risers, which are owned by customers, on Columbia of Ohio s distribution system have been evaluated under a study required by the PUCO, and have been found to be prone to leak natural gas under certain conditions. On February 1, 2007, Columbia of Ohio announced plans to identify and replace these certain types of risers on its distribution system. Columbia of Ohio estimates that the cost to identify and replace the risers will approximate $200 million. On March 2, 2007, Columbia of Ohio filed a request with the PUCO seeking authority to defer the expenses from its investigation of risers on its system. On April 25, 2007, Columbia of Ohio filed an application with the PUCO seeking authority to recover the expenses for which it is seeking deferral authorization, and all other riser replacement-related costs, through an automatic adjustment mechanism for the infrastructure replacement program.

Customer Usage. The NiSource distribution companies continue to experience declining usage by customers, due in large part to the sensitivity of sales to volatile commodity prices. A significant portion of the LDC s operating costs are fixed in nature. Historically, rate design at the distribution level has been structured such that a large portion of cost recovery is based upon throughput, rather than in a fixed charge. Many of NiSource s LDCs are evaluating mechanisms that would de-couple the recovery of fixed costs from throughput, and implement recovery mechanisms that more closely link the recovery of fixed costs with fixed charges. Each of the states in which the NiSource LDCs operate has different requirements regarding the procedure for establishing such changes.

Gas Transmission and Storage Operations Regulatory Matters

Significant FERC Developments. On June 30, 2005, the FERC issued the Order on Accounting for Pipeline Assessment Costs. This guidance was issued by the FERC to address consistent application across the industry for accounting of the DOT s Integrity Management Rule. The effective date of the guidance was January 1, 2006 after which all assessment costs have been recorded as operating expenses. The rule specifically provides that amounts capitalized in periods prior to January 1, 2006 will be permitted to remain as recorded. In November, 2005, the INGAA sought review of the matter before the U. S. Court of Appeals for the D.C. Circuit (INGAA V. FERC, No. 05-1426). Oral argument was presented before the Court on January 16, 2007 and a ruling is currently pending.

On July 20, 2006, the FERC issued a declaratory order in response to a petition filed by Tennessee Gas Pipeline. The petition related to a Tennessee Gas Pipeline request to establish an interconnection with the Columbia Gulf operated portion of the Blue Water Pipeline system. Columbia Gulf has a long-standing practice of providing interconnections with other interstate pipelines only as long as there is an interconnection agreement in place that governs the rules of the interconnection. Among other things, these agreements help protect the integrity of Columbia Gulf s system and the reliability of service to its customers. The FERC ruled that Tennessee Gas Pipeline s interconnection request should be governed by the existing Blue Water Pipeline Operating Agreement between Columbia Gulf and Tennessee Gas Pipeline. Columbia Gulf constructed the necessary taps and Tennessee Gas Pipeline then completed its portion of the interconnection facilities. The interconnection was ready to flow gas on October 1, 2006. On December 29, 2006, Columbia Gulf filed in the D.C. Circuit Court of Appeals a Petition for Review of the Commission s July 20, 2006 order and a subsequent order denying Columbia Gulf s Request for Rehearing.

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

In the declaratory order, the FERC also referred the matter to the Office of Enforcement to determine if there should be any action taken against Columbia Gulf for failing to comply with prior orders that directed Columbia Gulf to allow Tennessee Gas Pipeline to make an interconnection. While disappointed with the FERC s referral of this matter to the Office of Enforcement, Columbia Gulf has cooperated with the Office of Enforcement s investigation. Columbia Gulf believes that an acceptable resolution of this matter can be reached during the second quarter 2007, which may include the payment of a fine by Columbia Gulf, the amount of which cannot be predicted at this time.

Columbia Gulf and Columbia Transmission are also cooperating with FERC on an informal non-public investigation of certain operating practices regarding tariff services offered by those companies. At this time, the companies cannot predict what the result of that investigation will be, but the FERC has indicated that it may seek to impose fines and possibly seek other remedies as well.

Proposed Millennium Pipeline Project

Millennium received FERC approval for a pipeline project, in which Columbia Transmission is participating and will serve as operator, which will provide access to a number of supply and storage basins and the Dawn, Ontario trading hub. The reconfigured project, which was approved by the FERC in a certificate order issued December 21, 2006, will begin at an interconnect with Empire, an existing pipeline that originates at the Canadian border and extends easterly towards Syracuse, New York. Empire will construct a lateral pipeline southward to connect with Millennium near Corning, New York. Millennium will extend eastward to an interconnect with Algonquin Gas Transmission Co. at Ramapo, New York. The Millennium partnership is currently made up of the following companies: Columbia Transmission (47.5%), DTE Millennium (26.25%), and KeySpan Millennium (26.25%). Columbia Transmission will be the operator.

The reconfigured Millennium project relies on completion of some or all of several other related pipeline projects proposed by Empire, Algonquin, Iroquois, and Islander East collectively referred to as the Companion Pipelines. The December 21, 2006 certificate order also granted the necessary project approvals to the Companion Pipelines. In addition, Millennium has received requested tax relief in New York. Millennium is in the process of bidding and analyzing the project costs for both 2007 and 2008. If the cost review determines the Millennium Project is still economically viable, construction will start in the spring of 2007 with a projected in-service date of November 1, 2008.

Hardy Storage Project. Both Hardy Storage and Columbia Transmission filed the necessary applications for the projects with the FERC on April 25, 2005, and received favorable orders on November 1, 2005. On October 26, 2006, Hardy Storage filed an application seeking to amend the November 1, 2005 order to revise the initial rates and estimated costs for the project pursuant to executed settlement agreements with Hardy Storage s customers. The certificate amendment was approved by FERC on March 15, 2007. Hardy Storage was approved to go in-service on March 29, 2007 and began injecting gas into storage on April 1, 2007.

Electric Operations Regulatory Matters

Significant Rate Developments. To settle a proceeding regarding Northern Indiana s request to recover intermediate dispatchable power costs, Northern Indiana has agreed to file an electric base rate case on or before July 1, 2008.

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

During 2002, Northern Indiana settled certain regulatory matters related to an electric rate review. On September 23, 2002, the IURC issued an order adopting most aspects of the settlement. The order approving the settlement provides that electric customers of Northern Indiana will receive bill credits of approximately $55.1 million each year. The credits will continue at the same annual level and per the same methodology, until the IURC enters a basic rate order that approves revised Northern Indiana s electric rates. The order included a rate moratorium that expired on July 31, 2006. The order also provides that 60% of any future earnings beyond a specified earnings level will be retained by Northern Indiana. The revenue credit is calculated based on electric usage and therefore in times of high usage the credit may be more than the $55.1 million target. Credits amounting to $13.7 million and $10.7 million were recognized for electric customers for the first quarter of 2007 and 2006, respectively.

MISO. As part of Northern Indiana s participation in the MISO transmission service and wholesale energy market, certain administrative fees and non-fuel costs have been incurred. IURC Orders have been issued authorizing the deferral for consideration in a future rate case proceeding the administrative fees and non-fuel related costs incurred after Northern Indiana s rate moratorium, which expired on July 31, 2006. During the first quarter of 2007 administrative fees of $1.3 million and non-fuel costs of $0.9 million were deferred. Total MISO costs deferred through March 31, 2007 were $6.5 million.

On April 25, 2006, the FERC issued an order on the MISO s Transmission and Energy Markets Tariff, stating that MISO had violated the tariff on several issues including not assessing revenue sufficiency guarantee charges on virtual bids and offers and for charging revenue sufficiency guarantee charges on imports. The FERC ordered MISO to perform a resettlement of these charges back to April 1, 2005. This resettlement is scheduled to commence in July 2007. Although the amount of resettlements applicable to Northern Indiana cannot be quantified at this time, it is not expected to be material.

Cost Recovery and Trackers. A significant portion of the Northern Indiana s revenue is related to the recovery of fuel costs to generate power and the fuel costs related to purchased power. These costs are recovered through a standard, quarterly, summary regulatory proceeding in Indiana (FAC). Northern Indiana has historically been found prudent in the procurement of fuel and purchased power.

In July 2006, the IURC issued an order creating a sub-docket in FAC 71 based upon a motion by interveners, the Industrial Group and La Porte County. The motion requested an investigation into Northern Indiana s generation and purchases practices that could not be fully considered in a summary proceeding. The sub-docket will also address concerns raised by the OUCC related to the reasonableness of recovering financial hedging transactions within the FAC. Subsequently, the IURC has approved FAC 72, 73 and 74 subject to the sub-docket in FAC 71. Amounts collected pursuant to FAC 71, 72, 73 and 74 are subject to refund based upon the final order in the sub-docket. A hearing in the FAC 71 sub-docket is scheduled for the second quarter of 2007 and an order anticipated before the end of 2007.

On November 26, 2002, Northern Indiana received approval for an ECT. Under the ECT, Northern Indiana is permitted to recover (1) AFUDC and a return on the capital investment expended by Northern Indiana to implement IDEM s NOx State Implementation Plan through an ECRM and (2) related operation and maintenance and depreciation expenses once the environmental facilities become operational through an EERM. Under the IURC s November 26, 2002 order, Northern Indiana is permitted to submit filings on a semi-annual basis for the ECRM and on an annual basis for the EERM. On December 13, 2006, the IURC approved Northern Indiana s latest compliance plan with the estimate of $312.8 million. On April 11, 2007, the IURC approved EER-9 and EER-4 for capital expenditures (net of accumulated depreciation) and operating expenses of $222.2 million and $14.1 million, through December 31, 2006, respectively.

On December 8, 2006, Northern Indiana filed a petition requesting a certificate of public convenience and necessity for clean coal technology projects, to address the first phase of CAIR and CAMR. The request included initiating ongoing review of the construction of the projects; finding that the projects constitute qualified pollution control property and are eligible for the rate-making treatment; finding that the projects constitute clean coal and energy projects and finding that the projects are reasonable and necessary and therefore eligible for the financial incentives; approving accounting, rate-making treatment, cost recovery and other relief in connection with Northern Indiana s clean coal technology, qualified pollution control property and clean coal and energy projects. Testimony

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

was filed in February 2007 requesting approval of $23 million of cost estimates for the projects. The hearing is scheduled for May 22, 2007.

Mitchell Station. In January 2002, Northern Indiana indefinitely shut down its Mitchell Station. In February 2004, the City of Gary announced an interest in acquiring the land on which the Mitchell Station is located for economic development, including a proposal to increase the length of the runways at the Gary International Airport. Northern Indiana, with input from a broad based stakeholder group, is evaluating the appropriate course of action for the Mitchell Station facility in light of Northwest Indiana s need for that property and the substantial costs associated with restarting the facility including the potential increase in level of environmental controls required.

8. Risk Management and Energy Trading Activities

NiSource uses commodity-based derivative financial instruments primarily to manage commodity price risk and interest rate risk exposure in its business as well as for commercial and industrial sales. NiSource is not involved in speculative energy trading activity. NiSource accounts for its derivatives in accordance with SFAS No. 133. Under SFAS No. 133, if certain conditions are met, a derivative may be specifically designated as (a) a hedge of the exposure to changes in the fair value of a recognized asset or liability or an unrecognized firm commitment, or (b) a hedge of the exposure to variable cash flows of a forecasted transaction.

NiSource s derivatives on the Condensed Consolidated Balance Sheets at March 31, 2007 were:

(in millions)	Hedge	Non-Hedge	Total
Price risk management assets			
Current assets	$ 121.4	$ 7.2	$ 128.6
Other assets	33.8	2.6	36.4
Total price risk management assets	$ 155.2	$ 9.8	$ 165.0
Price risk management liabilities			
Current liabilities	$ (31.7)	$ (3.7)	$ (35.4)
Other liabilities	(22.5)		(22.5)
Total price risk management liabilities	$ (54.2)	$ (3.7)	$ (57.9)

NiSource s derivatives on the Condensed Consolidated Balance Sheets at December 31, 2006 were:

(in millions)	Hedge	Non-Hedge	Total
Price risk management assets			
Current assets	$ 236.6	$ 1.1	$ 237.7
Other assets	49.8	0.1	49.9
Total price risk management assets	$ 286.4	$ 1.2	$ 287.6
Price risk management liabilities			
Current liabilities	$ (202.8)	$ (56.6)	$ (259.4)

Other liabilities	(32.5)	(5.7)	(38.2)
Total price risk management liabilities	$ (235.3)	$ (62.3)	$ (297.6)

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

The hedging activity for the first quarter of 2007 and 2006 affecting accumulated other comprehensive income, with respect to cash flow hedges included the following:

Three Months Ended March 31, *(in millions, net of taxes)*	**2007**	2006
Net unrealized gains on derivatives qualifying as cash flow hedges at the beginning of the period	**$ 31.4**	$ 150.7
Unrealized hedging gains (losses) arising during the period on derivatives qualifying as cash flow hedges	**28.4**	(51.7)
Reclassification adjustment for net loss (gain) included in net income	**(0.2)**	0.7
Net unrealized gains on derivatives qualifying as cash flow hedges at the end of the period	**$ 59.6**	$ 99.7

During the first quarter of 2007 and 2006, no amounts were recognized in earnings due to the ineffectiveness of derivative instruments being accounted for as hedges. All derivatives classified as a hedge are assessed for hedge effectiveness, with any components determined to be ineffective charged to earnings or classified as a regulatory asset or liability per SFAS No. 71 as appropriate. During the first quarter of 2007 and 2006, NiSource reclassified no amounts related to its cash flow hedges from accumulated other comprehensive income to earnings, due to the probability that certain forecasted transactions would not occur. It is anticipated that during the next twelve months the expiration and settlement of cash flow hedge contracts will result in income statement recognition of amounts currently classified in accumulated other comprehensive income of approximately $59.2 million of income, net of taxes.

Commodity Price Risk Programs. Northern Indiana, Northern Indiana Fuel and Light, Kokomo Gas, Northern Utilities, Columbia of Pennsylvania, Columbia of Kentucky, Columbia of Maryland and Columbia of Virginia use NYMEX derivative contracts to minimize risk associated with gas price volatility. These derivative hedging programs must be marked to fair value, but because these derivatives are used within the framework of their gas cost recovery mechanism, regulatory assets or liabilities are recorded to offset the change in the fair value of these derivatives.

Northern Indiana offers a PPS as an alternative to the standard gas cost recovery mechanism. This service provides Northern Indiana customers with the opportunity to either lock in their gas cost or place a cap on the total cost that could be charged for any future month specified. In order to hedge the anticipated physical future purchases associated with these obligations, Northern Indiana purchases NYMEX futures and options contracts that correspond to a fixed or capped price in the associated delivery month. The NYMEX futures and options contracts are designated as cash flow hedges. Columbia of Virginia started a program in April 2005 similar to the Northern Indiana PPS, which allows non-jurisdictional customers the opportunity to lock in their gas cost. These derivative programs are accounted for as cash flow hedges.

Northern Indiana also offers a DependaBill program to its customers as an alternative to the standard tariff rate that is charged to residential customers. The program allows Northern Indiana customers to fix their total monthly bill at a flat rate regardless of gas usage or commodity cost. In order to hedge the anticipated physical purchases associated with these obligations, Northern Indiana purchases NYMEX futures and options contracts that match the anticipated delivery needs of the program. This derivative program is accounted for as a cash flow hedge.

As part of the MISO Day 2 initiative, Northern Indiana was allocated and has purchased FTRs. These rights help Northern Indiana offset congestion costs due to the MISO Day 2 activity. The FTRs do not qualify for hedge accounting treatment, but since congestion costs are recoverable through the fuel cost recovery mechanism the related gains and losses associated with these transactions are recorded as a regulatory asset or liability, in accordance with SFAS No. 71. Additionally, Northern Indiana also uses derivative contracts to minimize risk associated with power price volatility. These derivative programs must be marked to fair value, but because these derivatives are used within the framework of their cost recovery mechanism, regulatory assets or liabilities are recorded to offset the change in the fair value of there derivatives.

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

For regulatory incentive purposes, Northern Indiana enters into purchase contracts at first of the month prices that give counterparties the daily option to either sell an additional package of gas at first of the month prices or recall the original volume to be delivered. Northern Indiana charges a fee for this option. The changes in the fair value of these options are primarily due to the changing expectations of the future intra-month volatility of gas prices. These written options are derivative instruments, must be marked to fair value and do not meet the requirement for hedge accounting treatment. However, in accordance with SFAS No. 71, Northern Indiana records the related gains and losses associated with these transactions as a regulatory asset or liability.

For regulatory incentive purposes, Columbia of Kentucky, Columbia of Ohio, Columbia of Pennsylvania, Columbia of Virginia and Columbia of Maryland (collectively, the Columbia LDCs) have the opportunity to enter into contracts that allow counterparties the option to sell gas to Columbia LDCs at first of the month prices for a particular month of delivery. Columbia LDCs charge the counterparties a fee for this option. The changes in the fair value of the options are primarily due to the changing expectations of the future intra-month volatility of gas prices. Certain of the Columbia LDCs defer a portion of the change in the fair value of the options as either a regulatory asset or liability in accordance with SFAS No. 71. Remaining changes for those Columbia LDCs and changes in fair value associated with the other Columbia LDCs are recognized currently in earnings or other current assets or liabilities based on the regulatory customer sharing mechanisms in place.

Columbia Energy Services has fixed price gas delivery commitments to three municipalities in the United States. Columbia Energy Services entered into a forward purchase agreement with a gas supplier, wherein the supplier will fulfill the delivery obligation requirements at a slight premium to index. In order to hedge this anticipated future purchase of gas from the gas supplier, Columbia Energy Services entered into commodity swaps priced at the locations designated for physical delivery. These commodity swap derivatives are accounted for as cash flow hedges.

Commodity price risk programs included in price risk assets and liabilities:

	March 31, 2007		December 31, 2006	
(in millions)	Assets	Liabilities	Assets	Liabilities
Gas price volatility program derivatives	$ 7.3	$ (2.3)	$	$ (58.9)
PPS program derivatives	0.4	(0.2)	0.7	(7.3)
DependaBill program derivatives		(0.1)	0.3	(2.4)
Electric energy program derivitives	2.5		0.7	(1.6)
Regulatory incentive program derivatives		(1.4)	0.5	(1.8)
Forward purchase agreements derivatives	114.1		110.0	
Total commodity price risk programs included	$ 124.3	$ (4.0)	$ 112.2	$ (72.0)

Interest Rate Risk Activities. Contemporaneously with the pricing of the 5.25% and 5.45% notes issued September 16, 2005, NiSource Finance settled $900 million of forward starting interest rate swap agreements with six counterparties. NiSource paid an aggregate settlement payment of $35.5 million which is being amortized as an increase to interest expense over the term of the underlying debt, resulting in an effective interest rate of 5.67% and 5.88%, respectively.

NiSource has entered into interest rate swap agreements to modify the interest rate characteristics of its outstanding long-term debt from fixed to variable. On May 12, 2004, NiSource Finance entered into fixed-to-variable interest rate swap agreements in a notional amount of $660 million with six counterparties having a 6 1/2-year term. NiSource Finance will receive payments based upon a fixed 7.875% interest rate and pay a floating interest amount based on U.S. 6-month BBA LIBOR plus an average of 3.08% per annum. There was no exchange of premium at the initial date of the swaps. In addition, each party has the right to cancel the swaps on May 15, 2009.

ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

On July 22, 2003, NiSource Finance entered into fixed-to-variable interest rate swap agreements in a notional amount of $500 million with four counterparties with an 11-year term. NiSource Finance will receive payments based upon a fixed 5.40% interest rate and pay a floating interest amount based on U.S. 6-month BBA LIBOR plus an average of 0.78% per annum. There was no exchange of premium at the initial date of the swaps. In addition, each party has the right to cancel the swaps on either July 15, 2008 or July 15, 2013.

As a result of the fixed-to-variable interest rate swap transactions referenced above, $1,160 million of NiSource Finance s existing long-term debt is now subject to fluctuations in interest rates. These interest rate swaps are designated as fair value hedges. The effectiveness of the interest rate swaps in offsetting the exposure to changes in the debt s fair value is measured using the short-cut method pursuant to SFAS No. 133. NiSource had no net gain or loss recognized in earnings due to hedging ineffectiveness from prior years.

Interest rate risk activities programs included in price risk management assets and liabilities:

	March 31, 2007		December 31, 2006	
(in millions)	Assets	Liabilities	Assets	Liabilities
Interest rate swap derivatives	$	$ (21.0)	$	$ (27.3)

Marketing, Trading and Other Activities. The operations of TPC primarily involve commercial and industrial gas sales, whereby TPC utilizes gas derivatives to hedge its expected future gas purchases. TPC, on behalf of Whiting Clean Energy, has also entered into power and gas derivative contracts to manage commodity price risk associated with operating Whiting Clean Energy.

Marketing and power programs included in price risk management assets and liabilities:

	March 31, 2007		December 31, 2006	
(in millions)	Assets	Liabilities	Assets	Liabilities
Gas marketing derivatives	$ 40.7	$ (31.8)	$ 174.3	$ (198.3)
Power forward derivatives		(1.1)	1.1	
Total marketing and power programs	$ 40.7	$ (32.9)	$ 175.4	$ (198.3)

9. Income Taxes

On January 1, 2007, NiSource adopted the provisions of FIN 48. As a result of the implementation of FIN 48, NiSource recognized a charge of $0.9 million to the opening balance of retained earnings, which includes the adjustment to the liability for unrecognized tax benefits shown below. The total amount of the liability for unrecognized tax benefits as of the date of adoption was $16.0 million, which is included in Other noncurrent liabilities, on the Condensed Consolidated Balance Sheets. As a result of the implementation of FIN 48, NiSource recognized the following changes in the liability for unrecognized tax benefits:

(in millions)	Total
Reduction in Retained Earnings (cumulative effect)	$ 0.9
Additional Deferred Tax Liabilities	(0.9)

Net increase in liability for unrecognized tax benefits	$

Included in the balance of unrecognized tax benefits at January 1, 2007, are $2.9 million of tax benefits that, if recognized, would affect the effective tax rate. Also included in the balance of unrecognized tax benefits at January 1, 2007, are $7.5 million of tax benefits that, if recognized, would result in an increase to Gain on Disposition of Discontinued Operations and $5.6 million of tax benefits that, if recognized, would result in adjustments to deferred taxes.

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ITEM 1. FINANCIAL STATEMENTS (continued)
NiSource Inc.
Notes to Consolidated Financial Statements (continued)

Effective January 1, 2007, NiSource recognizes accrued interest and penalties related to unrecognized tax benefits in income tax expense. In prior years, NiSource recognized such accrued interest in interest expense and penalties in other expenses. During the years ended December 31, 2006, and December 31, 2005, NiSource recognized approximately $1.3 million and $0.8 million, respectively, of interest in the Statements of Consolidated Income. NiSource also had $3.5 million and $2.2 million accrued on the Condensed Consolidated Balance Sheets for the payment of interest at December 31, 2006, and December 31, 2005. No amounts have been estimated or accrued for penalties. Upon adoption of FIN 48 on January 1, 2007, NiSource decreased its accrual for interest on unrecognized tax benefits to $3.3 million, resulting in a $0.1 million increase (net of tax) to the opening balance of retained earnings.

NiSource is subject to income taxation in the U.S. and various state jurisdictions, primarily Indiana, West Virginia, Virginia, Pennsylvania, Kentucky, Massachusetts, New Hampshire, Maine, Louisiana, Mississippi, Maryland, Illinois, New Jersey and New York.

Because NiSource is part of the IRS s Large and Mid-Size Business program, each year s federal income tax return is typically audited by the IRS. Tax years through 1998 have been audited and are settled and closed to further assessment. Years 1999 through 2002 have been audited and are settled with the exception of two issues that have been petitioned to the Tax Court. Tax years 2003 and 2004 are currently under examination. The audit is expected to be concluded in the second quarter of 2007.

The statute of limitations in each of the state jurisdictions in which NiSource operates remain open until the years are settled for federal income tax purposes, at which time amended state income tax returns reflecting all federal income tax adjustments are filed. There are no state income tax audits currently in progress.

NiSource s interim effective tax rates reflect the estimated annual effective tax rate for 2007 and 2006, respectively, adjusted for tax expense associated with certain discrete items. The effective tax rates for the quarter ended March 31, 2007 and March 31, 2006 were 37.2% and 35.4%, respectively. The effective tax rates differ from the federal tax rate of 35% primarily due to the effects of tax credits, state income taxes, utility rate-making, and other permanent book-to-tax differences such as the electric production tax deduction provided under Internal Revenue Code Section 199. The 1.8% increase from the comparable period last year is primarily the result of reductions in deferred state income liabilities that were recorded in the first quarter of 2006.

The quarter ended March 31, 2007 Condensed Consolidated Balance Sheet includes a reduction of $1.5 million in the liability for unrecognized tax benefits as a result of re-evaluation of those liabilities in the first quarter of 2007 to reflect negotiations associated with the 1999-2002 Tax Court petition. This reduction did not materially impact the effective tax rate because of required offsets recorded in deferred income taxes. Together with the $7.5 million reduction discussed in Note 5, Discontinued Operations and Assets Held for Sale, NiSource s ending liability for unrecognized tax benefits as of March 31, 2007 is $7.0 million. NiSource does not anticipate any significant changes in its liability for unrecognized tax benefits over the next twelve months.

10. Pension and Other Postretirement Benefits

NiSource provides defined contribution plans and noncontributory defined benefit retirement plans that cover its employees. Benefits under the defined benefit retirement plans reflect the employees compensation, years of service and age at retirement. Additionally, NiSource provides health care and life insurance benefits for certain retired employees. The majority of employees may become eligible for these benefits if they reach retirement age while working for NiSource.

As of December 31, 2006, NiSource used September 30 as its measurement date for its pension and postretirement benefit plans. On January 1, 2007, NiSource adopted the SFAS No. 158 measurement date provisions requiring employers to measure plan assets and benefit obligations as of the fiscal year-end. The pre-tax impact of adopting the SFAS No. 158 measurement date provisions increased deferred charges and other assets by $9.4 million, decreased regulatory assets by $89.6 million, decreased retained earnings by $11.3 million, increased accumulated other comprehensive income by $5.3 million and decreased accrued liabilities for postretirement and postemployment benefits by $74.2 million. NiSource also recorded a reduction in deferred income taxes of

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ITEM 1. FINANCIAL STATEMENTS (continued)

NiSource Inc.

Notes to Consolidated Financial Statements (continued)

approximately $2.6 million. In addition, 2007 expense for pension and postretirement benefits will reflect the updated measurement date valuations. In the fourth quarter of 2006, NiSource adopted the provisions of SFAS No. 158 requiring employers to recognize in the statement of financial position the overfunded or underfunded status of a defined benefit postretirement plan, measured as the difference between the fair value of the plan assets and the benefit obligation.

The following table provides NiSource s various postretirement benefit plans funded status at January 1, 2007, based on a December 31, 2006 measurement date compared to the funded status of NiSource s various postretirement benefit plans at December 31, 2006 based on a September 30, 2006 measurement date:

	Pension Benefits		Other Postretirement Benefits	
(in millions)	**Jan. 1, 2007**	Dec. 31, 2006	**Jan. 1, 2007**	Dec. 31, 2006
Benefit obligation	**$ 2,278.6**	$ 2,285.7	**$ 774.1**	$ 770.4
Fair value of plan assets	**$ 2,129.7**	$ 2,052.3	**$ 257.3**	$ 255.2
Funded Status	**$ (148.9)**	$ (233.4)	**$ (516.8)**	$ (515.2)

The key assumptions used to measure NiSource s various postretirement benefits plans funded status at January 1, 2007 were the same as those used for the previous September 30, 2006, measurement date.

NiSource expects to make contributions of $50.4 million to its pension plans and $52.3 million to its other postretirement benefit plans during 2007. Through March 31, 2007, NiSource has contributed $47.1 million to its pension plans and $12.4 million to its other postretirement benefit plans.

The following tables provide the components of the plans net periodic benefits cost for the first quarter of 2007 and 2006:

	Pension Benefits		Other Postretirement Benefits	
Three Months Ended March 31, *(in millions)*	**2007**	2006	**2007**	2006
Components of Net Periodic Benefit Cost				
Service cost	**$ 10.3**	$ 10.7	**$ 2.4**	$ 2.3
Interest cost	**31.9**	31.2	**10.9**	10.1
Expected return on assets	**(46.7)**	(43.9)	**(5.2)**	(4.6)
Amortization of transitional obligation			**2.0**	2.0
Amortization of prior service cost	**1.4**	1.5	**0.1**	0.1
Recognized actuarial loss	**2.0**	4.6	**1.5**	1.6
Total Net Periodic Benefits Cost	**$ (1.1)**	$ 4.1	**$ 11.7**	$ 11.5

11. Redemption of Preferred Stock

On April 14, 2006, Northern Indiana redeemed all of its outstanding cumulative preferred stock, having a total redemption value of $81.6 million.

12. Share-Based Compensation

NiSource currently issues long-term incentive grants to key management employees under a long-term incentive plan approved by stockholders on April 13, 1994 (1994 Plan). The 1994 Plan, as amended and restated, permits the following types of grants, separately or in combination: nonqualified stock options, incentive stock options, restricted stock awards, stock appreciation rights, performance units, contingent stock awards and dividend equivalents payable on grants of options, performance units and contingent stock awards. At March 31, 2007, there were approximately 26.7 million shares reserved for future awards under the amended and restated 1994 Plan.

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