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> Blanca S. Bayo, Director Division of Records and Reporting FLORIDA PUBLIC SERVICE COMMISSION 2540 Shumard Oak Boulevard Tallahassee, FL 32399-0850

RECEIVED

MAY 28 1998

FPSC - Records/Reporting

Re: Application Form for Authority to Provide Interexchange Telecommunications Service within the State of Florida by Williams Communications

980697 - TI

Dear Ms. Bayo:

Enclosed herewith for filing is the application referenced above, a Petition for Waiver of Bond Requirement, and a check from Williams Communications in the amount of \$250 to cover the cost of filing. Thank you for your assistance in this matter.

Sincerely yours,

Thomas A. Cloud, Esquire

GRAY, HARRIS & ROBINSON, P.A.

Enclosures

cc: William H. Gault, Esquire

DOCUMENT REMBER - DATE

05797 HAY 28 #

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DOCUMENT NUMBER - DATE

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MELBOURNE (407) 727 - 8100

original

FLORIDA PUBLIC SERVICE COMMISSION

APPLICATION FORM
for
AUTHORITY TO PROVIDE INTEREXCHANGE
TELECOMMUNICATIONS SERVICE
WITHIN THE STATE OF FLORIDA
980497-77

DOCUMENT NUMBER - DATE

FPSC-RECORDS/REPORTING

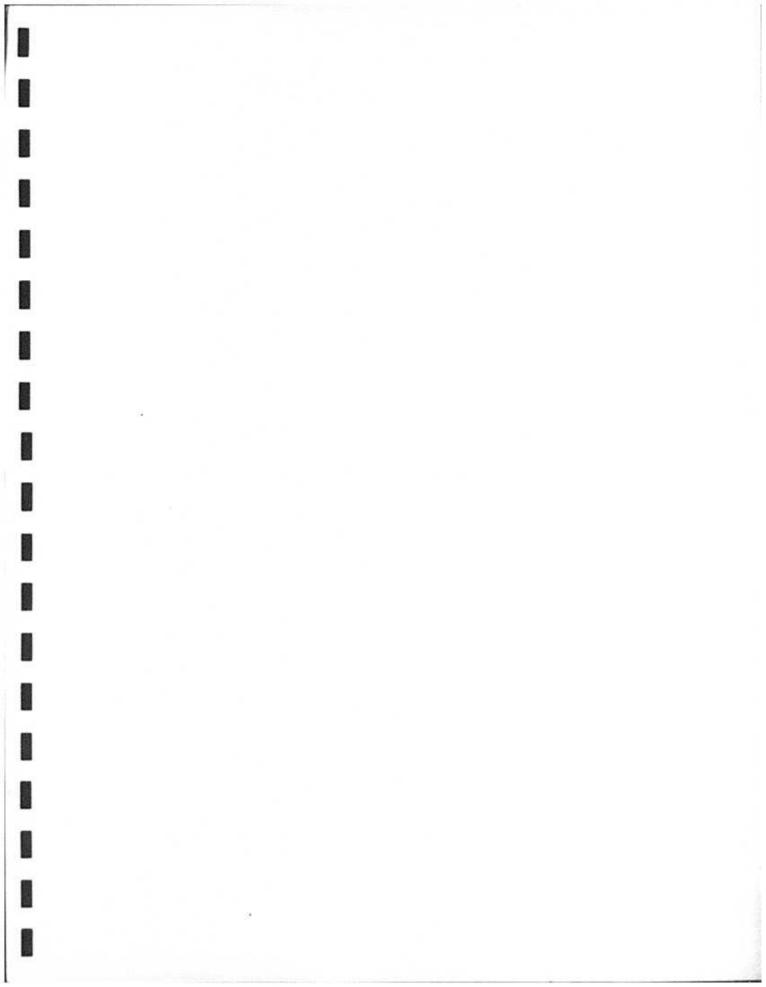
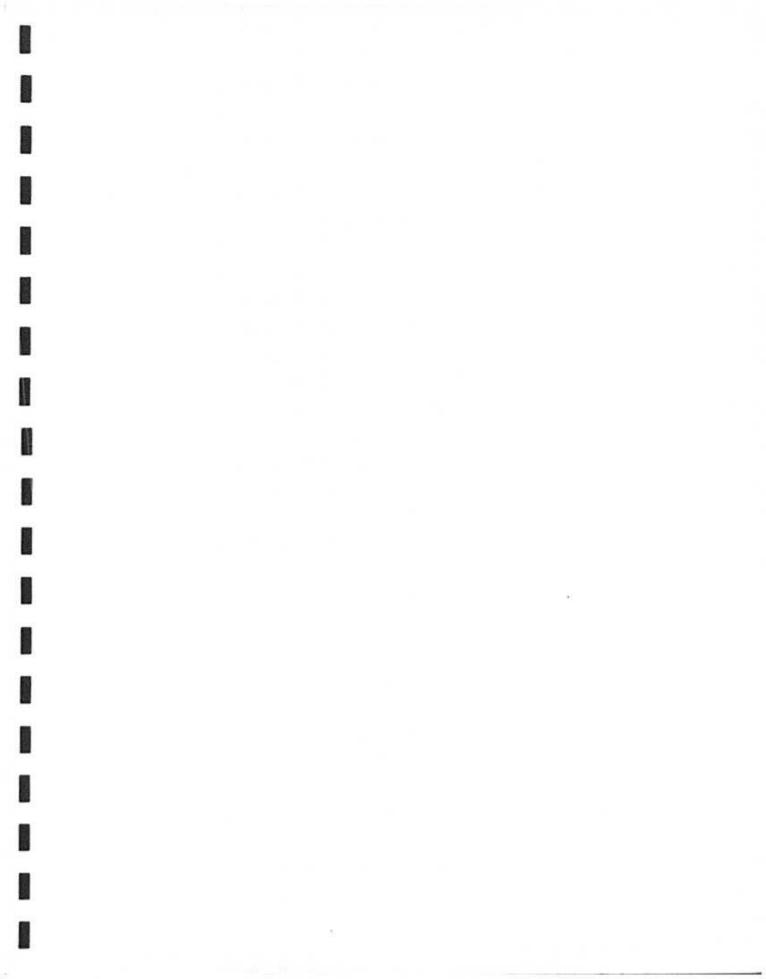


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ATTACHMENT E:	Map	Tab 6



** FLORIDA PUBLIC SERVICE COMMISSION *

DIVISION OF COMMUNICATIONS BUREAU OF SERVICE EVALUATION

APPLICATION FORM

AUTHORITY TO PROVIDE INTEREXCHANGE TELECOMMUNICATIONS SERVICE WITHIN THE STATE OF FLORIDA

Instructions

- A. This form is used for an original application for a certificate and for approval of sale, assignment or transfer of an existing certificate. In case of a sale, assignment or transfer, the information provided shall be for the purchaser, assignee or transferee (See Appendix A).
- B. Respond to each item requested in the application and appendices. If an item is not applicable, please explain why.
- C. Use a separate sheet for each answer which will not fit the allotted space.
- D. If you have questions about completing the form, contact:

Plorida Public Service Commission Division of Communications Bureau of Service Evaluation 2540 Shumard Oak Blvd. Gunter Building Tallahassee, Florida 32399-0850 (904) 413-6600

E. Once completed, submit the original and six (6) copies of this form along with a non-refundable application fee of \$250.00 to:

Plorida Public Service Commission Division of Administration 2540 Shumard Oak Blvd. Gunter Building Tallahassee, Florida 32399-0850 (904) 413-6251

- Select what type of business your company will be conducting (check all that apply):
 - (x) Facilities based carrier company owns and operates or plans to own and operate telecommunications switches and transmission facilities in Florida.
 - () Operator Service Provider company provides or plans to provide alternative operator services for IXCs; or toll operator services to call aggregator locations; or clearinghouse services to bill such calls.
 - () Reseller company has or plans to have one or more switches but primarily leases the transmission facilities of other carriers. Bills its own customer base for services used.
 - () Switchless Rebiller company has no switch or transmission facilities but may have a billing computer. Aggregates traffic to obtain bulk discounts from underlying carrier. Rebills end users at a rate above its discount but generally below the rate end users would pay for unaggregated traffic.
 - () Multi-Location Discount Aggregator company contracts with unaffiliated entities to obtain bulk/volume discounts under multi-location discount plans from certain underlying carriers. Then offers the resold service by enrolling unaffiliated customers.
 - () Prepaid Debit Card Provider any person or entity that purchases 800 access from an underlying carrier or unaffiliated entity for use with prepaid debit card service and/or encodes the cards with personal identification numbers.

This is an application for (check one):

(x) Original Authority (New company).

- () Approval of Transfer (To another certificated company).
- () Approval of Assignment of existing certificate (To an uncertificated company).
- () Approval for transfer of control (To another certificated company).
- Name of corporation, partnership, cooperative, joint venture or sole proprietorship:

Williams Communications, Inc., d/b/a Vyvx, Inc. (hereinafter "Williams")

- 4. Name under which the applicant will do business (fictitious name, etc.):
 Vyvx, Inc.
- National address (including street name & number, post office box, city, state and zip code).
 P.O. Box 22067

One Williams Center, Tulsa, Oklahoma 74121-2206

- 6. Florida address (including street name & number, post office box, city, state and zip code):
 See attached response.
- Structure of organization;

() Individual (x) Corporation

- () Foreign Corporation () Foreign Partnership () General Partnership () Limited Partnership () Other, _____
- If applicant is an individual or partnership, please give name, title and address of sole proprietor or partners.
 - (a) Provide proof of compliance with the foreign limited partnership statute (Chapter 620.169 FS), if applicable. See Attachment A
 - (b) Indicate if the individual or any of the partners have previously been:

- adjudged bankrupt, mentally incompetent, or found guilty of any felony or of any crime, or whether such actions may result from pending proceedings.
- (2) officer, director, partner or stockholder in any other Florida certificated telephone company. If yes, give name of company and relationship. If no longer associated with company, give reason why not.

9. If incorporated, please give:

(a) Proof from the Florida Secretary of State that the applicant has authority to operate in Florida.

Corporate charter number: F93000005378
See Attachment A

(b) Name and address of the company's Florida registered agent.

See attached response.

(c) Provide proof of compliance with the fictitious name statute (Chapter 865.09 FS), if applicable.

Fictitious name registration number: F93000005378 See Attachment A

- (c) Indicate if any of the officers, directors, or any of the ten largest stockholders have previously been:
 - adjudged bankrupt, mentally incompetent, or found guilty of any felony or of any crime, or whether such actions may result from pending proceedings.

None have been so adjudged.

(2) officer, director, partner or stockholder in any other Florida certificated telephone company. If yes, give name of company and relationship. If no longer associated with company, give reason why not.

- 10. Who will serve as liaison with the Commission in regard to (please give name, title, address and telephone number):
 - (a) The application;

See attached response.

(b) Official Point of Contact for the ongoing operations of the company;

See attached response.

(c) Tariff;

See attached response.

(d) Complaints/Inquiries from customers;

See attached response.

- 11. List the states in which the applicant:
 - (a) Has operated as an interexchange carrier.

Williams provides interstate interexchange services nationwide. It offers intrastate interexchange services in Alabama, Georgia, Louisiana, Mississippi, Texas, & South Carolina. (b) Has applications pending to be certificated as an interexchange carrier.

Williams has an application for certification pending in North Carolina. Vyvx of Virginia, Inc., a wholly owned subsidiary of Williams, has an application pending in Virginia. (c) Is certificated to operate as an

interexchange carrier.

Alabama, Georgia, Louisiana, Mississippi, and South Carolina. Williams has a Registration Statement on file with the Texas Public Utility Commission.

(d) Has been denied authority to operate as an interexchange carrier and the circumstances involved.

No states have denied Williams authority to operate as an interexchange

carrier.

(e) Has had regulatory penalties imposed for violations of telecommunications statutes and the circumstances involved.

No states have imposed regulatory penalties on Williams for violation of telecommunications statutes.

(f) Has been involved in civil court proceedings with an interexchange carrier, local exchange company or other telecommunications entity, and the circumstances involved.

See attached response.

12.	What services will the applicant offer to other certificated telephone companies:
	<pre>(x) Facilities. () Operators. () Billing and Collection. () Sales. (x) Maintenance. () Other:</pre>
13.	Do you have a marketing program?
14.	Will your marketing program: (x) Pay commissions? () Offer sales franchises? () Offer multi-level sales incentives? (x) Offer other sales incentives?
15.	Explain any of the offers checked in question 14 (To whom, what amount, type of franchise, etc.).
	See attached response.
16.	Who will receive the bills for your service (Check all that apply)?
	() Residential customers. (x) Business customers. () PATS providers. () PATS station end-users. () Hotels & motels. () Hotel & motel guests. (x) Universities. () Univ. dormitory residents. (X) Other: (specify) Telecommunications carriers
17.	Please provide the following (if applicable):
	(a) Will the name of your company appear on the bill for your services, and if not who will the billed party contact to ask questions about the bill (provide name and phone number) and how is this information provided?
	See attached response.
	(b) Name and address of the firm who will bill for your service.
	Not applicable.

- 18. Please provide all available documentation demonstrating that the applicant has the following capabilities to provide interexchange telecommunications service in Florida.
 - A. Financial capability.

Regarding the showing of financial capability, the following applies:

The application should contain the applicant's financial statements for the most recent 3 years, including:

- 1. the balance sheet
- income statement
- statement of retained earnings.

Further, a written explanation, which can include supporting documentation, regarding the following should be provided to show financial capability.

- Please provide documentation that the applicant has sufficient financial capability to provide the requested service in the geographic area proposed to be served.
- Please provide documentation that the applicant has sufficient financial capability to maintain the requested service.
- 3. Please provide documentation that the applicant has sufficient financial capability to meet its lease or ownership obligations.

NOTE: This documentation may include, but is not limited to, financial statements, a projected profit and loss statement, credit references, credit bureau reports, and descriptions of business relationships with financial institutions.

If available, the financial statements should be audited financial statements.

If the applicant does not have audited financial statements, it shall be so stated. The unaudited financial statements should then be signed by the applicant's chief executive officer and chief financial officer. The signatures should affirm that the financial statements are true and correct.

B. Managerial capability.

See attached response.

C. Technical capability.

See attached response.

 Please submit the proposed tariff under which the company plans to begin operation. Use the format required by Commission Rule 25-24.485 (example enclosed).

Attached.

MTS with distance sensitive per minute rates
Method of access is FGA
Method of access is FGB
Method of access is FGD
Method of access is 800
MTS with route specific rates per minute Method of access is FGA Method of access is FGB Method of access is FGD Method of access is 800
MTS with statewide flat rates per minute (i.e. no distance sensitive)
Method of access is FGA
Method of access is FGB
Method of access is FGD
Method of access is 800

	MTS for pay telephone service providers
	Block-of-time calling plan (Reach out Florida, Ring America, etc.).
	800 Service (Toll free)
	WATS type service (Bulk or volume discount) Method of access is via dedicated facilities Method of access is via switched facilities
	X Private Line services (Channel Services) (For ex. 1.544 mbs., DS-3, etc.)
	Travel Service Method of access is 950 Method of access is 800
	900 service
	Operator Services Available to presubscribed customers Available to non presubscribed customers (for example to patrons of hotels, students in universities, patients in hospitals Available to inmates
	Services included are:
	Station assistance Person to Person assistance Directory assistance Operator verify and interrupt Conference Calling
21.	What does the end user dial for each of the interexchange carrier services that were checked in services included (above).
	Not applicable.
22.	Other: Not applicable.
	MU 31 (11/95) by Commission Rule Nos. 25-24.471, 25-24.473, and 25

** APPLICANT ACKNOWLEDGEMENT STATEMENT **

- REGULATORY ASSESSMENT FEE: I understand that all telephone companies must pay a regulatory assessment fee in the amount of .15 of one percent of its gross operating revenue derived from intrastate business. Regardless of the gross operating revenue of a company, a minimum annual assessment fee of \$50 is required.
- GROSS RECEIPTS TAX: I understand that all telephone companies must pay a gross receipts tax of two and one-half percent on all intra and interstate business.
- SALES TAX: I understand that a seven percent sales tax must be paid on intra and interstate revenues.
- APPLICATION FEE: A non-refundable application fee of \$250.00 must be submitted with the application.
- 5. RECEIPT AND UNDERSTANDING OF RULES: I acknowledge receipt and understanding of the Florida Public Service Commission's Rules and Orders relating to my provision of interexchange telephone service in Florida. I also understand that it is my responsibility to comply with all current and future Commission requirements regarding interexchange service.
- 6. ACCURACY OF APPLICATION: By my signature below, I the undersigned owner or officer of the named utility in the application, attest to the accuracy of the information contained in this application and associated attachments. I have read the foregoing and declare that to the best of my knowledge and belief, the information is a true and correct statement.

Further, I am aware that pursuant to Chapter 837.06, Florida Statutes, "Whoever knowingly makes a false statement in writing with the intent to mislead a public servant in the performance of his official duty shall be guilty of a misdemeanor of the second degree, punishable as provided in s. 775.082 and s. 775.083".

UTILITY OFFICIAL:

Signature

Joseph C. Turcotte

Vice President

Title

Vice President

Title

Vice President

Telephone No.

GEROVE

** APPENDIX A **

CERTIFICATE TRANSFER STATEMENT

I, (TYPE NAME) _			
(TITLE)		_, of (NA	ME OF COMPANY)
and the state of the same			_, and current
holder of certificate nu	mber	, h	ave reviewed
this application and joi	n in the petitione	r's reque	st for a
transfer of the above-me	ntion certificate.		
UTILITY OFFICIAL:			
VALUE OF FACABLE	Signature		Date
	*		
	Title		elephone No.

** APPENDIX B **

CUSTOMER DEPOSITS AND ADVANCE PAYMENTS

A statement of how the Commission can be assured of the security of the customer's deposits and advance payments may be responded to in one of the following ways (applicant please check one):

- () The applicant will not collect deposits nor will it collect payments for service more than one month in advance.
- *(X) The applicant will file with the Commission and maintain a surety bond in an amount equal to the current balance of deposits and advance payments in excess of one month. (Bond must accompany application.)

*Williams plans to file a petition requesting relief from the bond requirement pursuant to Fla. Admin. Code r. 25-24.490 concurrent with the filing of this application.

UTILITY OFFICIAL:

Signature

5/1/55 Date

Joseph C. Turcotte

Vice President

Title

(918) 573-3098

Telephone No.

** APPENDIX C **

INTRASTATE NETWORK

- POP: Addresses where located, and indicate if owned or leased.
 - 1) Jacksonville
- 2) Orlando
- 3) Tampa 4) Miami
 Williams occupies these locations pursuant to collocate agreements
 that do not grant ownership or leasehold interests.
- SWITCHES: Address where located, by type of switch, and indicate if owned or leased.
 - Not applicable.
- 2)

3)

- 4)
- 3. TRANSMISSION FACILITIES: Pop-to-Pop facilities by type of facilities (microwave, fiber, copper, satellite, etc.) and indicate if owned or leased.
 - POP-to-POP

TYPE

OWNERSHIP

See attached response.

- 2)
- 4. ORIGINATING SERVICE: Please provide the list of exchanges where you are proposing to provide originating service within thirty (30) days after the effective date of the certificate (Appendix D).

 TRAFFIC RESTRICTIONS: Please explain how the applicant will comply with the EAEA requirements contained in Commission Rule 25-24.471 (4) (a) (copy enclosed).

Not applicable. Williams initially does not seek authority to offer, nor presently plan to offer intrastate switched voice services. If Williams seeks to offer such services in the future, it will comply with all applicable rules of the Commission.

- 6. CURRENT FLORIDA INTRASTATE SERVICES: Applicant has () or has not (x) previously provided intrastate telecommunications in Florida. If the answer is has, fully describe the following:
 - a) What services have been provided and when did these services begin?
 - b) If the services are not currently offered, when were they discontinued?

Joseph C. Turcotte

Vice President

Title

Vice President

Vice President

Telephone No.

** APPENDIX D **

FLORIDA TELEPHONE EXCHANGES

AND

EAS ROUTES

Describe the service area in which you hold yourself out to provide service by telephone company exchange. If all services listed in your tariff are not offered at all locations, so indicate.

In an effort to assist you, attached is a list of major exchanges in Florida showing the small exchanges with which each has extended area service (EAS).

** FLORIDA EAS FOR MAJOR EXCHANGES **

Extended Service Area	·. with	These Exchanges
PENSACOLA:		Cantonment, Gulf Breeze Pace, Milton Holley-Navarre.
PANAMA CITY:		Lynn Haven, Panama City Beach,
		Youngstown-Fountain and Tyndall AFB.
TALLAHASSEE:		Crawfordville, Havana, Monticello, Panacea, Sopchoppy and St. Marks.
JACKSONVILLE:		Baldwin, Ft. George, Jacksonville Beach, Callahan, Maxville, Middleburg Orange Park, Ponte Vedra and Julington.
GAINESVILLE:		Alachua, Archer, Brooker, Hawthorne, High Springs, Melrose, Micanopy, Newberry and Waldo.
OCALA:		Belleview, Citra, Dunnellon,

Forest Lady Lake (B21), McIntosh, Oklawaha, Orange Springs, Salt Springs and Silver Springs Shores.

DAYTONA BEACH:

New Smyrna Beach.

TAMPA:

Central None East Plant City North Zephyrhills South Palmetto West Clearwater

CLEARWATER:

St. Petersburg, Tampa-West and

Tarpon Springs.

ST. PETERSBURG:

Clearwater.

LAKELAND:

Bartow, Mulberry, Plant City, Polk City and Winter Haven.

ORLANDO:

Apopka, East Orange, Lake Buena Vista, Oviedo, Windermere,

Winter Garden,

Winter Park, Montverde, Reedy

Creek, and Oviedo-Winter

Springs.

WINTER PARK: Apopka, East Orange, Lake Buena Vista, Orlando, Oviedo, Sanford, Windermere, Winter Garden, Oviedo-Winter Springs Reedy Creek, Geneva and Montverde.

TITUSVILLE:

Cocoa and Cocoa Beach.

COCOA:

Cocoa Beach, Eau Gallie, Melbourne and Titusville.

MELBOURNE:

Cocoa, Cocoa Beach, Eau Gallie

and Sebastian.

SARASOTA:

Bradenton, Myakka and Venice.

FT. MYERS:

Cape Coral, Ft. Myers Beach, North Cape Coral, North Ft. Myers, Pine Island, Lehigh

Acres and Sanibel-Captiva Islands.

NAPLES:

Marco Island and North Naples.

WEST PALM BEACH:

Boynton Beach and Jupiter.

POMPANO BEACH:

Boca Raton, Coral Springs, Deerfield Beach and Ft.

Lauderdale.

FT. LAUDERDALE:

Coral Springs, Deerfield Beach, Hollywood and Pompano Beach.

HOLLYWOOD:

Ft. Lauderdale and North Dade.

NORTH DADE:

Hollywood, Miami and Perrine.

MIAMI:

Homestead, North Dade and

Perrine

** APPENDIX E **

** GLOSSARY **

ACCESS CODE: The term denotes a uniform four or seven digit code assigned to an individual IXC. The five digit code has the form 10XXX and the seven digit code has the form 950-XXXX.

BYPASS: Transmission facilities that go direct from the local exchange end user to an IXC point of presence, thus bypassing the local exchange company.

CARRIERS CARRIER: An IXC that provides telecommunications service, mainly bulk transmission service, to other IXC only.

CENTRAL OFFICE: A local operating unit by means of which connections are established between subscribers' lines and trunk or toll lines to other central offices within the same exchange or other exchanges. Each three (3) digit central office code (NXX) used shall be considered a separate central office unit.

CENTRAL OFFICE CODE: The term denotes the first three digits (NXX) of the seven (7) digit telephone number assigned to a customer's telephone exchange service.

COMMISSION: The Florida Public Service Commission.

COMPANY, TELEPHONE COMPANY, UTILITY: These terms may be used interchangeably herein and shall mean any person, firm, partnership or corporation engaged in the business of furnishing communication service to the public under the jurisdiction of the Commission.

DEDICATED FACILITY: The term denotes a transmission circuit which is permanently for the exclusive use of a customer or a pair of customers.

END USER: The term denotes any individual, partnership, association, corporation, governmental agency or any other entity which (A) obtains a common line, uses a pay telephone or obtains interstate service arrangements in the operating territory of the company or (B) subscribes to interstate services provided by an IXC or uses the services of the IXC when the IXC provides interstate service for its own use.

EQUAL ACCESS EXCHANGE AREAS: EAEA means a geographic area, configured based on 1987 planned toll center/access tandem areas, in which local exchange companies are responsible for providing equal access to both carriers and customers of carriers in the most economically efficient manner.

EXCHANGE: The entire telephone plant and facilities used in providing telephone service to subscribers located in an exchange area. An exchange may include more than one central office unit.

EXCHANGE (SERVICE) AREA: The territory, including the base rate suburban and rural areas served by an exchange, within which local telephone service is furnished at the exchange rates applicable within that area.

EXTENDED AREA SERVICE: A type of telephone service furnished under tariff provision whereby subscribers of a given exchange or area may complete calls to, and receive messages from, one or more other contiguous exchanges without toll charges, or complete calls to one or more other exchanges without toll message charges.

FACILITIES BASED: An IXC that has its own transmission and/or switching equipment or other elements of equipment and does not rely on others to provide this service.

FOREIGN EXCHANGE SERVICES: A classification of exchange service furnished under tariff provisions whereby a subscriber may be provided telephone service from an exchange other than the one from which he would normally be served.

FEATURE GROUPS: General categories of unbundled tariffs to stipulate related services.

Feature Group A: Line side connections presently serving specialized common carriers.

Feature Group B: Trunk side connections without equal digit or code dialing.

Feature Group C: Trunk side connections presently serving AT&T-C.

Feature Group D: Equal trunk access with subscription.

INTEREXCHANGE COMPANY: means any telephone company, as defined in Section 364.02(4), F.S. (excluding Payphone Providers), which provides telecommunication service between exchange areas as those areas are described in the approved tariffs of individual local exchange companies.

INTER-OFFICE CALL: A telephone call originating in one central office unit or entity but terminating in another central office unit or entity both of which are in the same designated exchange area.

INTRA-OFFICE CALL: A telephone call originating and terminating within the same central office unit or entity.

INTRASTATE COMMUNICATIONS: The term denotes any communications in Florida subject to oversight by the Florida Public Service Commission as provided by the laws of the State.

INTRA-STATE TOLL MESSAGE: Those toll messages which originate and terminate within the same state.

LOCAL ACCESS AND TRAMSPORT AREA: LATA means the geographic area established for the administration of communications service. It encompasses designated exchanges, which are grouped to serve common social, economic and other purposes.

LOCAL EXCHANGE COMPANY (LEC): Means any telephone company, as defined in Section 364.02(4), F.S., which, in addition to any other telephonic communication service, provides telecommunication service within exchange areas as those areas are described in the approved tariffs of the telephone company.

OPTIONAL CALLING PLAM: An optional service furnished under tariff provisions which recognizes a need of some subscribers for extended area calling without imposing the cost on the entire body of subscribers.

900 SERVICE: A service similar to 800 service, except this service is charged back to the customer based on first minute plus additional minute usage.

PIN NUMBER: A group of numbers used by a company to identify their customers.

PAY TELEPHONE SERVICE COMPANY: Means any telephone company, other than a Local Exchange Company, which provides pay telephone service as defined in Section 364.335(4), F.S.

POINT OF PRESENCE (POP): Bell-coined term which designates the

actual (physical) location of an IXC's facility. Replaces some applications of the term "demarcation point."

PRIMARY SERVICE: Individual line service or party line service.

RESELLER: An IXC that does not have certain facilities but purchases telecommunications service from an IXC and then resells that service to others.

STATION: A telephone instrument consisting of a transmitter, receiver, and associated apparatus so connected as to permit sending and/or receiving telephone messages.

SUBSCRIBER, CUSTOMER: These terms may be used interchangeably herein and shall mean any person, firm, partnership, corporation, municipality, cooperative organization, or governmental agency supplied with communication service by a telephone company.

SUBSCRIBER LINE: The circuit or channel used to connect the subscriber station with the central office equipment.

TRUNK: A communication channel between central office units or entities, or private branch exchanges.

ATTACHMENTS:

A - CERTIFICATE TRANSFER STATEMENT

B - CUSTOMER DEPOSITS AND ADVANCE PAYMENTS

C - INTRASTATE NETWORK

D - FLORIDA TELEPHONE EXCHANGES and EAS ROUTES

E - GLOSSARY

 Although Williams has facilities and employees in Florida, it does not presently have a regular business office in Florida. Its regional sales office is located at 2655 LeJeune Road, Suite 412, Coral Gables, Florida 33134 (Tel: 305-448-6096). 9. (b) CT Corporation System 1200 South Pine Island Road Plantation, FL 33324 954/473-5503 9. (c)(2)

The Williams Companies ("TWC") indirectly owned WilTel, Inc. ("WilTel"), a Florida Certificated telephone company. In addition, Delwin L. Bothof and S. Miller Williams were officers and stockholders of WilTel. TWC sold the network services operations of WilTel, Inc. ("WilTel") to LDDS Communications, Inc. ("LDDS"), on January 5, 1995. TWC indirectly owns all of the outstanding stock of Williams Communications, Inc ("Williams") and Messrs. Bothof and Williams are currently officers of Williams.

Thomas A. Cloud, Esq.
Gray, Harris & Robinson
201 East Pine Street
Suite 1200
Orlando, Florida 32801
Tel: (407) 244-5624

Joseph C. Turcotte Senior Vice President, Operations & Engineering Williams - Network, a division of Williams Communications, Inc. One Williams Center, MD RC3-1 Tulsa, Oklahoma 74172 Tel: (918) 573-3098

10. (c) Joseph W. Miller, Esq.
The Williams Companies, Inc.
One Williams Center, Suite 4100
Tulsa, Oklahoma 74172
Tel: (918) 573-2108

10. (d) Gordon Martin
Vice President, Sales and Marketing
Williams - Network
Williams Communications, Inc.
One Williams Center, MD 26-1
Tulsa, OK 74172
Tel: 918-573-5115

11.(f)

In addition to miscellaneous collection actions that may have involved telecommunications entities, Williams recently filed a petition against WorldCom Network Services, Inc. ("WorldCom") alleging several claims arising from an agreement connected with the acquisition by WorldCom of WilTel, Inc. (and certain sister subsidiaries), a former affiliate of Williams. In 1997 Williams filed a complaint alleging breach of contract against a telecommunications entity (known as BAF) involving the sale or lease of a satellite transponder. The parties settled this dispute before judicial resolution.

¹ Plaintiff's Petition for Declaratory relief, Money Damages, and other Relief, Williams Communications, Inc. v. WorldCom Network Services, Inc., Case No. CJ 98 1386 (Okla. D. Ct. Tulsa County March 20, 1998)

15.

Williams uses internal Sales and Marketing departments for marketing and sales activity. Williams occasionally employs, on a limited scale, direct marketing, such as direct mail or outbound telemarketing, in addition to print advertising. Williams pays commissions to internal sales force members as a standard component of their compensation plan. Commission payments vary from approximately twenty percent to fifty percent of total compensation. Salespersons may also receive certain bonuses and trips to vacation destinations.

17.(a)

Williams bills for services by means of monthly invoices unless customers request alternative arrangements. Williams' name appears on such invoices. Customers with questions regarding invoices for services can contact a customer service representative at Williams' toll-free customer service number ((800)-934-8435).

Williams is a wholly owned subsidiary of Williams Communications Group, Inc., which, in turn, is a wholly owned subsidiary of Williams Holdings of Delaware, Inc. The Williams Companies, Inc. ("Williams Companies"), a publicly traded company, owns 100 percent of Williams Holdings of Delaware, Inc. The Williams Companies is a publicly traded Fortune 500 company and is solidly profitable. Its annual reports filed with the Securities and Exchange Commissions for the years 1995, 1996, and 1997 are attached as Attachment B. Those filings, together with the reliance that Williams' customers have placed on its services (see discussion in response to question 18(c), demonstrate Williams' financial ability to provide high-quality service to the area proposed to be served, maintain such service, and satisfy its lease and ownership obligations. Williams has operated on an interstate brsis since 1990 and has never been in default of any material financial obligation.

18.(B)

A select team of telecommunications professionals who possess extensive experience in the telecommunications industry manage Williams. Attachment C provides a summary of the background of Williams' key management personnel.

18.(C)

Williams' twenty-four-hour network monitoring center in Tulsa, Oklahoma, provides highly efficient and effective centralized management of its network. Williams regularly provides training to maintain its employees' ability to respond to the demands of a changing, technologically driven market.

Williams currently provides, and will continue to provide, repair and maintenance of its facilities in order to ensure that its customers obtain high quality service. Customers may report service problems to Williams' customer service center. Because of the nature of Williams' services, Williams normally diverts signals to alternate facilities in the event of problems, in order to avoid significant service interruptions. Williams performs this diversion from its centralized network management center by means of automatic devices or its electronic fiber-optic transmission equipment may automatically switch a transmission link to standby facilities. Williams takes the affected facilities out of service and dispatches repair personnel. Williams typically detects and remedies problems before receiving a call from a customer.

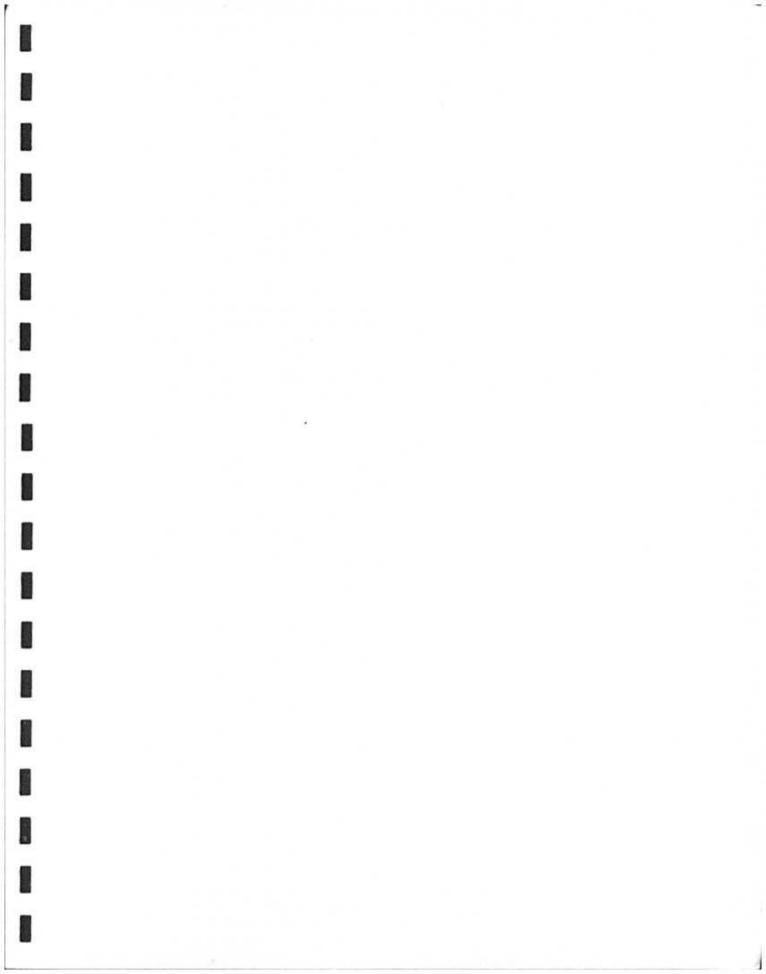
The best evidence of Williams' technical capability, however, is the reliance that its customers place on it for telecommunications services used in very high profile broadcasts. Television networks have used Williams in covering most major news events in this decade, such as the Oklahoma City bombing, visits by foreign leaders, and airline accident investigations. Williams also provides telecommunications services for the majority of all major league football, baseball, basketball, and hockey games televised in the United States. Since 1990, Williams has annually provided the primary feed for the National Football League's Super Bowl. The Super Bowl is the world's most widely viewed sporting event and even a brief interruption of Super Bowl coverage would have a significant impact on a network's reputation and could result in hundreds of thousands of dollars in lost revenue.

Pop-to-Pop	Type*	Ownership
Jacksonville	optical fiber	neither owned nor leased
Orlando	optical fiber	neither owned nor leased
Tampa	optical fiber	neither owned nor leased
Miami	optical fiber	neither owned nor leased

^{*}Williams recently agreed to purchase, and plans to construct additional fiber optic facilities in Florida. Attachment E is a map showing existing facilities and the planned location of new facilities.

Appendix D

Williams intends to offer its broadcast quality point-to-point video transmission services on a statewide basis by means of interconnections with other local exchange and interexchange telecommunications providers.





FLORIDA DEPARTMENT OF STATE Sandra B. Mortham Secretary of State

March 19, 1998

CT Corporation System

Tallahassee, FL

Re: Document Number F93000005378

The Amendment to the Application of a Foreign Corporation for VYVX, INC. which changed its name to WILLIAMS COMMUNICATIONS, INC. doing business in Florida as VYVX, INC., a Delaware corporation authorized to transact business in Florida, was filed on March 19, 1998.

The certification you requested is enclosed.

Should you have any questions regarding this matter, please telephone (850) 487-6050, the Amendment Filing Section.

Susan Payne Senior Section Administrator Division of Corporations

Letter Number: 098A00014956



Bepartment of State

I certify from the records of this office that WILL!AMS COMMUNICATIONS, INC. doing business in Florida as VYVX, INC. is a Delaware corporation authorized to transact business in the State of Florida, qualified on November 24, 1993.

The document number of this corporation is F93000005378.

I further certify that said corporation has paid all fees and penalties due this office through December 31, 1997, that its most recent annual report was filed on May 1, 1997, and its status is active.

I further certify that said corporation has not filed a Certificate of Withdrawal.

Given under my hand and the Great Seal of the State of Florida at Tallahassee, the Capitol, this the Nineteenth day of March, 1998



Sandra B. Mortham Secretary of State

APPLICATION BY FOREIGN CORPORATION TO FILE AMENDMENT TO APPLICATION FOR AUTHORIZATION TO TRANSACT BUSINESS IN FLORIDA

SECTION I (1-3 must be completed)	90 00
1. yyyx, Inc.	
Name of corporation as it appears within the records of the Department	of State.
2. Incorporated under laws of: Delaware	
3. Date authorized to do business in Florida: November 24, 1993	
SECTION II (4-7 complete only the applicable changes)	
4. If the amendment changes the name of the corporation, when was the effected under the laws of its jurisdiction of incorporation?	ne change
January 29, 1998	
Name of corporation after the amendment, adding suffix "corporation," "corporated," or appropriate abbreviation, if not contained in new name of the	mpany," in corporation
Williams Communications, Inc.	
6. If the amendment changes the period of duration, indicate new period of duration	ration.
No Change	
7. If the amendment changes the jurisdiction of incorporation, indicate new juri	sdiction.
2/27/9	8
Signature Date .	

Name and Title David M. Highee, Secretary

(FLA.- 2251 - 3/19/93)

WILLIAMS COMMUNICATIONS, INC.

I, the undersigned, DAVID M. HIGBEE, Secretary of WILLIAMS COMMUNICATIONS, INC., a Delaware corporation (hereinafter called the "Corporation"), do hereby certify that by unanimous written consent of the Board of Directors of this Corporation, the following resolution was duly adopted on March 3, 1998:

RESOLVED that Williams Communications, Inc., organized and existing in the State of Delaware, hereby adopts the name Vyvx, for use in all states and for all purposes; and further resolved that the officers of the Corporation are authorized and directed to take all steps that they deem necessary and appropriate to qualify the Corporation to do business under the assumed name of Vyvx, within any state.

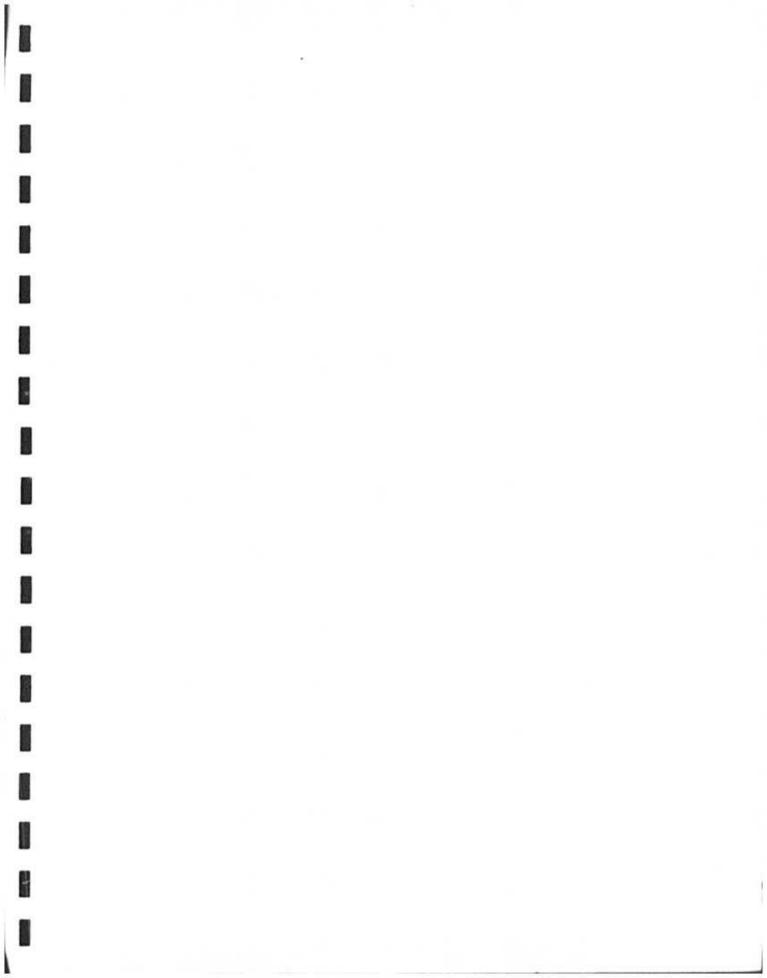
I further certify that the foregoing resolution has not been modified, revoked or rescinded and is in full force and effect.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of WILLIAMS COMMUNICATIONS, INC., this 17th day of March, 1998.

David M. Higbee Secretary

(CORPORATE SEAL)

H:\CORPSEC\MINUTES\VYVX\VYVX.RES



Form 10-K

SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549

(Mark One)

 \otimes

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES AND EXCHANGE ACT OF 1934 (FEE REQUIRED) For the fiscal year ended December 31, 1995

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 (NO FEE REQUIRED)

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

(State or other jurisdiction of incorporation or organization)

73-0569878

(LR.S. Employer Identification No.)

One Williams Center Tulsa, Oklahoma

74172

(Zip Code)

(Address of principal executive office)

Registrant's Telephone Num

Registrant's Telephone Number: (918) 588-2000

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Each Class

Common Stock, \$1.00 par value Preferred Stock Purchase Rights \$2.21 Cumulative Preferred Stock, \$1.00 par value Name of Each Exchange on Which Registered

New York Stock Exchange and the Pacific Stock Exchange New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

None

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 ⊠ No □

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

The aggregate market value of the registrant's voting stock held by nonaffiliates as of the close of business on March 22, 1996, was approximately \$5.1 billion.

The number of shares of the registrant's Common Stock outstanding at March 22, 1996, was 104,651,013, excluding 2,280,246 shares held by the Company.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement prepared for the solicitation of proxies in connection with the Annual Meeting of Stockholders of the Company for 1996 are incorporated by reference in Part III.

THE WILLIAMS COMPANIES, INC. FORM 10-K PART I

Item 1. Business

(a) General Development of Business

The Williams Companies, Inc. (the "Company" or "Williams") was incorporated under the laws of the State of Nevada in 1949 and was reincorporated under the laws of the State of Delaware in 1987. The principal executive offices of the Company are located at One Williams Center, Tulsa, Oklahoma 74172 (telephone (918) 588-2000). Unless the context otherwise requires, references to the "Company" and "Williams" herein include The Williams Companies, Inc. and its subsidiaries.

On January 5, 1995, the Company sold the network services operations of Williams Telecommunications Group, Inc., its telecommunications subsidiary, to LDDS Communications, Inc. for \$2.5 billion in cash, (the "WNS Sale"). The Company retained Williams Telecommunications Systems, Inc., a telecommunications equipment supplier and service company, and Vyvx, Inc., which operates a video network specializing in broadcast television applications. The Company has reported the network services operations as discontinued operations for financial reporting purposes. See Note 3 of Notes to Consolidated Financial Statements. The Company used the proceeds from the WNS Sale to pay off short-term credit facilities, fund the acquisition of Transco Energy Company discussed below, finance its ongoing capital program and for other uses.

On December 12, 1994, the Company entered into a merger agreement with Transco Energy Company. Under the agreement, the Company acquired approximately 60 percent of Transco Energy Company's common stock through a cash tender offer completed in January 1995. On April 28, 1995, the Transco Energy Company stockholders approved an agreement and plan of merger whereby Transco Energy Company became a wholly owned subsidiary of the Company effective May 1, 1995. Total value of the transaction was more than \$3 billion, including cash, stock and the assumption of Transco Energy Company debt. As of May 1, 1995, the Company caused Transco Energy Company to declare and pay as dividends to the Company all of Transco Energy Company's interest in Transcontinental Gas Pipe Line Corporation and Texas Gas Transmission Corporation. In addition, the Company continued Transco Energy Company's program of disposing of noncore assets. See Note 2 of Notes to Consolidated Financial Statements.

On January 16, 1996, the Company acquired a 49.9 percent interest from its partner in Kern River Gas Transmission Company giving the Company 99.9 percent ownership of this natural gas pipeline system. The purchase price was \$205 million. See Note 5 of Notes to Consolidated Financial Statements.

(b) Financial Information About Industry Segments

See Part II, Item 8 - Financial Statements and Supplementary Data.

(c) Narrative Description of Business

The Company, through subsidiaries, is engaged in the transportation and sale of natural gas and related activities, natural gas gathering, processing and production activities, the transportation of petroleum products, natural gas trading, natural gas liquids marketing and provides a variety of other products and services to the energy industry and financial institutions. The Company also is engaged in the telecommunications business. In 1995, the Company's subsidiaries owned and operated: (i) four interstate natural gas pipeline systems and had a 50 percent interest in a fifth; (ii) a common carrier crude and petroleum products pipeline system; and (iii) natural gas gathering and processing facilities and production properties. The Company also trades natural gas and markets natural gas liquids. The Company's telecommunications subsidiaries offer data, voice

and video-related products and services and customer premises equipment nationwide. The Company also has investments in the equity of certain other companies. See Note 5 of Notes to Consolidated Financial Statements.

Substantially all operations of Williams are conducted through subsidiaries. Williams performs management, legal, financial, tax, consultative, administrative and other services for its subsidiaries. Williams' principal sources of cash are from dividends and advances from its subsidiaries, investments, payments by subsidiaries for services rendered by its staff and interest payments from subsidiaries on cash advances. The amount of dividends available to Williams from subsidiaries largely depends upon each subsidiary's earnings and operating capital requirements. The terms of certain subsidiaries' borrowing arrangements limit the transfer of funds to the Company. See Note 13 of Notes to Consolidated Financial Statements.

To achieve organizational and operating efficiencies, the Company's interstate natural gas pipelines are grouped together and are referred to internally as the interstate natural gas systems. All other operating companies are owned directly by Williams Holdings of Delaware, Inc., a wholly-owned subsidiary of the Company. Item 1 of this report is formatted to reflect this structure.

WILLIAMS INTERSTATE NATURAL GAS SYSTEMS

The Company's interstate natural gas pipeline group owns and operates a combined total of approximately 28,000 miles of pipelines with a total annual throughput of approximately 3,500 TBtu* of natural gas and peak-day delivery capacity of approximately 15 Bcf of natural gas. The interstate natural gas pipeline group consists of Transcontinental Gas Pipe Line Corporation, Northwest Pipeline Corporation, Texas Gas Transmission Corporation, Kern River Gas Transmission Company and Williams Natural Gas Company, owners and operators of interstate natural gas pipeline systems. As previously noted, Transcontinental Gas Pipe Line Corporation and Texas Gas Transmission Corporation were acquired by the Company in 1995. For the accounting treatment of the acquisition, see Note 2 of Notes to Consolidated Financial Statements. Also as noted above, the Company acquired an additional 49.9 percent interest in Kern River Gas Transmission Company in January 1996. The results of operations included herein only reflect the Company's previously-owned 50 percent ownership interest in Kern River.

The interstate natural gas pipeline group's transmission and storage activities are subject to regulation by the Federal Energy Regulatory Commission ("FERC") under the Natural Gas Act of 1938 ("Natural Gas Act") and under the Natural Gas Policy Act of 1978 ("NGPA"), and, as such, their rates and charges for the transportation of natural gas in interstate commerce, the extension, enlargement or abandonment of jurisdictional facilities, and accounting, among other things, are subject to regulation. Each pipeline holds certificates of public convenience and necessity issued by FERC authorizing ownership and operation of all pipelines, facilities and properties considered jurisdictional for which certificates are required under the Natural Gas Act. Each pipeline is also subject to the Natural Gas Pipeline Safety Act of 1968, as amended by Title I of the Pipeline Safety Act of 1979, which regulates safety requirements in the design, construction, operation and maintenance of interstate gas transmission facilities.

There follows a business description of each company in the interstate natural gas pipeline group. The discussion of certain items required to be disclosed by Form 10-K are reported in generic form following the individual company business descriptions.

TRANSCONTINENTAL GAS PIPE LINE CORPORATION (Transco)

Transco is an interstate natural gas transmission company which owns and operates a natural gas pipeline system extending from Texas, Louisiana, Mississippi and the offshore Gulf of Mexico through the states of Alabama, Georgia, South Carolina, North Carolina, Virginia, Maryland, Pennsylvania and New Jersey to the

^{*} The term "Mcf" means thousand cubic feet, "MMcf" means million cubic feet and "Bcf" means billion cubic feet. All volumes of natural gas are stated at a pressure base of 14.73 pounds per square inch absolute at 60 degrees Fahrenheit. The term "MMBtu" means one million British Thermal Units and "TB::" means one trillion British Thermal Units.

New York City metropolitan area. The system serves customers in Texas and the eleven southeast and Atlantic seaboard states mentioned above, including major metropolitan areas in Georgia, North Carolina, New York, New Jersey and Pennsylvania. Effective May 1, 1995, the operation of certain production area facilities were transferred to Williams Field Services Group, Inc., an affiliated company.

Pipeline System and Customers

At December 31, 1995, Transco's system had a mainline delivery capacity of approximately 3.7 Bcf of gas per day from production areas to its primary markets. Using its Leidy Line and market-area storage capacity, Transco can deliver an additional 2.7 Bcf of gas per day for a system-wide delivery capacity total of approximately 6.4 Bcf of gas per day. Excluding the production area facilities operated by Williams Field Services Group, Inc., Transco's system is composed of approximately 7,300 miles of mainline and branch transmission pipelines, 37 compressor stations and six storage locations. Compression facilities at a sea level rated capacity total approximately 1.2 million horsepower.

Transco's major gas transportation customers are public utilities and municipalities that provide residential service to approximately 35 million people and serve numerous commercial and industrial users. Shippers on Transco's pipeline system include public utilities, municipalities, intrastate pipelines, direct industrial users, electrical generators, marketers and producers. Transco's largest customer in 1995 accounted for approximately 14 percent of Transco's total operating revenues. No other customer accounted for more than 10 percent of total operating revenues. Transco's firm transportation agreements are generally long-term agreements with various expiration dates and account for the major portion of Transco's business. Additionally, Transco offers interruptible transportation services under agreements that are generally short term.

Transco has natural gas storage capacity in five underground storage fields located on or near its pipeline system and/or market areas and operates three of these storage fields and a liquefied natural gas (LNG) storage facility. The total storage capacity available to Transco and its customers from such storage fields and LNG facility is approximately 219 Bcf of gas. Storage capacity permits Transco's customers to inject gas into storage during the summer and off-peak periods for delivery during peak winter demand periods.

Major Expansion Projects

In August 1995, Transco announced its SeaBoard 97 Expansion Project. The project is expected to provide an additional 115 MMcf of gas per day of firm transportation capacity from points of receipt on Transco's Leidy Line to Transco's northeastern market area by the 1997-1998 winter heating season. To render this service, Transco will construct compression and pipeline looping facilities at an estimated cost of \$115 million. Transco plans to file in mid-1996 for FERC approval of the project.

In October 1995, Transco filed for FERC approval of the SunBelt Expansion Project. The project will provide additional firm transportation capacity to markets in Georgia, South Carolina and North Carolina. The SunBelt Expansion Project will provide a total of 146 MMcf of gas per day of firm transportation capacity to existing and new Transco customers by the 1997-1998 winter heating season. Transco's FERC application estimates the cost of the expansion to be approximately \$85 million.

In November 1995, Transco announced the filing for FERC approval of the Pine Needle LNG storage project. The facility is to be constructed and owned by Transco and several of its major customers and will be located near Transco's mainline system in Guilford, North Carolina. The project will have 4 Bcf of storage capacity and 400 MMcf of gas per day of withdrawal capacity. Transco will operate the facility and have a 35 percent ownership interest. The project is expected to be in service by the second quarter of 1999. The FERC application estimates the cost of the project to be \$107 million.

In December 1995, Transco and several major customers announced the Cardinal Pipeline System project. The project involves the acquisition of an existing 37-mile pipeline in North Carolina and construction of a 65-mile pipeline extension. Construction of the pipeline extension is expected to be completed by the end of 1999. Transco will operate the expanded pipeline system and have a 45 percent ownership interest. Total costs of the acquisition and extension are expected to be \$97 million.

Transco's 1994 Southeast Expansion Project was completed and placed into service in November 1994, and provides 35 MMcf of gas per day of additional firm transportation capacity to Transco's customers in the southeast. Phase I of Transco's 1995/1996 Southeast Expansion Project was completed and placed into service in December 1995, and provides 115 MMcf of gas per day of additional firm transportation capacity to Transco's customers in the Southeast. Phase II of such expansion will add an additional 55 MMcf of gas per day for the 1996-1997 winter heating season. Transco invested \$63 million in these projects in 1995 and expects to invest approximately \$21 million in these projects in 1996.

Operating Statistics

The following table summarizes transportation data for the periods indicated, including periods during which the Company did not own Transco:

All the second s	1995	1994	1993
System Deliveries (TBtu)			
Market-area deliveries:			
Long-haul transportation	858.4	805.1	852.0
Market-area transportation	467.3	453.6	387.4
Total market-area deliveries	1,325.7	1,258.7	1,239.4
Production-area transportation	165.9	185.9	177.5
Total system deliveries	1,491.6	1,444.6	1,416.9
Average Daily Transportation Volumes (TBtu)	4.1	4.0	3.9
Average Daily Firm Reserved Capacity (TBtu)	5.2	4.9	4.8

Transco has expressed concerns to FERC that inconsistent treatment of Transco and its competitor pipelines with regard to rate design and cost allocation issues in production areas may result in rates which could make Transco less competitive, both in terms of production-area and long-haul transportation. On July 19, 1995, an administrative law judge (ALJ) issued an initial decision finding that Transco's proposed production area rate design, and its existing use of a system-wide cost of service and allocation of firm capacity in production areas are unjust and unreasonable. The ALJ recommended that Transco divide its costs between its production area and market area and permit its customers to renominate their firm entitlements. The ALJ's decision is subject to review by FERC. Should FERC issue an order consistent with the ALJ's recommendations, such order would have prospective effect only.

NORTHWEST PIPELINE CORPORATION (Northwest Pipeline)

Northwest Pipeline is an interstate natural gas transmission company which owns and operates a pipeline system for the mainline transmission of natural gas extending from the San Juan Basin in northwestern New Mexico and southwestern Colorado through Colorado, Utah, Wyoming, Idaho, Oregon and Washington to a point on the Canadian border near Sumas, Washington. Northwest Pipeline provides services for markets in California, New Mexico, Colorado, Utah, Nevada, Wyoming, Idaho, Oregon and Washington, directly or indirectly through interconnections with other pipelines.

Pipeline System and Customers

At December 31, 1995, Northwest Pipeline's system, having an aggregate mainline deliverability of approximately 2.6 Bcf of gas per day was composed of approximately 3,900 miles of mainline and branch transmission pipelines and 43 mainline compressor stations with a combined capacity of approximately 306,000 horsepower.

In 1995, Northwest Pipeline transported natural gas for a total of 127 customers. Transportation customers include distribution companies, municipalities, interstate and intrastate pipelines, gas marketers and direct industrial users. The three largest customers of Northwest Pipeline in 1995 accounted for approximately 18.5 percent, 12.2 percent and 10.2 percent, respectively, of total operating revenues. No other customer

accounted for more than 10 percent of total operating revenues. Northwest Pipeline's firm transportation agreements are generally long-term agreements with various expiration dates and account for the major portion of Northwest Pipeline's business. Additionally, Northwest Pipeline offers interruptible transportation service under agreements that are generally short term. Northwest Pipeline's transportation services represented 100 percent of its total throughput in 1995.

Northwest Pipeline completed mainline expansion projects that were placed into service on December 1, 1995. These expansion projects increased system capacity by an additional 144 MMcf of gas per day and added 14,820 horsepower of new compression and 44 miles of pipeline loop line to Northwest Pipeline's system.

As a part of its transportation services, Northwest Pipeline utilizes underground storage facilities in Utah and Washington enabling it to balance daily receipts and deliveries. Northwest Pipeline also owns and operates a liquefied natural gas storage plant in Washington which provides a needle-peaking service for the system. These storage facilities have an aggregate delivery capacity of approximately 973 MMcf of gas per day.

Operating Statistics

The following table summarizes gas sales and transportation data for the periods indicated:

	1995	1994	1993
Gas Volumes (TBtu):			
Gas sales	-	-	18
Transportation	826	679	606
Total throughput	826	679	624
Average Daily Transportation Volumes (TBtu)		1.9	1.7
Average Daily Firm Reserved Capacity (TBtu)		2.4	-

TEXAS GAS TRANSMISSION CORPORATION (TXG)

TXG is an interstate natural gas transmission company which owns and operates a natural gas pipeline system originating in the Louisiana Gulf Coast area and in east Texas and running generally north and east through Louisiana, Arkansas, Mississippi, Tennessee, Kentucky, Indiana and into Ohio, with smaller diameter lines extending into Illinois. TXG's direct market area encompasses eight states in the South and Midwest, and includes the Memphis, Tennessee, Louisville, Kentucky, Cincinnati and Dayton, Ohio, and Indianapolis, Indiana, metropolitan areas. TXG also has indirect market access to the Northeast through interconnections with unaffiliated pipelines.

Pipeline System and Customers

At December 31, 1995, TXG's system, having a mainline delivery capacity of approximately 2.7 Bcf of gas per day, was composed of approximately 6,000 miles of mainline and branch transmission pipelines and 32 compressor stations having a sea level rated capacity totaling approximately 548,000 horsepower.

In 1995, TXG transported gas to customers in Louisiana, Arkansas, Mississippi, Tennessee, Kentucky, Indiana, Illinois and Ohio and to customers in the Northeast served indirectly by TXG. Gas was transported for 130 distribution companies and municipalities for resale to residential, commercial and industrial users. Transportation services were provided to approximately 200 industrial customers and processing plants located along the system. At December 31, 1995, TXG had transportation contracts with approximately 625 shippers. Transportation shippers include distribution companies, municipalities, intrastate pipelines, direct industrial users, electrical generators, marketers and producers. The largest customer of TXG in 1995 accounted for approximately 11 percent of total operating revenues. No other customer accounted for more than 10 percent of total operating revenues. TXG's firm transportation agreements are generally long-term agreements with various expiration dates and account for the major portion of TXG's business. Additionally, TXG offers interruptible transportation services under agreements that are generally short-term.

TXG owns and operates natural gas storage reservoirs in ten underground storage fields located on or near its pipeline system and/or market areas. The storage capacity of TXG's certificated storage fields is approximately 177 Bcf of gas. TXG's storage gas is used in part to meet operational balancing needs on its system, and in part to meet the requirements of TXG's "no-notice" transportation service, which allows TXG's customers to temporarily draw from TXG's storage gas to be repaid in-kind during the following summer season. A large portion of the gas delivered by TXG to its market area is used for space heating, resulting in substantially higher daily requirements during winter months.

Operating Statistics

The following table summarizes total system delivery data, which excludes unbundled sales, for the periods indicated, including periods during which the Company did not own TXG:

	1995	1994	1993
System deliveries (TBtu):			
Sales	-	-	52.8
Long-haul transportation	635.7	618.8	534.0
Total mainline deliveries	635.7	618.8	586.8
Short-haul transportation	57.6	188.6	214.0
Total system deliveries	693.3	807.4	800.8
Average Daily Transportation Volumes (TBtu)	1.9	2.2	2.0
Average Daily Firm Reserved Capacity (TBtu)	2.0	2.1	2.0

KERN RIVER GAS TRANSMISSION COMPANY (Kern River)

Kern River is an interstate natural gas transmission company which owns and operates a natural gas pipeline system extending from Wyoming through Utah and Nevada to California. In 1995, Kern River was jointly owned and operated by Williams Western Pipeline Company, a subsidiary of the Company, and a subsidiary of an unaffiliated company. As previously indicated, the Company acquired an additional 49.9 percent interest in Kern River in January 1996. See Note 5 of Notes to Consolidated Financial Statements. The transmission system, which commenced operations in February 1992 following completion of construction, delivers natural gas primarily to the enhanced oil recovery fields in southern California. The system also transports natural gas for utilities, municipalities and industries in California, Nevada and Utah.

Pipeline System and Customers

As of December 31, 1995, Kern River's pipeline system was composed of 707 miles of pipeline and three mainline compressor stations having an aggregate mainline delivery capacity of 700 MMcf of gas per day. The pipeline system interconnects with the pipeline facilities of another pipeline company at Daggett, California. From the point of interconnection, Kern River and the other pipeline company have a common 219-mile pipeline which is owned 63.6 percent by Kern River and 36.4 percent by the other pipeline company, as tenants in common, and is designed to accommodate the combined throughput of both systems. This common facility has a capacity of 1.1 Bcf of gas per day.

Gas is transported for others under firm long-term transportation contracts totaling 682 MMcf of gas per day. In 1995, Kern River transported natural gas for customers in California, Nevada and Utah. Gas was transported for five customers in Kern County, California, for reinjection as a part of enhanced oil recovery operations and for 28 local distribution customers, electric utilities, cogeneration projects and commercial and other industrial customers. The five largest customers of Kern River in 1995 accounted for approximately 14 percent, 14 percent, 12 percent, 12 percent and 10 percent, respectively, of operating revenues. Three of these customers serve the enhanced oil recovery fields. No other customer accounted for more than 10 percent of operating revenues in 1995.

During 1995, a seasonal firm transportation contract was executed to deliver natural gas into the Las Vegas, Nevada, market area during the winter months. Deliveries of 10 MMcf of gas per day will be initiated in December 1997 and will escalate to 40 MMcf of gas per day on a seasonal basis in 1999.

Operating Statistics

The following table summarizes transportation data for the periods indicated:

	1995	1994	1993
Transportation Volumes (TBtu)	286	278	272
Average Daily Transportation Volumes (TBtu)	.78	.76	.75
Average Daily Firm Reserved Capacity (TBtu)	.72	.74	.74

WILLIAMS NATURAL GAS COMPANY (Williams Natural Gas)

Williams Natural Gas is an interstate natural gas transmission company which owns and operates a natural gas pipeline system located in Colorado, Kansas, Missouri, Nebraska, Oklahoma, Texas and Wyoming. The system serves customers in seven states, including major metropolitan areas of Kansas and Missouri, its chief market areas.

Pipeline System and Customers

At December 31, 1995, Williams Natural Gas' system, having a mainline delivery capacity of approximately 2.2 Bcf of gas per day, was composed of approximately 6,300 miles of mainline and branch transmission and storage pipelines and 41 compressor stations having a sea level rated capacity totaling approximately 240,000 horsepower.

In 1995, Williams Natural Gas transported gas to customers in Colorado, Kansas, Missouri, Nebraska, Oklahoma, Texas and Wyoming. Gas was transported for 77 distribution companies and municipalities for resale to residential, commercial and industrial users in approximately 530 cities and towns. Transportation services were provided to approximately 350 industrial customers, federal and state institutions and agricultural processing plants located principally in Kansas, Missouri and Oklahoma. At December 31, 1995, Williams Natural Gas had transportation contracts with approximately 203 shippers. Transportation shippers included distribution companies, municipalities, intrastate pipelines, direct industrial users, electrical generators, marketers and producers.

In 1995, approximately 35 percent and 33 percent, respectively, of total operating revenues were generated from gas transportation services to Williams Natural Gas' two largest customers, Western Resources, Inc. and Missouri Gas Energy Company. Western Resources sells or resells gas to residential, commercial and industrial customers principally in certain major metropolitan areas of Kansas. Missouri Gas Energy sells or resells gas to residential, commercial and industrial customers principally in certain major metropolitan areas of Missouri. No other customer accounted for more than 10 percent of operating revenues during 1995.

A significant portion of the transportation services provided to Western Resources is pursuant to a twenty-year transportation service agreement. After the initial two-year period ending in November 1996, the contract allows Western Resources, on twelve months prior notice, to reduce contracted capacity if Williams Natural Gas does not meet the terms of a competing offer from another natural gas pipeline to serve such capacity. Transportation services are provided to Missouri Gas Energy under contracts primarily varying in terms from two to five years. These contracts do not have "competitive out" provisions as described in connection with the Western Resources' contract. During 1995, these two customers entered into contracts with a competitor as part of a litigation settlement. The Western Resources contracts are subject to state regulatory approval and hearings before the Kansas Corporation Commission (KCC) which were conducted in September 1995. A decision on whether to approve the contracts has been stayed by the KCC in light of an October 1995 FERC ruling asserting federal jurisdiction over the competitor. The competitor has appealed the FERC decision, as well as the authority of the KCC to stay the contracts approval proceeding. While the

Missouri Gas Energy contracts with this competitor are not subject to Missouri Public Service Commission approval, the exercise of FERC jurisdiction over the project could cause the cancellation of the proposed pipeline project that supports the contracts. Up to 25 percent of the firm capacity now transported by Williams Natural Gas into the Kansas City market could be at risk if the pipeline contemplated by the contracts is built. If FERC's decision to exercise jurisdiction over the competing pipeline is upheld, the competitor will be required to formulate rate structures under the same rules as Williams Natural Gas and other interstate competitors.

Williams Natural Gas operates nine underground storage fields with an aggregate working gas storage capacity of approximately 43 Bcf and an aggregate delivery capacity of approximately 1.2 Bcf of gas per day. Williams Natural Gas' customers inject gas in these fields when demand is low and withdraw it to supply their peak requirements. During periods of peak demand, approximately two-thirds of the firm gas delivered to customers is supplied from these storage fields. Storage capacity enables the system to operate more uniformly and efficiently during the year.

Operating Stutistics

The following table summarizes gas sales and transportation data for the periods indicated:

	1995	1994	1993
Volumes (TBtu):			
Resale sales	_	-	50
Direct and gas processing plant sales	-	_	1
Transportation	334	346	344
Total throughput	334	346	395
Average Daily Transportation Volumes (TBtu)	.9	.9	.9
Average Daily Firm Reserved Capacity (TBtu)	2.0	2.0	_

Certain of Williams Natural Gas' gathering and processing activities have been or will be transferred to third parties, including subsidiaries of Williams Field Services Group, Inc., an affiliated company, as discussed elsewhere herein. Applications for orders permitting and approving abandonment of certain natural gas facilities have been filed with FERC and final approval has been granted by FERC on three of these filings. Preliminary approval on all other systems has been granted by FERC.

REGULATORY MATTERS

In 1992, FERC issued Order 636 which required interstate pipelines to restructure their tariffs to eliminate traditional on-system sales services. In addition, the Order required implementation of various changes in forms of service, including unbundling of gathering, transmission and storage services; terms and conditions of service; rate design; gas supply realignment cost recovery; and other major rate and tariff revisions. Williams Natural Gas implemented its restructuring on October 1, 1993, and Transco, Northwest Pipeline and TXG implemented their restructurings on November 1, 1993. Certain aspects of each pipeline company's Order 636 restructuring are under appeal.

Each interstate natural gas pipeline has various regulatory proceedings pending. Rates are established primarily through FERC's ratemaking process. Key determinants in the ratemaking process are (1) costs of providing service, including depreciation rates, (2) allowed rate of return, including the equity component of the capital structure, and (3) volume throughput assumptions. The allowed rate of return is determined by FERC in each rate case. Rate design and the allocation of costs between the demand and commodity rates also impact profitability. As a result of such proceedings, a portion of the revenues of these pipelines may have been collected subject to refund. See Note 12 of Notes to Consolidated Financial Statements for the amount of revenues reserved for potential refund as of December 31, 1995.

Each interstate natural gas pipeline, with the exception of Kern River, has undertaken the reformation of its respective gas supply contracts. None of the pipelines has any significant pending supplier take-or-pay,

ratable-take or minimum-take claims. For information on outstanding issues with respect to contract reformation, gas purchase deficiencies and related regulatory issues, see Note 17 of Notes to Consolidated Financial Statements.

COMPETITION

Competition for natural gas transportation has intensified in recent years due to customer access to other pipelines, rate competitiveness among pipelines, customers' desire to have more than one supplier and regulatory developments. FERC's stated purpose for implementing Order 636 was to improve the competitive structure of the natural gas pipeline industry. Future utilization of pipeline capacity will depend on competition from other pipelines and alternative fuels, the general level of natural gas demand and weather conditions. Electricity and distillate fuel oil are primary competitive forms of energy for residential and commercial markets. Coal and residual fuel oil compete for industrial and electric generation markets. Nuclear power and power purchased from grid arrangements among electric utilities also compete with gas-fired power generation in certain markets.

As mentioned, when restructured tariffs became effective under Order 636, all suppliers of natural gas were able to compete for any gas markets capable of being served by the pipelines using nondiscriminatory transportation services provided by the pipelines. As the Order 636 regulated environment has matured, many pipelines have faced reduced levels of subscribed capacity as contractual terms expire and customers opt to reduce firm capacity under contract in favor of alternative sources of transmission and related services. This issue, known as "capacity turnback" in the industry, is forcing the pipelines to evaluate the consequences of major demand reductions on system utilization and cost structure to remaining customers.

The Company is aware that several state jurisdictions have been involved in implementing changes similar to the changes that have occurred at the federal level under Order 636. Such activity, frequently referred to as "LDC unbundling," has been most pronounced in the states of New York, New Jersey and Pennsylvania. In New York and New Jersey, regulations regarding "LDC unbundling" were enacted during the past year, and Pennsylvania is expected to act on an "LDC unbundling" program in 1996. It is expected that these regulations will encourage greater competition in the natural gas marketplace.

OWNERSHIP OF PROPERTY

The facilities of each interstate natural gas pipeline are generally owned in fee. However, a substantial portion of each pipeline's facilities is constructed and maintained pursuant to rights-of-way, easements, permits, licenses or consents on and across properties owned by others. Compressor stations, with appurtenant facilities, are located in whole or in part either on lands owned or on sites held under leases or permits issued or approved by public authorities. The storage facilities are either owned or contracted under long-term leases or easements.

ENVIRONMENTAL MATTERS

Each interstate natural gas pipeline is subject to the National Environmental Policy Act and federal, state and local laws and regulations relating to environmental quality control. Management believes that, with respect to any capital expenditures and operation and maintenance expenses required to meet applicable environmental standards and regulations, FERC would grant the requisite rate relief so that, for the most part, such expenditures would be recoverable in rates. For this reason, management believes that compliance with applicable environmental requirements by the interstate pipelines is not likely to have a material effect upon the Company's earnings or competitive position.

For a discussion of specific environmental issues involving the interstate pipelines, including estimated cleanup costs associated with certain pipeline activities, see "Environmental" under Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 17 of Notes to Consolidated Financial Statements.

WILLIAMS HOLDINGS OF DELAWARE, INC. (Williams Holdings)

In 1994, the Company established Williams Holdings to be a holding company for its assets other than its interstate natural gas pipelines and related assets. Virtually all of Williams Holdings' assets have been transferred to it by the Company since January 1, 1995, and were previously operated by subsidiaries of the Company.

Williams Holdings owns all of the capital stock of four entities in the energy industry and two entities in the telecommunications industry. Williams Holdings' energy subsidiaries are engaged in natural gas gathering, processing and production, the transportation of crude oil and petroleum products, natural gas trading activities, natural gas liquids marketing and provide a variety of other products and services to the energy industry. Williams Holdings' telecommunications subsidiaries offer data, voice and video-related products and services and customer premise equipment nationwide. Williams Holdings also has certain other equity investments. See Note 5 of Notes to Consolidated Financial Statements.

WILLIAMS FIELD SERVICES GROUP, INC. (Williams Field Services)

Williams Field Services, through subsidiaries, owns and/or operates both regulated and nonregulated natural gas gathering and processing facilities and owns and operates natural gas leasehold properties. In 1995 and 1994, gathering and processing activities represented 98 percent and 89 percent, respectively, of Williams Field Services' operating profit. Natural gas production represented the balance.

In 1995, Williams Field Services completed an expansion of its Manzanares coal seam gas gathering systems in northwestern New Mexico increasing capacity of the systems to over 1 Bcf of gas per day. A plant expansion in the Wamsutter field of south-central Wyoming completed in the fourth quarter of 1995 increased capacity of this field to 240 MMcf of gas per day. Also in 1995, Williams Field Services completed the construction of a 75 MMcf of gas per day processing plant in the Oklahoma Panhandle.

Effective May 1, 1995, the Company transferred to Williams Field Services the operation of certain production area transmission assets and certain gathering and processing assets which the Company had acquired as of such date from Transco Energy Company. The production area transmission assets consist of approximately 3,500 miles of pipeline located in gas producing areas offshore and onshore in Texas and Louisiana which are currently owned by Transco and classified by FERC as interstate transmission lines. The gathering assets consist of nonjurisdictional and intrastate gas gathering lines located offshore and onshore in Texas. Such facilities consist of approximately 28 miles of gathering pipelines. The processing assets consist of two natural gas processing facilities. The first is a 50 percent joint ownership interest in a processing facility with a 500 MMcf per day capacity located in southwestern Louisiana and the second is a 50 percent partnership interest in a 60 MMcf per day cryogenic extraction facility located in south Texas.

In June 1995, Williams Field Services acquired the natural gas gathering and processing assets of Public Service Company of New Mexico located in the San Juan and Permian basins of New Mexico for \$154 million. Williams Field Services immediately thereafter sold the southeastern New Mexico portion of the acquired assets for \$14.2 million. The assets retained consist of approximately 1,400 miles of gathering pipelines and three gas processing plants which have an aggregate daily inlet capacity of 300 MMcf of gas.

Williams Field Services' first nonregulated merchant power plant is scheduled to begin operation in New Mexico in 1996. The \$53 million 62-megawatt facility, powered by coal-seam gas, will produce electricity, which will be sold under a long-term contract. Other areas on Williams Field Services' system hold the potential for similar cogeneration investments.

Gathering and Processing

Williams Field Services, through subsidiaries, owns and operates natural gas gathering and processing facilities located in the San Juan Basin in northwestern New Mexico and southwestern Colorado, southwest Wyoming, the Rocky Mountains of Utah and Colorado, northwest Oklahoma, Louisiana and also in areas offshore and onshore in Texas. Williams Field Services, through subsidiaries, also operates natural gas gathering and processing facilities located in the Texas Panhandle and the Hugoton Basin in northwest

Oklahoma and southwest Kansas, which are owned by Williams Natural Gas, an affiliated company, and operates natural gas gathering and processing facilities located both onshore and offshore in Texas and Louisiana, which are owned by Transco, an affiliated company. The facilities operated for affiliates are the subject of applications for orders permitting abandonment so the facilities can be transferred to Williams Field Services. Gathering services provided include the gathering of gas and treating of coal seam gas.

Customers and Operations. Facilities owned and operated by Williams Field Services consist of approximately 12,000 miles of gathering pipelines, 11 gas treating plants and 14 gas processing plants (five of which are partially owned) which have an aggregate daily inlet capacity of 6.7 Bcf of gas. Gathering and processing customers have direct access to interstate pipelines, including affiliated pipelines, which provide access to multiple markets.

During 1995, Williams Field Services gathered natural gas for 286 customers. The largest gathering customer accounted for approximately 18 percent of total gathered volumes. During 1995, natural gas was processed for a total of 108 customers. The three largest customers accounted for approximately 26 percent, 12 percent and 11 percent, respectively, of total processed volumes. No other customer accounted for more than 10 percent of gathered or processed volumes. Williams Field Services' gathering and processing agreements with large customers are generally long-term agreements with various expiration dates. These long-term agreements account for the majority of the gas gathered and processed by Williams Field Services.

Liquids extracted at the processing plants are ethane, propane, butane and natural gasoline. During 1995, liquid products were sold to a total of 52 customers under short-term contracts. The four largest customers accounted for approximately 32 percent, 18 percent, 16 percent and 15 percent, respectively, of total liquid products volumes sold. No other customer accounted for more than 10 percent of volumes sold.

Operating Statistics. The following table summarizes gathering, processing and natural gas liquid volumes for the periods indicated. The information includes operations attributed to facilities owned by affiliated entities but operated by Williams Field Services:

	1995	1994	1993
Gas volumes (TBtu, except where noted):			
Gathering	1,806	895	789
Processing	406	392	323
Natural gas liquid sales (millions of gallons)	298	281	295

Production

Williams Field Services, through a subsidiary, owns and operates producing gas leasehold properties in Colorado, Louisiana, New Mexico, Utah and Wyoming.

Gas Reserves. As of December 31, 1995, 1994 and 1993, Williams Field Services had proved developed natural gas reserves of 292 Bef, 269 Bef and 229 Bef, respectively, and proved undeveloped reserves of 222 Bef, 220 Bef and 319 Bef, respectively. Of Williams Field Services' total proved reserves, 96 percent are located in the San Juan Basin of Colorado and New Mexico. As discussed below, Williams Field Services conveyed gas reserves to the Williams Coal Seam Gas Royalty Trust in 1993. No major discovery or other favorable or adverse event has caused a significant change in estimated gas reserves since year end.

Customers and Operations. As of December 31, 1995, the gross and net developed leasehold acres owned by Williams Field Services totaled 261,973 and 107,046, respectively, and the gross and net undeveloped acres owned were 152,977 and 44,296, respectively. As of such date, Williams Field Services owned interests in 2,795 gross producing wells (496 net) on its leasehold lands. The following table summarizes drilling activity for the periods indicated:

		pment
Completed During	Gross Wells	Net Wells
1995		22
1994	66	19
1993	39	2

The majority of Williams Field Services' gas production is currently being sold in the spot market at market prices. Total net production sold during 1995, 1994 and 1993 was 25.9 TBtu, 22.6 TBtu and 16.3 TBtu, respectively. The average production costs per MMBtu of gas produced were \$.14, \$.14 and \$.17 in 1995, 1994 and 1993, respectively. The average sales price per MMBtu was \$.88, \$1.21 and \$1.44, respectively, for the same periods.

In 1993, Williams Field Services conveyed a net profits interest in certain of its properties to the Williams Coal Seam Gas Royalty Trust. Trust Units were subsequently sold to the public by Williams in an underwritten public offering. The Company holds 3,568,791 Trust Units representing 36.8 percent of outstanding Units. Substantially all of the production attributable to the properties conveyed to the Trust was from the Fruitland coal formation and constituted coal seam gas. Proved developed coal seam gas reserves at December 31, 1995, attributed to the properties conveyed were 163 Bcf. Production information reported herein includes Williams Field Services' interest in such Units.

Regulatory Matters

Historically, an issue has existed as to whether FERC has authority under the Natural Gas Act to regulate gathering and processing prices and services. During 1994, after reviewing its legal authority in a Public Comment Proceeding, FERC determined that while it retains some regulatory jurisdiction over gathering and processing performed by interstate pipelines, pipeline affiliated gathering and processing companies are outside its authority under the Natural Gas Act. Orders issued in 1994 which implement FERC's conclusion that it lacks jurisdiction have been appealed to the United States Court of Appeals for the District of Columbia Circuit. Williams Field Services cannot predict the ultimate outcome of these proceedings.

As a result of these FERC decisions, several of the individual states in which Williams Field Services operates may consider whether to impose regulatory requirements on gathering companies. No state currently regulates Williams Field Services' gathering or processing rates or services.

Competition

Williams Field Services competes for gathering and processing business with interstate and intrastate pipelines, producers and independent gatherers and processors. Numerous factors impact any given customer's choice of a gathering or processing services provider, including rate, term, timeliness of well connections, pressure obligations and the willingness of the provider to process for either a fee or for liquids taken in-kind.

Ownership of Property

Williams Field Services' gathering and processing facilities are owned in fee. Gathering systems are constructed and maintained pursuant to rights-of-way, easements, permits, licenses and consents on and across properties owned by others. The compressor stations and gas processing and treating facilities are located in whole or in part on lands owned by Williams Field Services or on sites held under leases or permits issued or approved by public authorities.

Environmental Matters

Williams Field Services is subject to various federal, state and local laws and regulations relating to environmental quality control. Management believes that Williams Field Services' operations are in substantial compliance with existing environmental legal requirements. Management expects that compliance with such existing environmental legal requirements will not have a material adverse effect on the capital expenditures, earnings and competitive position of Williams Field Services.

WILLIAMS ENERGY SERVICES COMPANY (WESCO)

WESCO, through subsidiaries, offers a full range of products and services to energy markets throughout North America. WESCO's core business includes natural gas and energy commodity trading activities, energy-related price-risk management products and services and computer-based information products. WESCO was incorporated in 1993. See Note 15 of Notes to Consolidated Financial Statements.

Trading Activities and Services

In addition to its own natural gas trading operations, WESCO conducts certain natural gas trading operations formerly conducted by a subsidiary of Transco Energy Company as well as third party trading activities managed by an affiliate. WESCO trades natural gas throughout North America, primarily serving local distribution company markets in the eastern and midwestern United States. The Operating Statistics presented below, for periods prior to 1995, represent previously existing financial trading services conducted by Williams subsidiaries, coupled with third-party trading services provided by an affiliate and do not include operations previously conducted by the Transco Energy Company subsidiary.

WESCO serves a customer base of approximately 700 companies across its natural gas trading operations, with net revenues primarily derived from sales to local distribution companies, other gas marketers and certain end-users. WESCO's gas trading activities are conducted on both interstate and intrastate pipelines, with most sales activity coordinated with transportation along pipeline systems owned by Williams.

WESCO offers financial instruments and derivatives to producers and consumers of energy as well as to financial entities participating in energy price-risk management. WESCO also enters into energy-related financial instruments to manage market price fluctuations. The customer base for these activities is comprised of other gas marketing and trading companies, energy-based entities and brokers trading in energy commodities. See Note 15 of Notes to Consolidated Financial Statements.

Information Products

In 1995, WESCO marketed various computer-based trading and trader-match services including Chalkboard, an electronic trader-match system for buyers and sellers of liquid fuels, crude oil and refined products; Streamline, a physical cash forward gas trading system located at seven U.S. hubs; and Capacity Central, a natural gas pipeline capacity information system. These products are utilized primarily by a customer base of approximately 200 energy-based companies under short-term service commitments. The information products' architecture was developed in 1993 and introduced to the marketplace in 1994. These activities have not been profitable to date as costs of establishing marketing liquidity and product usage still outpace the returns from this developing market.

Effective January 1, 1996, Streamline and Capacity Central were contributed to a limited liability company along with the energy-related information services of a PanEnergy Corp. subsidiary. The new entity (Altra Energy Technologies, L.L.C.) is owned equally by WESCO and PanEnergy.

Operating Statistics (dollars in millions, volumes in TBtu)

	1995	1994	1993
Operating profit	\$30.0	\$.5	\$ 7.9
Natural gas physical trading		148	152

Regulatory Matters

Management believes that WESCO's natural gas trading activities are conducted in substantial compliance with the marketing affiliate rules of FERC Order 497. Order 497 imposes certain nondiscrimination, disclosure and separation requirements upon interstate natural gas pipelines with respect to their natural gas trading affiliates. WESCO has taken steps to ensure it does not share employees with affiliated interstate natural gas pipelines and does not receive information from such affiliates that is not also available to unaffiliated natural gas trading companies.

Competition

WESCO's gas trading operations are in direct competition with large independent gas marketers, marketing affiliates of regulated pipelines and natural gas producers. The financial trading business competes with other energy-based companies offering similar services as well as certain brokerage houses. This level of competition contributes to a business environment of constant pricing and margin pressure.

Ownership of Property

The primary assets of WESCO are its term contracts, employees and related technological support. Costs to develop the information products and certain trading systems have been capitalized.

Environmental Matters

WESCO is subject to federal, state and local laws and regulations relating to the environmental aspects of its business. Management believes that WESCO is in substantial compliance with existing environmental legal requirements for its business. Management expects that compliance with such existing environmental legal requirements will not have a material adverse effect on the capital expenditures, earnings and competitive position of WESCO.

WILLIAMS PIPE LINE COMPANY (Williams Pipe Line)

Williams Pipe Line operates a crude oil and petroleum products pipeline system which covers an 11-state area extending from Oklahoma in the south to North Dakota and Minnesota in the north and Illinois in the east. The system is operated as a common carrier offering transportation and terminalling services on a nondiscriminatory basis under published tariffs. The system transports refined products, LP-gases, lube extracted fuel oil and crude oil.

Shippers and Pipeline System

At December 31, 1995, the system traversed approximately 7,000 miles of right-of-way and included over 9,200 miles of pipeline in various sizes up to 16 inches in diameter. The system includes 82 pumping stations, 23 million barrels of storage capacity and 47 delivery terminals. The terminals are equipped to deliver refined products into tank trucks and tank cars. The maximum number of barrels which the system can transport per day depends upon the operating balance achieved at a given time between various segments of the system. Since the balance is dependent upon the mix of products to be shipped and the demand levels at the various delivery points, the exact capacity of the system cannot be stated.

The operating statistics set forth below relate to the system's operations for the periods indicated:

	1995	1994	1993
Shipments (thousands of barrels):			
Refined products:			
Gasolines	125,060	120,682	109,841
Distillates	61,238	61,129	51,508
Aviation fuels	12,535	9,523	11,123
LP-Gases	12,839	10,849	9,778
Lube extracted fuel oil	4.462	0	0
Crude oil	860	1,062	3,388
Total shipments	216,994	203,245	185,638
Daily average (thousands of barrels)	595	557	509
Average haul (miles)	269	284	279
Barrel miles (millions)	58,326	57,631	51,821
Revenues (millions):			
Transportation	\$177.0	\$168.0	\$153.0
Nontransportation	65.7	41.7	26.3
	\$242.7	\$209.7	\$179.3
Average transportation revenue per barrel	\$.82	\$.83	\$.82

Williams Pipe Line began moving a new lube extracted fuel oil product in 1995 from an Oklahoma refinery to Toledo, Ohio, through a joint movement with other carriers. Volume movements approximate 28 thousand barrels per day.

In 1995, 73 shippers transported volumes through the system. The seven largest shippers accounted for 54 percent of transportation revenues. The highest transportation revenue-producing shipper accounted for approximately 11 percent of transportation revenues in 1995. Nontransportation activities accounted for 27 percent of total revenues in 1995. The increase in nontransportation revenues is primarily due to expanded gas liquids operations.

At December 31, 1995, the system was directly connected to, and received products from, 11 operating refineries reported to have an aggregate crude oil refining capacity of over 900,000 barrels per day. Eight of these refineries are located in Kansas and Oklahoma, two in Minnesota and one in Wisconsin. The system also received products through connecting pipelines from other refineries located in Illinois, Indiana, Kansas, Louisiana, Montana, North Dakota, Oklahoma and Texas. Crude oil is received through connections in Kansas and Oklahoma. The refineries, which are connected directly or indirectly to the system, have access to a broad range of crude oil producing areas, including foreign sources. LP-gases are transported from gas producing and storage areas in central Kansas through connecting pipelines in Iowa, Kansas, Missouri, Illinois, Nebraska and South Dakota. In addition to making deliveries to company-owned terminals, the system delivers products to third-party terminals and connecting pipelines.

The refining industry continues to be affected by environmental regulations and changing crude supply patterns. The industry's response to environmental regulations and changing supply patterns will directly affect volumes and products shipped on the Williams Pipe Line system. EPA regulations, driven by the Clean Air Act, require refiners to change the composition of fuel manufactured. A pipeline's ability to respond to the effects of regulation and changing supply patterns will determine its ability to maintain and capture new market shares. Williams Pipe Line has successfully responded to changes in diesel fuel composition and product supply and has adapted to new gasoline additive requirements. Reformulated gasoline regulations have not yet significantly affected Williams Pipe Line. Williams Pipe Line will continue to position itself to respond to changing regulations and supply patterns, but it is not possible to predict how future changes in the marketplace will affect Williams Pipe Line's market areas.

Regulatory Matters

General. Williams Pipe Line, as an interstate common carrier pipeline, is subject to the provisions and regulations of the Interstate Commerce Act. Under this Act, Williams Pipe Line is required, among other things, to establish just, reasonable and nondiscriminatory rates, to file its tariffs with FERC, to keep its records and accounts pursuant to the Uniform System of Accounts for Oil Pipeline Companies, to make annual reports to FERC and to submit to examination of its records by the audit staff of FERC. Authority to regulate rates, shipping rules and other practices and to prescribe depreciation rates for common carrier pipelines is exercised by FERC. The Department of Transportation, as authorized by the 1992 Pipeline Safety Reauthorization Act, is the oversight authority for interstate liquids pipelines. Williams Pipe Line is also subject to the provisions of various state laws which are applicable to intrastate pipelines.

Rate Proceeding. On December 31, 1989, a rate cap, which resulted from a settlement with several shippers, effectively freezing Williams Pipe Line's rates for the previous five years, expired. Williams Pipe Line filed a revised tariff on January 16, 1990, with FERC and the state commissions. The tariff set an average increase in rates of 11 percent and established volume incentives and proportional rate discounts. Certain shippers on the Williams Pipe Line system and a competing pipeline carrier filed protests with FERC alleging that the revised rates are not just and reasonable and are unlawfully discriminatory. Williams Pipe Line elected to bifurcate this proceeding in accordance with the then-current FERC policy. Phase 1 of FERC's bifurcated proceeding provides a carrier the opportunity to justify its rates and rate structure by demonstrating that its markets are workably competitive. Any issues unresolved in Phase 1 require cost justification in Phase II.

The FERC's Phase I order, as modified by a rehearing decision, has found that Williams Pipe Line lacks significant market power and is workably competitive in 20 of the 32 markets under investigation. A shipper has appealed this decision to the United States Court of Appeals for the District of Columbia Circuit which has stayed the appeal proceedings until Phase II has been completed. Williams Pipe Line filed its direct evidence in Phase II on January 23, 1995. In this filing, Williams Pipe Line departed from the more traditional cost allocation methodology in lieu of an overall total system revenue requirement and stand-alone cost ceiling in conjunction with incremental and short-run marginal cost floors. The hearings began December 4, 1995, and concluded January 19, 1996. The current procedural schedule forecasts an initial decision in Phase II in mid-year 1996. While Williams Pipe Line cannot predict the final outcome of these proceedings, it believes its revised tariffs will ultimately be found lawful. See Note 17 of Notes to Consolidated Financial Statements.

Competition

Williams Pipe Line operates without the protection of a federal certificate of public convenience and necessity that might preclude other entrants from providing like service in its area of operations. Further, Williams Pipe Line must plan, operate and compete without the operating stability inherent in a broad base of contractually obligated or owner-controlled usage. Since Williams Pipe Line is a common carrier, its shippers need only meet the requirements set forth in its published tariffs in order to avail themselves of the transportation services offered by Williams Pipe Line.

Competition exists from other pipelines, refineries, barge traffic, railroads and tank trucks. Competition is affected by trades of products or crude oil between refineries which have access to the system and by trades among brokers, traders and others who control products. Such trades can result in the diversion from the Williams Pipe Line system of volume which might otherwise be transported on the system. Shorter, lower revenue hauls may also result from such trades. Williams Pipe Line also is exposed to interfuel competition whereby an energy form shipped by a liquids pipeline, such as heating fuel, is replaced by a form not transported by a liquids pipeline, such as electricity or natural gas. While Williams Pipe Line faces competition from a variety of sources throughout its marketing areas, the principal competition is other pipelines. A number of pipeline systems, competing on a broad range of price and service levels, provide transportation service to various areas served by the system. The possible construction of additional competing products or crude oil pipelines, conversions of crude oil or natural gas pipelines to products transportation, changes in refining capacity, refinery closings, changes in the availability of crude oil to retineries located in its

marketing area, or conservation and conversion efforts by fuel consumers may adversely affect the volumes available for transportation by Williams Pipe Line.

Ownership of Property

Williams Pipe Line's system is owned in fee. However, a substantial portion of the system is operated, constructed and maintained pursuant to rights-of-way, easements, permits, licenses or consents on and across properties owned by others. The terminals, pump stations and all other facilities of the system are located on lands owned in fee or on lands held under long-term leases, permits or contracts. Management believes that the system is in such a condition and maintained in such a manner that it is adequate and sufficient for the conduct of business.

Environmental Matters

Williams Pipe Line's operations are subject to various federal, state and local laws and regulations relating to environmental quality control. Management believes that Williams Pipe Line's operations are in substantial compliance with existing environmental legal requirements. Management expects that compliance with such existing environmental legal requirements will not have a material adverse effect on the capital expenditures, earnings and competitive position of Williams Pipe Line.

Williams Pipe Line has been named by the EPA as a potentially responsible party as defined in Section 107(a) of the Comprehensive Environmental Response, Compensation, and Liability Act, for a site in Sioux Falls, South Dakota. This site was placed on the National Priorities List in July 1990. In April 1991, Williams Pipe Line and the EPA executed an administrative consent order under which Williams Pipe Line agreed to conduct a remedial investigation and feasibility study for this site. The EPA issued its "No Action" Record of Decision in 1994 concluding that there were no significant hazards associated with the site subject to two additional years of monitoring for arsenic in certain existing monitoring wells. Monitoring should be complete in the first quarter of 1997.

WILLIAMS ENERGY VENTURES, INC. (Williams Energy Ventures)

Another subsidiary of Williams Holdings, Williams Energy Ventures, is combined for financial reporting purposes with Williams Pipe Line, although Williams Energy Ventures' activities are not included in the Williams Pipe Line operating statistics on page 15 herein. Williams Energy Ventures is engaged in the manufacturing and marketing of petroleum products and oxygenates. Williams Energy Ventures also owns an approximate 70 percent interest in a 30 million gallon per year ethanol plant in Nebraska that began operations in November 1995. Williams Energy Ventures operates the facility and markets the fuel ethanol output. In addition, on August 1, 1995, Williams Energy Ventures purchased Pekin Energy Company in Pekin, Illinois, for \$167 million. The Pekin Energy facility produces 100 million gallons annually of fuel-grade and industrial ethanol and various coproducts.

WILLIAMS TELECOMMUNICATIONS SYSTEMS, INC. (WilTel)

WilTel provides data, voice and video communications products and services to a wide variety of customers nationally. WilTel is strategically positioned in the marketplace with more than 100 sales and service locations throughout the United States, over 2,800 employees and over 1,200 stocked service vehicles. WilTel employs more than 1,300 technicians and more than 400 sales representatives and sales support personnel to serve an estimated 40,000 commercial, governmental and institutional customers. WilTel's customer base ranges from Fortune 500 corporations and the Federal Government to small privately-owned entities.

WilTel offers its customers a full array of data, voice and video network interconnect products including digital key systems (generally designed for voice applications with fewer than 100 lines), private branch exchange (PBX) systems (generally designed for voice applications with greater than 100 lines), voice processing systems, interactive voice response systems, automatic call distribution applications, call accounting systems, network monitoring and management systems, desktop video, routers, channel banks, intelligent

WilTel's services also include the design, configuration and installation of voice and data and the management of customers injugant minimum aperations and facilities. WilTel's National Technical Resource center provides customers with on-line order entry and trouble reporting services, advanced technical assistance and training. Other service capabilities include Local Area Network and PBX remote monitoring and toll thread debounch.

In March 1994, WilTel acquired BellSouth's customer premise equipment sales and service operations in 29 states outside of BellSouth's local operating region in the nine southeastern-most states, and in October 1994, acquired Jackson Voice Data, a New York City-based customer premise equipment company. In 1996, WilTel acquired Comlink, Incorporated, a Massachusetts-based data and customer premise equipment company. The acquisition of these businesses has allowed WilTel to capitalize on its existing infrastructure, strengthen its national market presence and geographic customer density and has provided more diversity in product offerings.

Operating Statistics

The following table summarizes the results of operations for the periods indicated (dollars and ports in millions):

1013).	1995	1994	1993
Revenues	\$494.9	\$396.6	\$302.8
Percentage of revenues by type of service: New system sales		33%	39%
New system sales System modifications	39%	36%	30%
Maintenance	254	24%	23%
Other	2%	7%	\$ 95
Operating profit	\$ 28.3	\$ 18.9 \$ 92.4	
Backlog	\$ 85.0	4.1	2.7
Total ports		. 711	

A port is defined as an electronic address resident in a customer's PBX or key system that supports a station, trunk or data port.

In 1995, WilTel derived approximately 66 percent of its revenues from its existing customer base and approximately 34 percent from the sale of new telecommunications systems. WilTel's three largest suppliers accounted for 89 percent of equipment sold in 1995. A single manufacturer supplied 76 percent of all equipment sold. In this case, WilTel is the largest distributor of certain of this company's products. About 64 percent of WilTel's active customer base consists of this manufacturer's products. The distribution agreement with this supplier is scheduled to expire at the end of 1997. This agreement is expected to be renewed upon expiration. Management believes there is minimal risk as to the availability of product from suppliers.

Competition

WilTel has many competitors ranging from AT&T and the Regional Bell Operating Companies to small individually-owned companies which sell and service customer premise equipment. Competitors include companies that sell equipment that is comparable or identical to that sold by WilTel. (See discussion of telecommunications reform legislation below).

Regulatory Matters

The equipment sold by WilTel must meet the requirements of Part 68 of the Federal Communications Commission ("FCC") rules governing the equipment registration, labelling and connection of equipment to telephone networks. WilTel relies on the equipment manufacturers' compliance with these requirements for its own compliance regarding the equipment it distributes. A subsidiary of WilTel, which provides intrastate

microwave communications services for a Federal agency, is subject to FCC regulations as a common carrier microwave licensee. These regulations have minimal impact on WilTel's operations.

THE WILTECH GROUP, INC. (WilTech)

WilTech, through subsidiaries, seeks to develop growth opportunities in the telecommunications and technology industries. WilTech currently conducts its business through two principal operating subsidiaries, Vyvx, Inc. and Williams Learning Network, Inc. In October 1995, WilTech acquired a 22 percent interest in ITC mediaConferencing Company. The investment is expected to expand WilTech's offerings in the videoconferencing, teleconferencing and enhanced fax services markets. The total cost of the ITC investment, together with the ICG Wireless Services' assets and NUS Training Corporation acquisitions discussed below, is approximately \$51 million.

VYVX, INC. (Vyvx)

Vyvx offers fiber-optic television transmission services nationwide. It provides these broadcast-quality services as an alternative to satellite and microwave television transmissions. Vyvx primarily provides backhaul or point-to-point transmission of news and other programming between two or more customer locations. For example, the Vyvx network is used for the broadcast coverage of major professional sporting events. Vyvx's customers include all of the major broadcast and cable networks. Vyvx also provides videoconferencing business television services.

In 1995, Vyvx announced the acquisition of four teleports (including satellite earth station facilities) from ICG Wireless Services. The teleports are located in Atlanta, Denver, Los Angeles and New York (Carteret, N.J.). The acquisition will enable Vyvx to provide both fiber-optic backhaul and satellite distribution services. The acquisition, which is subject to certain conditions, including the receipt of regulatory approvals, is expected to close in the first half of 1996.

Regulatory Matters. Vyvx is subject to FCC regulations as a common carrier with regard to certain of its existing and future transmission services and is subject to the laws of certain states governing public utilities. Operation of to-be-acquired satellite earth stations and certain other related transmission facilities are also subject to FCC licensing and other regulations. These regulations do not have a significant impact on Vyvx's operations.

Competition. Competition for Vyvx's fiber-optic television transmission operations is derived primarily from companies offering video transmission services by means of satellite facilities and to a lesser degree from companies offering transmission services via microwave facilities or fiber-optic cable.

Federal telecommunications reform legislation enacted in February 1996, is designed to increase competition in the long distance market by significantly liberalizing current restrictions on market entry. In particular, Regional Bell Operating Companies are permitted to provide long distance services, including but not limited to, video transmission services, subject to certain restrictions and conditions precedent. Moreover, public utilities are permitted to provide telecommunications services, including long distance services, through separate subsidiaries. The legislation also calls for tariff forbearance and relaxation of regulation over common carriers. Any impact such legislation may have on Vyvx cannot be predicted at this time.

WILLIAMS LEARNING NETWORK, INC. (Williams Learning Network)

Williams Learning Network, formerly Williams Knowledge Systems, provides computer-based operator training primarily to the energy industry. Williams Learning Network has licensing agreements with over 150 customers in the oil and gas pipeline, terminal and trucking industries.

In October 1995, Williams Learning Network acquired NUS Training Corporation. This acquisition gives Williams Learning Network a large library of video-based and multimedia training products for the chemical, refining and utility industries plus an expanded customer base and sales force.

OTHER INFORMATION

Williams believes that it has adequate sources and availability of raw materials to assure the continued supply of its services and products for existing and anticipated business needs. Williams' pipeline systems are all regulated in various ways resulting in the financial return on the investments made in the systems being limited to standards permitted by the regulatory bodies. Each of the pipeline systems has ongoing capital requirements for efficiency and mandatory improvements, with expansion opportunities also necessitating periodic capital outlays.

A plant site in Pensacola, Florida, that was previously operated by a former subsidiary of Williams, has been placed on the National Priorities List. This former subsidiary has also been identified as a potentially responsible party at a National Priorities List cleanup site in Michigan. A third site, located in Lakeland, Florida, which was formerly owned and operated by this subsidiary, is under investigation by the Florida Department of Environmental Protection and cleanup is anticipated. Williams does not believe that the ultimate resolution of the foregoing matters, taken as a whole and after consideration of insurance coverage, contribution or other indemnification arrangements, will have a material adverse financial effect on the Company. See Note 17 of Notes to Consolidated Financial Statements.

At December 31, 1995, the Company had approximately 10,000 full-time employees, of whom approximately 1,350 were represented by unions and covered by collective bargaining agreements. The Company considers its relations with its employees to be generally good.

Forward-looking Information

Certain matters discussed in this report, excluding historical information, include forward-looking statements. Although the Company believes such forward-looking statements are based on reasonable assumptions, no assurance can be given that every objective will be reached. Such statements are made in reliance on the "safe harbor" protections provided under the Private Securities Litigation Reform Act of 1995.

As required by such Act, the Company hereby identifies the following important factors that could cause actual results to differ materially from any results projected, forecasted, estimated or budgeted by the Company in forward-looking statements: (i) risks and uncertainties impacting the Company as a whole primarily relate to changes in general economic conditions in the United States, changes in laws and regulations to which the Company is subject, including tax, environmental and employment laws and regulations, the cost and effects of legal and administrative claims and proceedings against the Company or its subsidiaries or which may be brought against the Company or its subsidiaries and conditions of the capital markets utilized by the Company to access capital to finance operations; (ii) for the Company's regulated businesses, risks and uncertainties primarily relate to the impact of future federal and state regulation of business activities, including allowed rates of return; and (iii) risks and uncertainties associated with the Company's nonregulated businesses primarily relate to the ability of such entities to develop expanded markets and product offerings as well as maintaining existing markets. In addition, future utilization of pipeline capacity will depend on energy prices, competition from other pipelines and alternate fuels, the general level of natural gas and petroleum product demand and weather conditions, among other things. Further, gas prices which directly impact transportation and gathering and processing throughput and operating profits may fluctuate in unpredictable ways. It is also not possible to predict which of many possible future products and service offerings will be important to maintaining a competitive position in the telecommunications business or what expenditures will be required to develop and provide such products and services.

(d) Financial Information about Foreign and Domestic Operations and Export Sales

Williams has no significant foreign operations.

Item 2. Properties

See Item 1(c) for description of properties.

Item 3. Legal Proceedings

Other than as described under Item 1 — Business and in Note 17 of Notes to Consolidated Financial Statements, there are no material pending legal proceedings. Williams is subject to ordinary routine litigation incidental to its businesses.

With respect to the Dakota litigation described in Note 17, certain parties have subsequently filed a motion with FERC requesting that FERC establish an additional proceeding to consider claims for additional refunds. The claimed additional refunds pertain to amounts paid Dakota from November 1, 1988, through April 30, 1993. Net to Transco's interest, the claimed additional refunds approximate \$90 million. Transco has filed documents with FERC opposing the motion for additional refunds. The administrative law judge's initial decision in this case pertained only to periods after April 30, 1993, and, if sustained, would require Transco to refund to ratepayers approximately \$75 million.

Item 4. Submission of Matters to a Vote of Security Holders

Not applicable.

Executive Officers of Williams

The names, ages, positions and earliest election dates of the executive officers of Williams are:

Name Age		Positions and Offices Held	Held Office Since	
Keith E. Bailey	53	Chairman of the Board, President, Chief Executive Officer and Director (Principal Executive Officer)	05-19-94	
John C. Bumgarner, Jr	53	Senior Vice President — Corporate Development and Planning	01-01-79	
James R. Herbster	54	Senior Vice President — Administration	01-01-92	
J. Furman Lewis	61	Senior Vice President and General Counsel	07-15-86	
Jack D. McCarthy	53	Senior Vice President — Finance (Principal Financial Officer)	01-01-92	
Gary R. Belitz	46	Controller (Principal Accounting Officer)	01-01-92	
Stephen L. Cropper	46	President — Williams Pipe Line, Williams Energy Services and Williams Energy Ventures	01-22-86	
Lloyd A. Hightower	61	President — Williams Field Services	05-11-93	
Henry C. Hirsch	53	President — Williams Telecommunications Systems	08-21-92	
Howard E. Janzen	41	President - The WilTech Group, Inc.	12-01-94	
Brian E. O'Neill	60	President — Transco, Northwest Pipeline, Kern River, TXG and Williams Natural Gas	01-01-88	

All of the above officers have been employed by Williams or its subsidiaries as officers or otherwise for more than five years and have had no other employment during such period.

PART II

Item 5. Market for the Registrant's Common Equity and Related Stockholder Matters

Williams' Common Stock is listed on the New York and Pacific Stock Exchanges under the symbol "WMB." At the close of business on December 31, 1995, Williams had 11,933 holders of record of its Common Stock. The daily closing price ranges (composite transactions) and dividends declared by quarter for each of the past two years are as follows:

	1995				1994		
Quarter	High	Low	Dividend	High	Low.	Dividend	
lst	\$30%	\$24%	\$.27	\$271/4	\$22%	\$.21	
2nd		\$301/4	\$.27	\$30%	\$221/4	5.21	
3rd		\$34%	\$.27	\$32%	\$28%	\$.21	
4th		\$37%	\$.27	\$30%	\$241/4	5.21	

In January 1996, the Board of Directors of the Company approved a 25.9 percent increase in the Common Stock dividend. The dividend approved for the first quarter of 1996 was \$.34 per share.

Terms of certain subsidiaries' borrowing arrangements limit transfer of funds to Williams. These terms have not impeded, nor are they expected to in the future, Williams' ability to meet its cash obligations. See Note 13 of Notes to Consolidated Financial Statements.

Item 6. Selected Financial Data

The following financial data are an integral part of, and should be read in conjunction with, the consolidated financial statements and notes thereto. Information concerning significant trends in the financial condition and results of operations is contained in Management's Discussion and Analysis of Financial Condition and Results of Operations on pages F-1 through F-9 of this report.

	1995	1994	1993	1992	1991			
	(Millions, except per-share amounts)							
Revenues*	\$ 2,855.7	\$1,751.1	\$1,793.4	\$1,983.5	\$1,704.5			
Income from continuing operations*	299.4	164.9	185.4	103.1	69.7			
Income from discontinued operations**	1,018.8	94.0	46.4	25.2	40.3			
Fully diluted earnings per share:	0.0000000000000000000000000000000000000				55-7-18-5			
Income from continuing operations	2.76	1.52	1.71	.97	.69			
Income from discontinued operations	9.72	.92	.45	.28	.48			
Cash dividends per common share	1.08	.84	.78	.76	.70			
Total assets at December 31	10,494.8	5,226.1	5,020.4	4,982.3	4,247.4			
Long-term obligations at December 31	2,874.0	1,307.8	1,604.8	1,683.2	1,541.9			
Stockholders' equity at December 31	3,187.1	1,505.5	1,724.0	1,518.3	1,220.0			

See Notes 5 and 6 of Notes to Consolidated Financial Statements for discussion of significant asset sales and write-off of project costs.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Results of Operations

1995 vs. 1994

Northwest Pipeline's revenues increased \$16.7 million, or 7 percent, due primarily to the \$16 million reversal of a portion of certain rate refund accruals and increased transportation rates put into effect in November 1994, partially offset by the completion in 1994 of billing contract-reformation surcharges. Mainline throughput increased 22 percent; however, revenues were not significantly affected due to the effects of the straight-fixed-variable rate design prescribed by the Federal Energy Regulatory Commission (FERC). Operating profit increased \$11.6 million, or 11 percent, due primarily to higher transportation rates and the approximate \$11 million net effect of two reserve accrual adjustments, partially offset by \$5 million, or 13 percent, higher operations and maintenance expenses. The reserve accrual adjustments involved a \$16 million adjustment to rate refund accruals because of favorable rate case developments, partially offset by a loss accrual (included in other income — net) in connection with a lawsuit involving a former transportation customer.

Williams Natural Gas' revenues decreased \$57 million, or 25 percent, and costs and operating expenses decreased \$62 million, or 40 percent, due primarily to \$36 million lower direct billing of purchased gas adjustments and lower contract-reformation recovery of \$21 million. Operating profit decreased \$3.8 million, or 8 percent, due primarily to the absence of the 1994 reversal of excess contract-reformation accruals of \$7.4 million and \$3.2 million from lower 1995 average firm reserved capacity, partially offset by \$4.6 million resulting from higher average firm reserved capacity rates, effective August 1, 1995, and higher storage revenues of \$3.7 million.

Transcontinental Gas Pipe Line's revenues were \$725.3 million in 1995, while costs and expenses were \$560 million and operating profit was \$165 million. Throughput was 1,410.9 TBtu in 1995 (for the period subsequent to the acquisition date). Transcontinental Gas Pipe Line placed new, higher rates into effect September 1, 1995, subject to refund. Market-area deliveries in 1995 and 1994 were approximately the same.

^{••} See Note 3 of Notes to Consolidated Financial Statements for discussion of the gain on the sale of discontinued operations.

Texas Gas Transmission's revenues were \$276.3 million in 1995, while costs and expenses were \$212 million and operating profit was \$64 million. Throughput was 653.4 TBtu in 1995 (for the period subsequent to the acquisition date). Texas Gas placed new, higher rates into effect April 1, 1995, subject to refund.

Williams Field Services Group's revenues increased \$216.1 million, or 58 percent, due primarily to \$172 million higher gathering revenues in addition to higher natural gas sales. Gathering revenues increased due primarily to a 102 percent increase in gathering volumes, including \$131 million attributable to Transco Energy's Gulf Coast gathering operations, combined with an increase in average gathering prices, excluding Gulf Coast operations. Natural gas sales increased due to higher volumes, partially offset by lower average prices. Liquids and processing volumes increased 6 percent and 4 percent, respectively. Costs and operating expenses increased \$171 million, or 79 percent, and selling, general and administrative expenses increased \$28 million, or 89 percent, with Transco Energy's activities contributing \$102 million and \$13 million, respectively. In addition, costs and operating expenses increased from higher natural gas purchase volumes and expanded facilities. Other income - net includes \$12 million in operating profit from the net effect of two unrelated items. One was \$20 million of income from the favorable resolution of contingency issues involving previously regulated gathering and processing assets. This was partially offset by an \$8 million accrual for a future minimum price natural gas commitment. Operating profit increased \$28.3 million, or 22 percent, primarily resulting from the \$12 million in other income and a doubling of gathering volumes, primarily a result of Transco Energy's gathering activities. Partially offsetting these increases was the effect of lower natural gas prices. Operating profit in 1994 included approximately \$12 million in favorable settlements and adjustments of certain prior period accru ils, including income of \$4 million from an adjustment to operating taxes.

Williams Energy Services' revenues and costs and operating expenses decreased \$177.9 million and \$238 million, respectively. The addition of Transco Energy's gas trading activities was more than offset by the reporting of 1995 natural gas marketing activities on a net-margin basis (see Note 15). Natural gas physical trading volumes increased to 753.8 TBtu in 1995 compared to 147.8 TBtu in 1994, primarily from the effect of the Transco Energy acquisition. Operating profit increased \$29.5 million from \$500,000 in 1994. Trading activities' operating profit increased \$34 million, attributable primarily to income recognition from long-term natural gas supply obligations and no-notice service provided to local distribution companies. Included in trading activities is a price-risk management adjustment of \$4 million from the valuation of certain natural gas supply and sales contracts previously excluded from trading activities. These increases were partially offset by \$6 million of loss provisions, primarily accruals for contract disputes, and increased costs of supporting its information services business. As a result of Williams Energy Services' price-risk management and trading activities, it is subject to risk from changes in energy commodity market prices, the portfolio position of its financial instruments and credit risk. Williams Energy Services manages its portfolio position by making commitments which manage risk by maintaining its portfolio within established trading policy guidelines.

Williams Pipe Line's revenues (including Williams Energy Ventures) increased \$39.5 million, or 13 percent, due to an increase in transportation and non-transportation revenues of \$9 million and \$30.5 million, respectively. Shipments, while 7 percent higher than 1994, were reduced by the November 1994 fire at our truck-loading rack and unfavorable weather conditions in the first half of 1995. The average transportation rate per barrel and average length of haul were slightly below 1994 due primarily to shorter haul movements. The increase in non-transportation revenues reflects \$84 million from the acquisition of Pekin Energy in August 1995 and increased gas liquids operations of \$16 million, largely offset by \$62 million related to lower petroleum-product services due to adverse market conditions and a \$15 million decrease in refined-product sales due to the unavailability of certain refined-product supplies. Costs and expenses increased \$22 million, or 8 percent, due primarily to increased operating expenses associated with transportation and non-transportation activities. Operating profit (including Williams Energy Ventures) increased \$17.8 million, or 34 percent, due primarily to higher transportation revenues of \$9 million and non-transportation activities of \$8.8 million. Non-transportation includes \$3 million related to the acquisition of Pekin Energy and the absence of \$5 million of costs in 1994 for evaluating and determining whether to build an oil refinery near

Phoenix. Williams Energy Ventures' results improved in 1995 with a \$400,000 operating loss compared to an \$8.1 million operating loss in 1994.

WilTel's revenues increased \$98.3 million, or 25 percent, due primarily to \$30 million from new systems, \$28 million from existing system enhancements and \$37 million from contract maintenance, moves, adds and changes. These amounts include the effect of the acquisitions of BellSouth Communications Systems in March 1994 and Jackson Voice Data, completed in October 1994. The number of ports in service at December 31, 1995, has increased 14 percent as compared to December 31, 1994. Costs and operating expenses increased \$79 million, or 26 percent, due primarily to the increase in volume of sales and services. While the \$11 million, or 15 percent, increase in selling, general and administrative expenses is due primarily to higher revenues, the selling, general and administrative expense to revenue percent declined from 19.2 percent to 17.7 percent, reflecting better leveraging of the company's existing infrastructure. Operating profit increased \$9.4 million, or 50 percent, due primarily to increased activity in new system sales, enhancements to existing systems, maintenance and the full-year 1995 impact of two 1994 acquisitions and cost control efforts.

WilTech Group's revenues increased \$24 million, or 120 percent, due primarily to \$15 million in higher occasional and dedicated digital television services revenues and the effect of an acquisition during 1995. Billable minutes from occasional service increased 110 percent and dedicated service voice grade equivalent miles at December 31, 1995, increased 50 percent as compared with December 31, 1994. The \$6 million, or 22 percent, increase in cost of sales and the \$10 million increase in selling, general and administrative expenses reflects the overall increase in sales activity and higher expenses for developing additional products and services. Operating loss decreased \$8 million, or 71 percent, due to higher demand for WilTech Group's digital television services, which produced volumes sufficient to result in operating profit for the fourth quarter.

General corporate expenses increased \$9.7 million, due primarily to a \$6.4 million increase in charitable contributions, including \$5 million to The Williams Companies Foundation. Interest accrued increased \$132.1 million, due primarily to the \$2 billion outstanding debt assumed as a result of the Transco Energy acquisition. Interest capitalized increased \$8.5 million, due primarily to increased expenditures for gathering and processing facilities and Northwest Pipeline's expansion projects. Investing income increased \$44.3 million, due primarily to interest earned on the invested portion of the cash proceeds from the sale of Williams' network services operations in addition to an \$11 million increase in the dividend from Texasgulf Inc. The 1995 loss on sales of assets results from the sale of the 15 percent interest in Texasgulf Inc. (see Note 5). The 1994 gain on sales of assets results from the sale of 3,461,500 limited partner common units in Northern Border Partners, L.P. The 1995 write-off of project costs results from the cancellation of an underground coal gasification project in Wyoming (see Note 6). Other income (expense) — net in 1995 includes approximately \$10 million of minority interest expense associated with the Transco Energy merger, \$4 million of dividends on subsidiary preferred stock and \$4 million of losses on sales of receivables, partially offset by \$11 million of equity allowance for funds used during construction (AFUDC). Other income (expense) --- net in 1994 includes a credit for \$4.8 million from the reversal of previously accrued liabilities associated with certain Royalty Trust contingencies that expired. Also included is approximately \$4 million of expense related to Statement of Financial Accounting Standards (FAS) No. 112, "Employers' Accounting for Postemployment Benefits," which relates to postemployment benefits being paid to employees of companies previously sold.

The \$20.3 million increase in the provision for income taxes on continuing operations is primarily a result of higher pre-tax income, partially offset by a lower effective income tax rate resulting from \$29.8 million of previously unrecognized tax benefits realized as a result of the sale of Texasgulf Inc. (see Note 5) and an \$8 million income tax benefit resulting from settlements with taxing authorities. The effective income tax rate in 1995 is significantly less than the federal statutory rate, due primarily to the previously unrecognized tax benefits realized as a result of the sale of the investment in Texasgulf Inc., income tax credits from coal-seam gas production and recognition of an \$8 million income tax benefit resulting from settlements with taxing authorities, partially offset by the effects of state income taxes and minority interest. The effective income tax rate in 1994 is lower than the statutory rate primarily because of income tax credits from coal-seam gas production, partially offset by state income taxes (see Note 7).

On January 5, 1995, Williams sold its network services operations to LDDS Communications, Inc. for \$2.5 billion in cash. The sale yielded an after-tax gain of approximately \$1 billion, which is reported as income from discontinued operations. Prior period operating results for the network services operations are reported as discontinued operations (see Note 3).

The 1994 extraordinary loss results from the early extinguishment of debt (see Note 8). Preferred stock dividends increased \$6.5 million as a result of the May 1995 issuance of 2.5 million shares of Williams \$3.50 cumulative convertible preferred stock in exchange for Transco Energy's \$3.50 cumulative convertible preferred stock (see Note 14) in addition to the \$3.5 million premium on exchange of \$2.21 cumulative preferred stock for debentures.

1994 vs. 1993

Northwest Pipeline's revenues decreased \$38 million, or 14 percent, as expanded firm transportation service was more than offset by the absence of natural gas sales following the fourth-quarter 1993 implementation of FERC Order 636 and \$10 million resulting from the 1994 completion of contract-reformation surcharges. Total mainline throughput increased 9 percent. Firm transportation service increased due to a mainline expansion, supported by 15-year firm transportation contracts, being placed into service on April 1, 1993. Northwest Pipeline placed new, increased transportation rates into effect on November 1, 1994, and April 1, 1993, subject to refund. The April 1, 1993, rates reflected the new mainline expansion and straight-fixed-variable rate design that moderates seasonal swings in operating revenues. Costs and operating expenses decreased \$43 million, or 32 percent, due primarily to the absence of natural gas purchase volumes of \$41 million and the completion of contract-reformation amortization, slightly offset by increased operating expenses primarily related to the full-year effect on 1994 of the mainline expansion. Operating profit increased \$5.3 million, or 5 percent, due primarily to expanded firm transportation service related to the company's mainline system expansion.

Williams Natural Gas' revenues decreased \$62.8 million, or 21 percent, primarily as a result of the absence of natural gas sales resulting from implementation of FERC Order 636 on October 1, 1993. The decrease in revenues was partially offset by the implementation of new rates required by the Order, direct billing of net purchased gas cost adjustment amounts of approximately \$40 million and higher direct billing of recoverable contract-reformation costs of approximately \$17 million. Costs and operating expenses decreased \$67 million, or 30 percent, primarily as a result of approximately \$120 million lower gas purchase costs resulting from the implementation of FERC Order 636, partially offset by the costs that were direct billed as discussed above. Operating profit increased \$7.8 million, or 19 percent, primarily as a result of the full-year effect of new rates, implementation of Order 636 and the reversal of excess contract-reformation accruals recorded in other income — net (\$7.4 million in 1994 and \$2.5 million in 1993), partially offset by the absence of the regulatory accounting effect of an income tax rate increase in 1993 (which was offset in income tax expense). FERC Order 636 utilizes a straight-fixed-variable rate design that is applied to each customer's annual firm contract demand for transportation.

Williams Field Services Group's revenues decreased \$56.5 million, or 13 percent, due primarily to \$71 million in lower natural gas sales revenues as a result of the March 1993 sale of Williams' intrastate natural gas pipeline system and related marketing operations in Louisiana, \$9 million in lower liquids revenues and lower average processing prices. Partially offsetting were higher gathering and processing revenues of \$22 million and \$8 million, respectively, from increased volumes of 13 percent and 21 percent, respectively. Increased other revenues in 1994 were offset by a 1993 favorable settlement involving processing revenues from prior periods. Costs and operating expenses decreased \$59 million, or 21 percent, due primarily to lower natural gas purchases of \$66 million and the effects of a favorable adjustment of an accrual related to operating taxes, partially offset by higher operations, maintenance and depreciation expenses at expanded gathering facilities. Operating profit increased \$2.6 million, or 2 percent, due primarily to higher gathering and processing volumes and a \$4 million favorable operating taxes adjustment, partially offset by \$5 million of lower per-unit liquids margins, lower average processing prices and higher operations, maintenance and depreciation expenses associated with expanded facilities.

Williams Energy Services' revenues decreased \$97.1 million, or 27 percent, due primarily to lower natural gas sales volumes and prices of \$45 million, lower refined-product trading margins and the \$45 million effect of reporting these trading activities on a "net margin" basis, effective July 1, 1993. Costs and operating expenses decreased 29 percent, due to lower natural gas purchase volumes and prices of \$46 million and the \$43 million effect of reporting refined-product trading activities on a "net margin" basis, partially offset by the cost of developing long-term energy industry businesses. General and administrative expenses increased 44 percent, reflecting the costs of establishing appropriate administrative and project support groups to serve growing business activities. Operating profit was \$500,000 in 1994 compared to \$7.9 million in 1993. Price-risk management services' results continued to be profitable but were lower by \$6 million in 1994 than 1993 because of reduced gasoline and distillate margins and the effect of location pricing differentials in refined-products trading activities, partially offset by an improvement in natural gas trading margins reflecting increased volumes. Costs to develop long-term energy industry opportunities also adversely affected operating profit. Results from natural gas marketing activities increased by \$2 million in 1994 compared to 1993.

Williams Pipe Line's shipments increased 9 percent, due primarily to new volumes resulting from the December 1993 acquisition of a pipeline system in southern Oklahoma. Revenues (including Williams Energy Ventures) increased \$130.2 million, or 72 percent, due primarily to higher shipments, increased gas liquids and fractionator operations of \$30 million and petroleum services activities of \$106 million. The slightly higher average transportation rate resulted primarily from longer hauls into the northern region and overall increases in tariff rates, effective December 1, 1994, and June 1, 1993, partially offset by lower rates on shorter haul movements from new business. Costs and operating expenses increased \$125 million, or 94 percent, due primarily to gas liquids and fractionator operations, additional operating expenses, petroleum services activities of \$104 million and the cost of developing long-term energy industry businesses. Operating profit (including Williams Energy Ventures) increased \$4.8 million, or 10 percent, reflecting \$15 million from increased shipments and a favorable insurance settlement, partially offset by higher operating and maintenance expenses. Operating profit also includes \$9 million of costs from developing long-term energy industry investment opportunities. Included in 1994's other income — net is approximately \$5 million of costs for evaluating and determining whether to build an oil refinery near Phoenix.

WilTel's revenues increased \$93.8 million, or 31 percent, due in large part to the March 31, 1994, acquisition of BellSouth's customer equipment sales and service operations in 29 states, as evidenced by a 52 percent increase in the number of ports. Costs and operating expenses and selling, general and administrative expenses increased 31 percent and 20 percent, respectively, due to the increase in volume of equipment sales and services. Operating profit increased to \$18.9 million in 1994 from \$9.5 million in 1993, primarily resulting from higher sales volumes, partially offset by an increase in selling, general and administrative expenses. Margins were level between 1994 and 1993, while selling, general and administrative expenses as a percent of revenue decreased in 1994 compared to 1993.

WilTech Group's revenues and operating losses for 1994 and 1993 are primarily from Vyvx, Inc.'s switched fiber-optic television transmission services. Results of Vyvx's operations improved significantly in 1994; however, the operations in both periods were not profitable as sufficient volumes had not been achieved to support the infrastructure in place. Revenues increased \$6.5 million, or 48 percent, in 1994 reflecting higher occasional and dedicated digital television services, which helped reduce operating losses 34 percent from \$17 million in 1993 to \$11.3 million in 1994.

General corporate expenses decreased \$10.4 million, reflecting lower supplemental retirement benefits (see Note 9) and incentive compensation accruals. Interest accrued decreased \$5.4 million, primarily because of lower effective interest rates, partially offset by higher average borrowing levels. Interest capitalized decreased \$4.4 million, reflecting the completion of Northwest Pipeline's mainline expansion, which was placed in service April 1, 1993. Investing income decreased \$15.6 million, due primarily to lower investment levels and lower equity earnings for Apoc Argentina Inc., in addition to the sale of a portion of Williams' interest in Northern Border Partners, L.P. The 1994 gain on sales of assets results from the sale of 3,461,500 limited partner common units in Northern Border Partners, L.P. The gain on sales of assets in 1993 results from the sale of 6.1 million units in the Williams Coal Seam Gas Royalty Trust and the sale of the intrastate natural gas pipeline system and other related assets in Louisiana (see Note 6). Other income (expense) — net

in 1994 includes a credit for \$4.8 million from the reversal of previously accrued liabilities associated with certain Royalty Trust contingencies that expired. Also included is approximately \$4 million of expense related to FAS No. 112, "Employers' Accounting for Postemployment Benefits," which relates to postemployment benefits being paid to employees of companies previously sold. Other income (expense)—net in 1993 includes \$6 million of expense accruals for certain costs associated with businesses previously sold, offset by \$6 million of equity AFUDC related to the Northwest Pipeline mainline expansion.

The \$30.9 million decrease in the provision for income taxes on continuing operations is primarily a result of lower pre-tax income and the \$15.8 million cumulative effect in 1993 of the 1 percent increase in the federal income tax rate. The effective income tax rate in 1994 is lower than the statutory rate, primarily because of income tax credits from coal-seam gas production, partially offset by state income taxes. The effective income tax rate in 1993 is higher than the statutory rate, primarily because of the effect of the federal income tax rate increase and state income taxes, partially offset by income tax credits from coal-seam gas production (see Note 7).

The network services operations of Williams have been presented in the Consolidated Financial Statements as discontinued operations (see Note 3). Income from discontinued operations more than doubled to \$94 million. The increase reflects a 93 percent increase in switched services minutes and a 24 percent increase in private line billable circuits. These increases more than offset a major carrier's long-expected removal of traffic from Williams' system to the carrier's expanded network. Income was also impacted by a decrease in interest accrued due to the early extinguishment of network services' long-term debt. The effective income tax rate for both 1994 and 1993 is greater than the federal statutory rate, due to the effect of state income taxes.

The extraordinary loss results from early extinguishment of debt (see Note 8). Preferred stock dividends decreased, reflecting the redemption of 3,000,000 shares of outstanding \$3.875 convertible exchangeable preferred stock during the second quarter of 1993 (see Note 14).

Financial Condition and Liquidity

Liquidity

Williams considers its liquidity to come from two sources: internal liquidity, consisting of available cash investments, and external liquidity, consisting of borrowing capacity from available bank-credit facilities, which can be utilized without limitation under existing loan covenants. At December 31, 1995, Williams had access to \$726 million of liquidity representing the available portion of its \$800 million bank-credit facility plus cash-equivalent investments. This compares with liquidity of \$495 million at December 31, 1994, and \$639 million at December 31, 1993. The increase in 1995 is due primarily to a \$200 million increase in the capacity of the bank-credit facility (see Note 13). In January 1996, Williams Holdings of Delaware, Inc., a wholly owned subsidiary of Williams, filed a \$400 million shelf registration statement with the Securities and Exchange Commission and subsequently issued \$250 million of debt securities. During 1993, Williams filed a \$300 million shelf registration statement with the Securities and Exchange Commission, increasing the total amount available to \$400 million. The registration statement may be used to issue Williams common or preferred stock, preferred stock purchase rights, debt securities, warrants to purchase Williams common stock or warrants to purchase debt securities. Williams does not anticipate the need for additional financing arrangements; however, Williams believes such arrangements could be obtained on reasonable terms if required.

Williams had a net working-capital deficit of \$706 million at December 31, 1995, compared with \$17 million at December 31, 1994. Williams manages its borrowings to keep cash and cash equivalents at a minimum and has relied on bank-credit facilities to provide flexibility for its cash needs. As a result, it historically has reported negative working capital. The increase in the working-capital deficit at December 31, 1995, as compared to the prior year-end is primarily a result of higher 1995 levels of accounts payable and accrued liabilities (see Note 12) and the effect of the 1994 net assets of discontinued operations (see Note 3).

Terms of certain borrowing agreements limit transfer of funds to Williams from its subsidiaries. The restrictions have not impeded, nor are they expected to impede, Williams' ability to meet its cash requirements in the future.

Subsequent to December 31, 1995, Williams entered into a \$205 million short-term borrowing agreement to finance the purchase of the remaining interest in Kern River Gas Transmission (see Notes 5 and 13). During 1996, Williams expects to finance capital expenditures, investments and working-capital requirements through cash generated from operations and the use of its \$800 million bank-credit facility or public debt/equity offerings.

Operating Activities

Cash provided by continuing operating activities was: 1995 — \$829 million; 1994 — \$180 million; and 1993 — \$187 million. Accrued liabilities increased, due primarily to the income tax and other liabilities associated with the sale of the network services operations in addition to the acquisition of Transco Energy. The increases in receivables, inventory, other current assets, property, plant and equipment, other noncurrent assets and deferred charges, payables, long-term debt, deferred income taxes, and other liabilities primarily reflect the acquisition of Transco Energy. In addition, the increase in receivables was partially offset by a \$556 million increase in the level of receivables sold. Cash provided by discontinued operations was: 1994 — \$169 million; and 1993 — \$162 million.

Financing Activities

Net cash provided (used) by financing activities was: 1995 — (\$1.4) billion; 1994 — \$50 million; and 1993 — (\$220) million. Notes payable decreased, reflecting the repayment of these notes with the proceeds from the sale of the network services operations. Long-term debt principal payments net of debt proceeds were \$610 million during 1995. Long-term debt proceeds, net of principal payments and early extinguishment of debt were \$24 million during 1994. Long-term debt principal payments totaled \$192 million during 1993.

On January 18, 1995, Williams acquired 60 percent of Transco Energy's outstanding common stock in a cash tender offer for \$430.5 million. Williams acquired the remaining 40 percent of Transco Energy's outstanding common stock on May 1, 1995, through a merger by exchanging the remaining Transco Energy common stock for approximately 10.4 million shares of Williams common stock valued at \$334 million. Additionally, \$2.3 billion in preferred stock and debt obligations of Transco Energy was assumed by Williams. Williams made payments to retire and/or terminate approximately \$700 million of Transco Energy's borrowings, preferred stock, interest-rate swaps and sale of receivable facilities. As part of the merger, Williams exchanged Transco Energy's \$3.50 cumulative convertible preferred stock (see Note 2). The cash portion of the acquisition and the payments to retire and/or terminate various Transco Energy facilities were financed with the proceeds from the sale of Williams' network services operations (see Note 3).

During 1995, Williams exchanged 2.8 million shares of its \$2.21 cumulative preferred stock with a carrying value of \$69 million for 9.6 percent debentures with a fair value of \$72.5 million (see Note 14).

The 1995 proceeds from issuance of common stock includes \$46.2 million from the sale of 1.2 million shares of Williams common stock, held by a subsidiary of Williams and previously classified as treasury stock in the Consolidated Balance Sheet, in addition to certain Williams benefit plan stock purchases and exercise of stock options under Williams' stock plans. The majority of the proceeds from issuance of common stock in 1994 and 1993 resulted from certain Williams benefit plan stock purchases and exercise of stock options under Williams' stock plan (see Note 14).

During 1994, Williams and one of its subsidiaries purchased 13.8 million shares of Williams common stock on the open market for \$407 million. Substantially all of the purchases were financed with a \$400 million bank-credit agreement. In 1995, the outstanding amounts under the credit agreement were repaid from the proceeds of the sale of Williams' network services operations, and the credit agreement was terminated.

Williams also repurchased 258,800 shares of its \$2.21 cumulative preferred stock on the open market for \$6 million in 1994.

During 1993, Williams called for redemption of its 3,000,000 shares of outstanding \$3.875 convertible exchangeable preferred stock. Substantially all of the preferred shares were converted into 7,600,000 shares of Williams common stock.

Long-term debt at December 31, 1995, was \$2.9 billion, compared with \$1.3 billion at December 31, 1994, and \$1.6 billion at December 31, 1993. The increase in long-term debt is due primarily to the \$2 billion outstanding debt assumed as a result of the Transco Energy acquisition. The long-term debt to debt-plus-equity ratio was 47.4 percent at year-end, compared with 46.5 percent and 48.2 percent at December 31, 1994 and 1993, respectively. Included in long-term debt due within one year at December 31, 1994, was \$350 million outstanding under Williams' revolving credit loan.

See Note 8 for information regarding early extinguishment of debt by Williams and one of its subsidiaries during 1994.

Investing Activities

Net cash provided (used) by investing activities was: 1995 — \$585 million: 1994 — (\$427) million; and 1993 — (\$277) million. Capital expenditures of pipeline subsidiaries, including gathering and processing facilities, primarily to expand and modernize systems, were \$734 million in 1995; \$272 million in 1994; and \$405 million in 1993. Capital expenditures for discontinued operations were \$143 million and \$101 million in 1994 and 1993, respectively, primarily to expand and enhance Williams' network services operations network. Expenditures in 1995 include Transcontinental Gas Pipe Line and Northwest Pipeline's expansions as well as expansion of gathering and processing facilities. Expenditures in 1994 include Northwest Pipeline's additional mainline expansion and the expansion of various gathering and processing facilities. Expenditures in 1993 include the completion of Northwest Pipeline's first mainline expansion and the expansion of various gathering and processing facilities. Budgeted capital expenditures and acquisitions for 1996 are approximately \$1.3 billion, primarily to expand pipeline systems and gathering and processing facilities, expand the telecommunications network and acquire the remaining interest in Kern River Gas Transmission.

During 1995, Williams received proceeds of \$124 million from the sale of its 15 percent interest in Texasgulf Inc. (see Note 5). During 1994, Williams received net proceeds of \$80 million from the sale of limited partner units in Northern Border Partners, L.P. During 1993. Williams received net proceeds of \$113 million from the sale of 6.1 million units in the Williams Coal Seam Gas Royalty Trust. In addition, Williams sold its intrastate natural gas pipeline system and other related assets in Louisiana for \$170 million (see Note 6).

During 1995, in addition to the Transco Energy acquisition (see Note 2), Williams acquired the Gas Company of New Mexico's natural gas gathering and processing assets in the San Juan and Permian basins for \$154 million (including approximately 10 percent of which was immediately sold to a third party) and Pekin Energy Co., the nation's second largest ethanol producer, for \$167 million in cash.

Effects of Inflation

Williams has experienced increased costs in recent years due to the effects of inflation. However, approximately 55 percent of Williams' property, plant and equipment was acquired or constructed during 1995, while the remainder was purchased or constructed since 1982, a period of relatively low inflation. A substantial portion of Williams' property, plant and equipment is subject to regulation, which limits recovery to historical cost. While Williams believes it will be allowed the opportunity to earn a return based on the actual cost incurred to replace existing assets, competition or other market factors may limit the ability to recover such increased costs.

Environmental

Williams is a participant in certain environmental activities in various stages involving assessment studies, cleanup operations and/or remedial processes. The sites, some of which are not currently owned by Williams (see Note 17), are being monitored by Williams, other potentially responsible parties, U.S. Environmental Protection Agency (EPA), or other governmental authorities in a coordinated effort. In addition, Williams maintains an active monitoring program for its continued remediation and cleanup of certain sites connected with its refined products pipeline activities. Williams has both joint and several liability in some of these activities and sole responsibility in others. Current estimates of the most likely costs of such cleanup activities, after payments by other parties, are approximately \$86 million, all of which is accrued at December 31, 1995. Williams expects to seek recovery of approximately \$72 million of the accrued costs through future rates. Williams will fund these costs from operations and/or available bank-credit facilities. The actual costs incurred will depend on the final amount, type and extent of contamination discovered at these sites, the final cleanup standards mandated by the EPA or other governmental authorities, and other factors.

Subsequent Events

In January 1996, the Williams Board of Directors increased the quarterly cash dividend on Williams common stock to \$.34 per share, a 25.9 percent increase over the previous amount.

Item 8. Financial Statements and Supplementary Data

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REPORT OF INDEPENDENT AUDITORS

To The Stockholders of The Williams Companies, Inc.

We have audited the accompanying consolidated balance sheet of The Williams Companies, Inc. as of December 31, 1995 and 1994, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 1995. Our audits also included the financial statement schedules listed in the Index at Item 14(a). These financial statements and schedules are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedules based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Williams Companies, Inc. at December 31, 1995 and 1994, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 1995, in conformity with generally accepted accounting principles. Also, in our opinion, the related financial statement schedules, when considered in relation to the basic financial statements taken as a whole, present fairly in all material respects the information set forth therein.

ERNST & YOUNG LLP

Tulsa, Oklahoma February 9, 1996

THE WILLIAMS COMPANIES, INC. CONSOLIDATED STATEMENT OF INCOME

	Years	er 31,	
	1995	1994*	1993*
	(Millions, e	acept per-shar	r amounts)
Revenues:			
Williams Interstate Natural Gas Systems (Note 4)	\$1,431.1	\$ 469.8	\$ 570.6
Williams Field Services Group	591.8	375.7	432.2
Williams Energy Services (Note 15)	85.8	263.7	360.8
Williams Pipe Line	350.2 494.9	310.7	180.5
WilTel	44.0	396.6 20.0	302.8 13.5
WilTech Group	17.4	20.0	-
Other Intercompany eliminations (Note 16)	(159.5)	(85.4)	(67.0)
Total revenues	2,855.7	1,751.1	1,793.4
Profit-center costs and expenses:			
Costs and operating expenses	1,700.7	1,187.7	1,283.9
Selling, general and administrative expenses	488.8	229.2	203.2
Other income — net	(4.5)	(8.1)	(7.8)
Total profit-center costs and expenses	2,185.0	1,408.8	1,479.3
Operating profit (loss):			
Williams Interstate Natural Gas Systems (Note 4)	389.7	152.9	139.8
Williams Field Services Group	157.6	129.3	126.7
Williams Energy Services	30.0	.5	7.9
Williams Pipe Line	69.8	52.0	47.2
WilTel	28.3	18.9	9.5
WilTech Group	(3.3)	(11.3)	(17.0)
Other	(1.4)		
Total operating profit	670.7	342.3	314.1
General corporate expenses	(37.7)	(28.0)	(38.4)
Interest accrued	(277.9)	(145.8)	(151.2)
Interest capitalized	14.5	6.0	10.4
Investing income (Note 5)	93.9	49.6	65.2
Gain (loss) on sales of assets (Notes 5 and 6)	(12.6)	22.7	97.5
Write-off of project costs (Note 6)	(41.4)	-	-
Other income (expense) — net	(8.1)	(.2)	.4
Income from continuing operations before income taxes	401.4	246.6	298.0
Provision for income taxes (Note 7)	102.0	81.7	112.6
Income from continuing operations	299.4	164.9	185.4
Income from discontinued operations (Note 3)	1,018.8	94.0	46.4
Income before extraordinary loss	1,318.2	258.9	231.8
Extraordinary loss (Note 8)	-	(12.2)	_
Net income	1,318.2	246.7	231.8
Preferred stock dividends (Note 14)	15.3	8.8	11.8
Income applicable to common stock	\$1,302.9	\$ 237.9	\$ 220.0
income applicable to common stock	destructure of the same of the	THE RESIDENCE AND ADDRESS OF THE PERSON NAMED IN COLUMN TWO IN COLUMN TO ADDRESS OF THE PERSON NAMED IN COLUMN TO ADDRE	2 250.0

[·] Reclassified as described in Note 1.

THE WILLIAMS COMPANIES, INC. CONSOLIDATED STATEMENT OF INCOME — (Concluded)

	Years Ended December 31			
	1995	1994	1993	
Primary earnings per common and common-equivalent share (Notes 1, 3 and 8):				
Income from continuing operations	\$ 2.78 9.99	\$1.52 .92	\$1.74	
Income before extraordinary loss	12.77	2.44	2.20	
Net income	\$12.77	\$2.32	\$2.20	
Fully diluted earnings per common and common-equivalent share (Notes 1, 3 and 8):	anacoma.	MUTUALINE.	total and	
Income from continuing operations	\$ 2.76 9.72	\$1.52	\$1.71	
Income before extraordinary loss	12.48	2.44	2.16	
Net income	\$12.48	\$2.32	\$2.16	

THE WILLIAMS COMPANIES, INC. CONSOLIDATED BALANCE SHEET

ASSETS

	Decemb	er 31.
	1995	1994
	(Dollars in except per-sha	
Current assets:	S311120414-1117	
Cash and cash equivalents	\$ 90.4	\$ 36.1
Receivables less allowance of \$11.3 (\$7.9 in 1994)	525.0	443.1
Transportation and exchange gas receivable	152.3	9.2
Inventories (Note 10)	189.0	112.3
Net assets of discontinued operations (Note 3)	_	743.6
Deferred income taxes (Note 7)	213.9	57.1
Other	173.2	55.4
Total current assets	1,343.8	1.456.8
Investments (Note 5)	307.6	379.1
Property, plant and equipment — net (Note 11)	8,014.7	3,124.0
Other assets and deferred charges	828.7	266.2
Total assets	\$10,494.8	\$5,226.1
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities: Notes payable (Note 13)	s -	\$ 507.0
Accounts payable (Note 12)	472.0	205.8
Transportation and exchange gas payable	127.8	16.7
Accrued liabilities (Note 12)	1,130.2	361.4
Long-term debt due within one year (Note 13)	319.9	383.0
Total current liabilities	2,049.9	1,473.9
Long-term debt (Note 13)	2,874.0	1,307.8
Deferred income taxes (Note 7)	1,568.2	662.9
Other liabilities	815.6	276.0
Contingent liabilities and commitments (Note 17)		
Stockholders' equity (Note 14):		
Preferred stock, \$1 par value, 30,000,000 shares authorized, 3,739,452 shares		
issued in 1995 and 4,000,000 shares issued in 1994	173.5	100.0
Common stock, \$1 par value, 240,000,000 shares authorized, 105,337,948 shares	1,000,000	2742100000
issued in 1995 and 104,401,819 shares issued in 1994	105.3	104.4
Capital in excess of par value	1,051.1	991.0
Retained earnings (Note 13)	1,915.6	716.5
Unamortized deferred compensation	(2.3)	(1.3
The second secon	3,243.2	1,910.6
Less treasury stock (at cost), 1,573,203 shares of common stock in 1995 and		
13,516,994 shares of common stock in 1994, 401,600 shares of preferred	166.11	cans a
stock in 1995 and 258,800 shares of preferred stock in 1994	(56.1)	(405.1
Total stockholders' equity	3,187.1	1,505.5
Total liabilities and stockholders' equity	\$10,494.8	\$5,226.1

THE WILLIAMS COMPANIES, INC. CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

	Preferred Stock	Common Stock	Capital in Excess of Par Value	Retained Earnings (Millions)	Unamortized Deferred Compensation	Treasury Stock	Total
Balance, December 31, 1992	\$ 250.0	\$ 92.3	\$ 755.4	\$ 421.3	\$ (.7)	s -	\$1,518.3
Net income — 1993 Cash dividends —	-	-		231.8	-	-	231.8
Common stock (\$.78 per share)	-	7.00	777	(77.6)	-		(77.6)
Preferred stock (Note 14)	-	***		(11.8)	_		(11.8)
Issuance of shares — 3,174,439 common		3.2	55.2	-	(1.7)	-	56.7
Tax benefit of non-qualified stock (Note 14)	(150.0)	7.6	141.8	_	-		(.6)
exercises	-	man.	6.7	-	_	-	6.7
Amortization of deferred compensation					.5	_	.5
Balance, December 31, 1993	100.0	103.1	959.1	563.7	(1.9)	-	1,724.0
Net income — 1994	-		-	246.7	_	(100)	246.7
Common stock (\$.84 per share)	-		-	(85.1)	-	-	(85.1)
Preferred stock (Note 14)	-	-	-	(8.8)	-		(8.8)
Issuance of shares — 1,596,409 common		1.3	30.1		(1.3)	8.1	38.2
Purchase of treasury stock —					400000		
Common 13,790,089	-	_	_	-		(406.8)	(406.8)
Preferred 258,800	-	-	_	_	-	(6.4)	(6.4)
Tax benefit of non-qualified stock option							
exercises	party.	_	1.8	_	-	-	1.8
Amortization of deferred compensation					1.9	-	1.9
Balance, December 31, 1994	100.0	104.4	991.0	716.5	(1.3)	(405.1)	1,505.5
Net income — 1995			-	1,318.2	-	-	1,318.2
Common stock (\$1.08 per share)		_	_	(107.2)	-	_	(107.2)
Preferred stock (Note 14)	-	-	-	(11.9)	-	-	(11.9)
12,879,920 common		.9	58.8	-	(1.7)	352.7	410.7
2,500,000 preferred	142.5	-		-	-	_	142.5
Exchange of shares for debentures -							
2,760,548 preferred (Note 14)	(69.0)	****	(3.5)	-	-	-	(72.5)
Purchase of treasury stock							
142,800 preferred	-	-	_	-	-	(3.7)	(3.7)
Tax benefit of non-qualified stock option							
exercises	-	-	4.8	-	-		4.8
Amortization of deferred compensation		-	-		7	-	7
Balance, December 31, 1995	\$ 173.5	\$105.3	\$1,051.1	\$1,915.6	\$(2.3)	\$ (56.1)	\$3,187.1

THE WILLIAMS COMPANIES, INC. CONSOLIDATED STATEMENT OF CASH FLOWS

	Years Ended December 31,		
	1995	1994	1993
		(Millions)	
Operating Activities: Net income	\$ 1,318.2	\$ 246.7	\$ 231.8
Adjustments to reconcile to cash provided from operations: Discontinued operations	(8.810,1)	(94.0)	(46.4
Extraordinary loss	2.0.4	12.2	127.0
Depreciation and depletion	369.4	150.3	137.8
Provision for deferred income taxes	125.4	25.8	8.1
Write-off of project costs	(2.1)	.9	(102.0
(Gain) loss on sales of property, plant and equipment	100		(102.0
(Gain) loss on sale of investments	12.6 55.9	(22.7)	(94.7
Changes in receivables sold	33.2	(175.0)	99.9
Changes in receivables	11.9	10.2	(.8
Changes in inventories	(10.2)	(2.8)	(16.9
Changes in other current assets	(6.5)	20.7	(37.6
Changes in accounts payable	(3.3)	8.1	(43.2
Changes in accrued liabilities	(72.9)	(2.4)	1,42.0
Net change in non-current unrealized trading assets and liabilities	(25.5)	1.6*	50.9
Other, including changes in non-current assets and liabilities	the same and		
Net cash provided by continuing operations Net cash provided by discontinued operations	828.7	179.6 169.4*	186.9 162.6
Net cash provided by operating activities	828.7	349.0	349.5
Financing Activities:		102.0	
Proceeds from notes payable	116.8	507.0	-
Payments of notes payable	(623.8)	400.0	
Proceeds from long-term debt	399.0	480.0	(192.2
Payments of long-term debt	(1,009.4)	(456.5)	63.4
Proceeds from issuance of common stock	78.1	(413.2)	0.5.
Purchases of treasury stock	(119.1)	(93.9)	(89.4
Dividends paid	(193.7)	(73.7)	(1.5
Subsidiary preferred stock redemptions	(3.5)		(.2
Other — net	(1,359.3)	49.8*	(220.3
Net cash provided (used) by financing activities	(1,337,3)	47.0	1220.
Property, plant and equipment:			
Capital expenditures:	(827.5)	(325.5)	(428.3
Continuing operations	(827.5)	(142.8)	(100.8
Discontinued operations	28.2	1.6	295.4
Proceeds from sales	(5.2)	19.1	(48.4
Changes in accounts payable and accrued liabilities	(858.9)	(56.5)	
	2,588.3	(1012)	
Proceeds from sales of businesses Income tax and other payments related to discontinued operations	(350.4)	(1.5)	(1.5
Proceeds from sales of investments	125.1	80.6	8.8
Purchase of investments	(49.7)	(3.3)	
Purchase of note receivable	(75.1)	-	-
Other — net	10.1	1.3	(2.0
Net cash provided (used) by investing activities	584.9	(427.0)	(277.2
Increase (decrease) in cash and cash equivalents	54.3	(28.2)	(148.0
Cash and cash equivalents at beginning of year	36.1	64.3	212.3
Cash and cash equivalents at beginning of year.			

[·] Reclassified to conform to current classification.

Note 1 - Summary of significant accounting policies

Nature of operations

The Williams Companies, Inc. (Williams) operations are located in the United States and consist primarily of the following: five interstate natural gas pipelines located in the eastern, midsouth, Gulf Coast, midwest and northwest regions; natural gas gathering and processing facilities in the rocky mountain, midwest and Gulf Coast regions; energy trading throughout the United States; petroleum products pipeline in the midwest region; and national data, voice and video communication products and services. Additional information about these businesses is contained throughout the following notes.

Basis of presentation

Revenues and operating profit amounts include the operating results of Transco Energy Company (Transco Energy) since its January 18, 1995, acquisition by Williams (see Note 2). The transportation operations from Transco Energy's two interstate natural gas pipelines are reported separately within Williams Interstate Natural Gas Systems (see Note 4). Transco Energy's gas gathering operations are included as part of Williams Field Services Group, and Transco Energy's gas marketing operations are included in Williams Energy Services.

Revenues and operating profit amounts for 1994 and 1993 have been reclassified to conform to current year classifications. Commodity price-risk management and trading operations and energy-related information services operations are included in Williams Energy Services. Liquid fuels operations are reported as part of Williams Pipe Line and continue with the Williams Energy Ventures name. In addition, certain natural gas marketing operations formerly reported as part of Williams Field Services Group are included in Williams Energy Services. The WilTech Group, which owns a national fiber-optic network, was previously reported in other revenues and operating profit.

Principles of consolidation

The consolidated financial statements include the accounts of Williams and its majority-owned subsidiaries. Companies in which Williams and its subsidiaries own 20 percent to 50 percent of the voting common stock, or otherwise exercise sufficient influence over operating and financial policies of the company, are accounted for under the equity method.

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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.

Cash and cash equivalents

Cash and cash equivalents include demand and time deposits, certificates of deposit and other marketable securities with maturities of three months or less when acquired.

Transportation and exchange gas imbalances

In the course of providing transportation services to customers, the natural gas pipelines may receive different quantities of gas from shippers than the quantities delivered on behalf of those shippers. Additionally, the pipelines and other Williams subsidiaries transport gas on various pipeline systems which may deliver different quantities of gas on their behalf than the quantities of gas received. These transactions result in gas transportation and exchange imbalance receivables and payables which are recovered or repaid in cash or

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

through the receipt or delivery of gas in the future. Settlement of imbalances requires agreement between the pipelines and shippers as to allocations of volumes to specific transportation contracts and timing of delivery of gas based on operational conditions. Transcontinental Gas Pipe Line's imbalances predating August 1, 1991, are being recovered or repaid in eash or through the receipt or delivery of gas upon agreements of allocation.

Inventory valuation

Inventories are stated at cost, which is not in excess of market, except for those held by Williams Energy Services which are stated at market. Inventories of natural gas are determined using the last-in, first-out (LIFO) method by Transcontinental Gas Pipe Line and the average-cost method by other subsidiaries. Except for Williams Energy Services, inventories of petroleum products are determined using average cost. The cost of materials and supplies inventories is determined using the first-in, first-out method (FIFO) by WilTel and principally using the average-cost method by other subsidiaries.

Property, plant and equipment

Property, plant and equipment is recorded at cost. Depreciation is provided primarily on the straight-line method over estimated useful lives. Gains or losses from the ordinary sale or retirement of property, plant and equipment for regulated pipeline subsidiaries are credited or charged to accumulated depreciation; other gains or losses are recorded in net income.

Treasury stock

Treasury stock purchases are accounted for under the cost method whereby the entire cost of the acquired stock is recorded as treasury stock. Gains and losses on the subsequent reissuance of shares are credited or charged to capital in excess of par value using the average-cost method.

Revenue recognition

Revenues generally are recorded when services have been performed or products have been delivered. Williams Pipe Line bills customers when products are shipped and defers the estimated revenues for shipments in transit. Williams interstate natural gas pipelines recognize revenues based upon contractual terms and the related transportation volumes through month-end. These pipelines are subject to Federal Energy Regulatory Commission (FERC) regulations and, accordingly, certain revenues are subject to possible refunds pending final FERC orders. Williams records rate refund accruals based on management's estimate of the expected outcome of these proceedings.

Commodity price-risk management activities

Williams Energy Services enters into energy-related financial instruments (forward contracts, futures contracts, option contracts and swap agreements) to provide price-risk management services to its third-party customers. This subsidiary also enters into short- and long-term energy-related purchase and sale commitments as part of its trading business. All of these investments and commitments are valued at market and are recorded in other current assets, other assets and deferred charges, accrued liabilities and other liabilities in the Consolidated Balance Sheet. The resulting change in unrealized market gains and losses is recognized in income currently and is recorded as revenues in the Consolidated Statement of Income. Such market values are subject to change in the near term and reflect management's best estimate of market prices considering various factors including closing exchange and over-the-counter quotations, the terms of the contract, credit considerations, time value and volatility factors underlying the positions.

Williams Energy Services reports sales of natural gas, refined products and crude oil net of the related costs to purchase such items, consistent with mark-to-market accounting for such trading activities.

Other Williams operations enter into energy-related financial instruments (primarily futures contracts, option contracts and swap agreements) to hedge against market price fluctuations of certain commodity inventories and sales and purchase commitments. Unrealized and realized gains and losses on these hedge contracts are deferred and recognized in income when the related hedged item is recognized. These contracts are evaluated to determine that there is a high correlation between changes in the market value of the hedge contract and fair value of the hedged item.

Capitalization of interest

Williams capitalizes interest on major projects during construction. Interest is capitalized on borrowed funds and, where regulation by the FERC exists, on internally generated funds. The rates used by regulated companies are calculated in accordance with FERC rules. Rates used by unregulated companies approximate the average interest rate on related debt. Interest capitalized on internally generated funds is included in other income (expense) — net.

Income taxes

Williams includes the operations of its subsidiaries in its consolidated federal income tax return. Deferred income taxes are computed using the liability method and are provided on all temporary differences between the financial basis and the tax basis of Williams' assets and liabilities.

Earnings per share

Primary earnings per share are based on the sum of the average number of common shares outstanding and common-share equivalents resulting from stock options and deferred shares. Fully diluted earnings per share for 1995 assumes conversion of the \$3.50 convertible preferred stock into common stock effective May 1, 1995. Shares used in determination of primary earnings per share are as follows (in thousands): 1995—102,046; 1994—102,470; and 1993—99,911. Shares used in determination of fully diluted earnings per share are as follows (in thousands): 1995—104,853; 1994—102,502; and 1993—103,171.

Note 2 - Transco Energy acquisition

On January 18, 1995, Williams acquired 60 percent of Transco Energy's outstanding common stock in a cash tender offer for \$430.5 million. Williams acquired the remaining 40 percent of Transco Energy's outstanding common stock on May 1, 1995, through a merger by exchanging the remaining Transco Energy common stock for approximately 10.4 million shares of Williams common stock valued at \$334 million. The acquisition is accounted for as a purchase with 60 percent of Transco Energy's results of operations included in Williams' Consolidated Statement of Income for the period January 18, 1995, through April 30, 1995, and 100 percent included beginning May 1, 1995. The purchase price, including transaction fees and other related costs, is approximately \$800 million, excluding \$2.3 billion in preferred stock and debt obligations of Transco Energy. The acquired assets and liabilities have been recorded based on an allocation of the purchase price with substantially all of the cost in excess of Transco Energy's historical carrying amounts allocated to property, plant and equipment of the two interstate natural gas pipeline systems. The cash portion of the acquisition was financed with the proceeds from the sale of Williams' network services operations (see Note 3).

Transco Energy was engaged primarily in the natural gas pipeline and natural gas marketing businesses. Williams has sold substantially all of Transco Energy's coal operations, coalbed methane properties and certain pipeline and gathering operations. Results of operations and changes in the carrying amount of these businesses during the holding period and from the ultimate dispositions are reflected in the purchase price and are not material.

In connection with the acquisition, Williams made payments to retire and/or terminate approximately \$700 million of Transco Energy borrowings, preferred stock, interest-rate swaps and sale of receivable facilities. As a part of the merger, Williams exchanged Transco Energy's \$3.50 preferred stock for Williams' \$3.50 preferred stock.

The following unaudited pro forma information combines the results of operations of Williams and Transco Energy as if the purchase of 100 percent of Transco Energy occurred January 1, 1994.

	Unaudited			
	1995	1994		
		amounts)		
Revenues	\$2,916.4	\$2,660.3		
Income from continuing operations	314.4	191.0		
Income before extraordinary loss	1,333.2	285.0		
Net income	1,333.2	272.8		
Primary earnings per share:				
Income from continuing operations	2.93	1.77		
Income before extraordinary loss	12.92	2.69		
Net income	12.92	2.57		
Fully diluted earnings per share:				
Income from continuing operations	2.90	1.77		
Income before extraordinary loss	12.62	2.69		
Nat income	12.62	2.57		

Pro forma financial information is not necessarily indicative of results of operations that would have occurred if the acquisition had occurred on January 1, 1994, or of future results of operations of the combined companies.

Note 3 - Discontinued operations

On January 5, 1995, Williams sold its network services operations to LDDS Communications, Inc. (LDDS) for \$2.5 billion in cash. The sale yielded a gain of \$1 billion (net of income taxes of approximately \$732 million) which is reported as income from discontinued operations. Prior period operating results for the network services operations are reported as discontinued operations. Under the terms of the agreement, Williams retained Williams Telecommunications Systems, Inc. (WilTel), a national telecommunications equipment supplier and service company, and Vyvx, Inc. (included in WilTech Group), which operates a national video network specializing in broadcast television applications.

Summarized operating results of discontinued operations are as follows:

	1994	1997
	(Mill	lions)
Revenues	\$921.8	\$663.8
Operating profit	163.1	97.0
Provision for income taxes	60.9	32.2
Income from discontinued operations	94.0	46.4

The assets and liabilities that were transferred to LDDS in the sale of the network services operations are presented in the Consolidated Balance Sheet on a net basis at December 31, 1994. Net assets consist of current assets (\$86.5 million), net property, plant and equipment (\$797.8 million), other assets and deferred charges (\$144.3 million), less current liabilities (\$218.3 million) and other liabilities (\$66.7 million).

Note 4 — Williams Interstate Natural Gas Systems

		Revenues		0	perating pro	ofit
	1995	1994	1993	1995	1994	1993
			(Mill	ions)		
Northwest Pipeline	\$ 255.2	\$238.5	\$276.5	\$115.7	\$104.1	\$ 98.8
Williams Natural Gas	174.	231.3	294.1	45.0	48.8	41.0
Transcontinental Gas Pipe Line	725.3	-	_	165.0	_	_
Texas Gas Transmission	276.3		_	64.0	_	_
	\$1,431.1	\$469.8	\$570.6	\$389.7	\$152.9	\$139.8
		-			The second second	1000

Note 5 - Investing activities

	1995	1994
	(Mil	lions)
Investments:		
Kern River Gas Transmission Company, at equity (50%)	\$178.6	\$179.4
Texasgulf Inc. (15%)	_	150.0
Other, at equity (varying ownerships from 3.2% to 50%)	84.2	49.7
Other, at cost	44.8	_
	\$307.6	\$379.1

At December 31, 1995, certain equity investments, with a carrying value of \$30.8 million, have a market value of \$81.5 million.

In 1995, Williams sold its 15 percent interest in Texasgulf Inc. for approximately \$124 million in cash, which resulted in an after-tax gain of approximately \$16 million because of previously unrecognized tax benefits included in the provision for income taxes.

Subsequent to December 31, 1995, Williams acquired the remaining interest in Kern River Gas Transmission Company for \$205 million in cash. The acquisition will be accounted for as a purchase in 1996, and the excess purchase price will be allocated to property, plant and equipment.

Summarized financial position and results of operations for Kern River Gas Transmission Company are presented below.

	1995		The second secon		and the second s		1993
			()	Millie)			
Current assets	S	55.4	S	98.3	5	80.1	
Non-current assets, principally natural gas transmission plant		994.5		1,026.3	- 1	,028.7	
Current liabilities		(47.3)		(86.9)		(62.1)	
Long-term debt		(620.5)		(643.2)		(662.9)	
Other non-current liabilities	_	(124.1)		(109.5)		(66.9)	
Partners' equity	5	258.0	\$	285.0	5	316.9	
Revenues	5	187.0	s	179.0	5	176.8	
Costs and expenses		65.7		54.9		48.7	
Net income		38.0		38.1		42.1	

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Investing income from continuing operations:

	1995	1994	1993
		(Millions)	S
Interest	\$37.2	\$ 5.5	\$10.0
Dividends	16.1	4.5	5.6
Equity earnings	40.6	39.6	49.6
	\$93.9	\$49.6	\$65.2

Dividends and distributions received from companies carried on an equity basis were \$44 million in 1995; \$43 million in 1994; and \$39 million in 1993.

Note 6 - Asset sales and write-off of project costs

In the fourth quarter of 1995, the development of a commercial coal gasification venture in south-central Wyoming was canceled, resulting in a \$41.4 million pre-tax charge. This amount includes what management believes to be a reasonable estimate of future costs of \$4 million to reclaim the site, of which it is expected that 60 percent to 70 percent will be incurred during 1996 and the remainder over a five-year period. Williams will perform the reclamation of the site in coordination with various governmental agencies and expects to receive necessary environmental releases and approvals upon completion of the reclamation.

In 1994, Williams sold 3,461,500 limited partner common units in Northern Border Partners, L.P. Net proceeds from the sale were approximately \$80 million and the sale resulted in a pre-tax gain of \$22.7 million. As a result of the sale, Williams' original 12.25 percent interest in Northern Border partnerships has been reduced to 3.2 percent.

In a 1993 public offering, Williams sold 6.1 million units in the Williams Coal Seam Gas Royalty Trust (Trust), which resulted in net proceeds of \$113 million and a pre-tax gain of \$51.6 million. The Trust owns defined net profits interests in the developed coal-seam properties in the San Juan Basin of New Mexico and Colorado, which were conveyed to the Trust by Williams Production Company. Ownership of an additional 3.6 million units remains with Williams.

In March 1993, Williams sold its intrastate natural gas pipeline system and other related assets in Louisiana for \$170 million in cash, resulting in a pre-tax gain of \$45.9 million.

Note 7 - Provision for income taxes

The provision (credit) for income taxes from continuing operations includes:

	1995	1994	1993
	-	(Millions)	
Current: Federal		\$45.8 10.1 55.9	\$ 84.1 20.4 104.5
Deferred:		-	
Federal	114.2	23.7	15.8
State	_11.2	2.1	_ (7.7)
	125.4	25.8	8.1
Total provision	\$102.0	\$81.7	\$112.5

Reconciliations from the provision for income taxes attributable to continuing operations at the statutory rate to the provision for income taxes are as follows:

	1995	(Millions)	1993
Provision at statutory rate	\$140.5	\$ 86.3	\$104.3
Increases (reductions) in taxes resulting from: Increase in statutory tax rate on beginning of year deferred tax			
balances	auto.	-	15.8
State income taxes	13.5	8.0	8.2
Coal-seam tax credits	(18.7)	(14.9)	(12.8)
Decrease in valuation allowance for deferred tax assets	(29.8)	-	
Reversal of prior tax accruals	(8.0)	-	-
Other — net	4.5	2.3	(2.9)
Provision for income taxes	\$102.0	\$ 81.7	\$112.6

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial purposes and the amounts used for income tax purposes.

Significant components of deferred tax liabilities and assets as of December 31 are as follows:

	1995	1994*
	(Mill	ons)
Deferred tax liabilities:		
Property, plant and equipment	\$1,669.2	\$704.6
Investments	96.9	81.9
Other	248.1	74.7
Total deferred tax liabilities	2,014.2	861.2
Deferred tax assets:		
Deferred revenues	23.5	40.0
Investments	31.3	55.9
Rate refunds	70.7	32.0
Accrued liabilities	226.4	64.2
Minimum tax credits	93.9	_
Other	220.5	93.1
Total deferred tax assets	666.3	285.2
Valuation allowance for deferred tax assets	6.4	29.8
Net deferred tax assets	659.9	255.4
Net deferred tax liabilities	\$1,354.3	\$605.8
	-	

[·] Reclassified to conform to current classification.

The valuation allowance for deferred tax assets decreased \$23.4 million and \$1.7 million during 1995 and 1994, respectively.

Cash payments for income taxes are as follows: 1995 — \$348 million, before refunds of \$9 million; 1994 — \$113 million, before refunds of \$6 million; and 1993 — \$129 million.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Note 8 — Extraordinary loss

The extraordinary loss in 1994 resulted from early extinguishment of debt. Williams and one of its subsidiaries paid \$316.7 million to redeem higher interest rate debt for a \$12.2 million net loss (net of a \$7.7 million benefit for income taxes).

Note 9 - Employee benefit plans

Pensions

Williams maintains non-contributory defined-benefit pension plans covering the majority of employees. Benefits are based on years of service and average final compensation. Pension costs are funded to satisfy minimum requirements prescribed by the Employee Retirement Income Security Act of 1974.

Net pension expense consists of the following:

1.00 E-1	_	1995	-	1994 ittions)	1993
Service cost for benefits earned during the year Interest cost on projected benefit obligation Actual return on plan assets Amortization and deferrals Settlement loss	\$	19.5 40.1 (120.3) 82.0		13.9 21.8 3.1 (24.2)	\$ 10.9 21.1 (28.3) 8.2 5.7
Net pension expense	\$	21.3	5	14.6	5 17.6
Net pension expense: Continuing operations Discontinued operations	5	21.3	s	10.0 4.6 14.6	\$ 14.9 2.7 \$ 17.6

Included in net pension expense at December 31, 1995, is approximately \$8.9 million for the Transco Energy plans' participants.

During 1993, certain supplemental retirement plan participants elected to receive lump-sum benefits, which resulted in a settlement loss of \$5.7 million.

The following table presents the funded status of the plans:

	1995	1994
	(Mill	ions)
Actuarial present value of benefit obligations:		
Vested benefits	\$422	\$191
Non-vested benefits	21	10
Accumulated benefit obligations	443	201
Effect of projected salary increases	137	58
Projected benefit obligations	580	259
Assets at market value	550	251
Assets less than projected benefit obligations	30	8
Unrecognized net loss	-	(12)
Unrecognized prior-service cost	(11)	(10)
Unrecognized transition asset	4	5
Pension liability (asset)	\$ 23	\$ (9)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

At December 31, 1995, assets of two pension plans exceeded the projected benefit obligations with assets at market value of \$103 million and projected benefit obligations of \$57 million. At December 31, 1994, assets of two other pension plans exceeded the projected benefit obligations with assets at market value of \$238 million and projected benefit obligations of \$233 million.

Included in the net pension liability at December 31, 1995, is approximately \$32 million for the participants of the Transco Energy plans.

Williams has retained all liabilities and obligations of its network services operations' plan participants up to the date of sale (see Note 3).

The discount rate used to measure the present value of benefit obligations is 7½ percent (8½ percent in 1994); the assumed rate of increase in future compensation levels is 5 percent; and the expected long-term rate of return on assets is 10 percent. Plan assets consist primarily of commingled funds and assets held in a master trust. The master trust is comprised primarily of domestic and foreign common and preferred stocks, corporate bonds, United States government securities and commercial paper.

Postretirement benefits other than pensions

Williams sponsors health care plans that provide postretirement medical benefits to retired Williams' employees who were employed full time, hired prior to January 1, 1992 (January 1, 1996 for Transco Energy employees), have worked five years, attained age 55 while in service and are a participant in the company pension plans. In addition, two Transco Energy plans provide certain health care and life insurance benefits to retired employees of Transcontinental Gas Pipe Line, Texas Gas and other subsidiaries of Transco Energy.

The plans provide for retiree contributions and contain other cost-sharing features such as deductibles and coinsurance. The accounting for the plans anticipates future cost-sharing changes to the written plans that are consistent with Williams' expressed intent to increase the retiree contribution rate annually, generally in line with health care cost increases, except for certain retirees whose premiums are fixed. A portion of the cost has been funded in trusts by Williams' FERC-regulated natural gas pipeline subsidiaries to the extent recovery from customers can be achieved. Plan assets consist of assets held in two master trusts and money market funds. One of the master trusts was previously described and the other consists primarily of domestic and foreign common stocks, commercial paper and government bonds.

Net postretirement benefit expense consists of the following:

	1995	(Millions)	1993
Service cost for benefits earned during the year Interest cost on accumulated postretirement benefit obligation Actual return on plan assets Amortization of unrecognized transition obligation	\$ 7.4 23.9 (17.9) 5.0	\$ 3.9 7.8	\$ 3.7 8.2 (.7) 5.2
Amortization and deferrals	23.1	1	(3.5)
Net postretirement benefit expense: Net postretirement benefit expense:	\$ 41.5	\$16.3	\$12.9
Continuing operations	\$ 41.5	\$14.7	\$11.4
	\$ 41.5	\$16.3	\$12.9

Net postretirement benefit expense at December 31, 1995, includes approximately \$26 million for the Transco Energy plans' participants.

The following table presents the funded status of the plans:

	1995	1994
	(Mitt	ions)
Actuarial present value of postretirement benefit obligation:		
Retirces	\$227	\$ 55
Fully eligible active plan participants	24	11
Other active plan participants	85	34
Accumulated postretirement benefit obligation	336	100
Assets at market value	124	16
Assets less than accumulated postretirement benefit obligation	212	84
Unrecognized net gain	25	19
Unrecognized prior-service cost	(6)	
Unrecognized transition obligation	(71)	(78)
Postretirement benefit liability	\$160	\$ 25

Included in the postretirement benefit liability at December 31, 1995, is approximately \$139 million for the Transco Energy plans' participants, substantially all of which is classified as non-current. The amount of postretirement benefit costs deferred as a regulatory asset at December 31, 1995, is \$133 million and is expected to be recovered through rates over the next 17 years.

The discount rate used to measure the present value of benefit obligations is 7½ percent (8½ percent in 1994). The expected long-term rate of return on plan assets is 10 percent (6 percent after taxes). The annual assumed rate of increase in the health care cost trend rate for 1996 is 10 to 13 percent, systematically decreasing to 5 percent by 2006. The health care cost trend rate assumption has a significant effect on the amounts reported. Increasing the assumed health care cost trend rate by 1 percent in each year would increase the aggregate of the service and interest cost components of postretirement benefit expense for the year ended December 31, 1995, by \$5 million and the accumulated postretirement benefit obligation as of December 31, 1995, by \$50 million.

Other

Williams maintains various defined-contribution plans covering substantially all employees. Company contributions are based on employees' companies and, in part, match employee contributions. Company contributions are invested primarily in Williams common stock. Williams' contributions to these plans were \$19 million in 1995, \$14 million in 1994 and \$13 million in 1993. Contributions to these plans made by discontinued operations were \$3 million in both 1994 and 1993.

Effective January 1, 1994, Williams adopted Statement of Financial Accounting Standards (FAS) No. 112, "Employers' Accounting for Postemployment Benefits," which requires the accrual of benefits provided to former or inactive employees after employment but before retirement. Adoption of the standard reduced 1994 net income by approximately \$2 million and is not reported as a change in accounting principle due to immateriality.

Note 10 - Inventories

	1995	1994
	(Mil	lions)
Natural gas in underground storage:		
Transcontinental Gas Pipe Line (LIFO)	\$ 21.4	s -
Williams Energy Services	6.0	8.7
Other	2.2	9.9
Petroleum products:		555
Williams Energy Services	12.8	13.5
Other	27.4	19.2
Materials and supplies:		7.5.5
WilTel	28.2	28.6
Other	87.8	32.4
Other	3.2	_
	\$189.0	\$112.3

Inventories valued on the LIFO method at December 31, 1995, approximate current average cost.

Note 11 - Property, plant and equipment

	1995	1994
	(Mill	lions)
Cost:		
Northwest Pipeline	\$ 1,403.5	\$ 1,275.4
Williams Natural Gas	761.6	745.0
Transcontinental Gas Pipe Line	2,756.7	N. Constant
Texas Gas Transmission	917.3	
Williams Field Services Group	2,324.9	1,273.2
Williams Pipe Line	1,023.3	809.6
WilTel	55.2	32.1
WilTech Group	90.7	69.5
Other	145.5	106.3
	9,478.7	4,311.1
Accumulated depreciation	(1,464.0)	(1,187.1)
	\$ 8,014.7	\$ 3,124.0

Commitments for construction and acquisition of property, plant and equipment are approximately \$256 million at December 31, 1995.

The Financial Accounting Standards Board has issued a new accounting standard, FAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of," effective for fiscal years beginning after December 15, 1995. The standard, which will be adopted in the first quarter of 1996, is not expected to have a material effect on Williams' financial position or results of operations.

Note 12 - Accounts payable and accrued liabilities

Under Williams' cash-management system, certain subsidiaries' cash accounts reflect credit balances to the extent checks written have not been presented for payment. The amounts of these credit balances included in accounts payable are \$136 million at December 31, 1995, and \$41 million at December 31, 1994.

1995	1994
(Mill	ions)
	£ 10.0
\$ 371.6	\$ 38.0
180.6	83.8
135.9	51.7
72.9	39.9
1000	3.000000
51.2	41.8
318.0	106.2
\$1,130.2	\$361.4
	\$ 371.6 180.6 135.9 72.9 51.2 318.0

Note 13 - Debt, leases and banking arrangements

Notes payable

During 1994, a subsidiary of Williams entered into a \$400 million short-term credit agreement to finance the acquisition of Williams common stock. Notes payable totaling \$398 million were outstanding under this agreement at December 31, 1994. These notes were repaid in January 1995. The weighted average interest rate on the outstanding short-term borrowings at December 31, 1994, was 6.75 percent.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Debt

	Weighted average interest rate*	1995	1994
		(Mill	
The Williams Companies, Inc.			
Revolving credit loans	6.2%	\$ 50.0	\$ 350.0
2025	9.6	587.7	379.7
Notes, 7.5% — 9.625%, payable through 2001	8.8	842.4	363.8
Capital lease obligations, 11.1%		042.4	31.0
Northwest Pipeline	-		31.0
Debentures, 7.125% — 10.65%, payable through 2025	9.0	369.2	293.0
Adjustable rate notes, payable through 2002	9.0	11.7	13.3
Variable rate notes, payable 1999	6.3	:30.0	130.0
Transcontinental Gas Pipe Line	0.5	1,50.0	150.0
Debentures, 9.125%, payable 1998 through 2017	9.1	153.0	
Notes, 8.125% — 9%, payable 1996, 1997 and 2002		381.1	_
Adjustable rate notes, payable 2000 (subject to remarketing in		20111	
1996)	6.2	125.1	_
Texas Gas Transmission			
Notes, 9.625% and 8.625%, payable 1997 and 2004	9.0	255.9	_
Williams Holdings of Delaware		******	
Revolving credit loans	6.3	150.0	
Williams Pipe Line	0.000	1.000	
Notes, 8.95% and 9.78%, payable through 2001	9.3	110.0	120.0
Williams Energy Ventures		1100000	
Adjustable rate notes, payable 1996 through 2002	8.3	21.0	-
Other, payable through 1999		6.8	10.0
Subtractive of the state of the state of the subtractive of the state of the state of the subtractive of the		3,193.9	1,690.8
Current portion of long-term debt		(319.9)	(383.0)
p vi long tolin acontititititititititititititititi		\$2,874.0	\$1,307.8
		\$2,874.0	31,307,8

At December 31, 1995.

During 1995, Williams replaced its \$600 million credit agreement, which was scheduled to terminate in December 1995, with a new \$800 million agreement. Under the new credit agreement, Northwest Pipeline, Transcontinental Gas Pipe Line, Texas Gas Transmission, Williams Pipe Line and Williams Holdings of Delaware, Inc. have access to various amounts of the facility while Williams (parent) has access to all unborrowed amounts. Interest rates vary with current market conditions. Certain amounts outstanding at December 31, 1995, under this facility do not reduce amounts available to Williams in the future. The available amount at December 31, 1995, is \$670 million.

In January 1996, Williams Holdings of Delaware, Inc., a subsidiary of Williams, issued \$250 million of 6.25 percent debentures due 2006.

In January 1996, Williams entered into a \$205 million short-term borrowing agreement to finance the purchase of the remaining 50 percent interest in Kern River Gas Transmission Company (see Note 5).

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

In conjunction with the issuance of \$130 million of variable rate debt by Williams Natural Gas in November 1994, Williams entered into an interest-rate swap agreement under which Williams pays a 7.78 percent fixed rate in exchange for a variable rate (5.88 percent at December 31, 1995). The difference between the fixed and variable rate is included in interest expense.

Terms of certain subsidiaries' borrowing arrangements with institutional lenders limit the transfer of funds to Williams. At December 31, 1995, approximately \$933 million of net assets of consolidated subsidiaries was restricted. Undistributed earnings of companies and partnerships accounted for under the equity method of \$62 million are included in Williams' consolidated retained earnings at December 31, 1995.

Aggregate minimum maturities and sinking-fund requirements, excluding lease payments, for each of the next five years are as follows:

	(Millions)
1996	\$319
1997	222
1998	341
1999	313
2000	405

Cash payments for interest (net of amounts capitalized) related to continuing operations are as follows: 1995 — \$266 million; 1994 — \$143 million; and 1993 — \$144 million. Cash payments for interest (net of amounts capitalized) related to discentinued operations are as follows: 1994 — \$6 million and 1993 — \$16 million.

Leases

Future minimum annual rentals under non-cancelable operating leases related to continuing operations are \$52 million in 1996, \$47 million in 1997, \$42 million in 1998, \$39 million in 1999, \$37 million in 2000 and \$186 million thereafter.

Total rent expense from continuing operations was \$78 million in 1995, \$26 million in 1994 and \$22 million in 1993. Total rent expense from discontinued operations was \$70 million in 1994 and \$59 million in 1993.

Note 14 - Stockholders' equity

In connection with the May 1, 1995, merger with Transco Energy, Williams exchanged all of Transco Energy's outstanding \$3.50 cumulative convertible preferred stock for 2.5 million shares of Williams' \$3.50 cumulative convertible preferred stock. These shares are redeemable by Williams beginning in November 1999, at an initial price of \$51.40 per share. Each share of \$3.50 preferred stock is convertible at the option of the holder into 1.5625 shares of Williams common stock. Dividends per share of \$2.33 were recorded during 1995.

During 1995, Williams exchanged 2.8 million shares of its \$2.21 cumulative preferred stock with a carrying value of \$69 million for 9.6 percent debentures with a fair value of \$72.5 million. The difference in the fair value of the new securities and the carrying value of the preferred stock exchanged is recorded as a decrease in capital in excess of par value. This amount did not impact net income, but is included in preferred stock dividends on the income statement and in the computation of earnings per share. The 837,852 outstanding shares of \$2.21 cumulative preferred stock are redeemable by Williams at a price of \$25 beginning in September 1997. Dividends per share of \$2.21 were recorded each year during 1995, 1994 and 1993.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

During 1993, Williams called for redemption of its 3,000,000 shares of outstanding \$3.875 convertible exchangeable preferred stock. Substantially all of the preferred shares were converted into 7.6 million shares of Williams common stock. Dividends per share of \$.97 were recorded during 1993.

Subsequent to December 31, 1995, the board of directors adopted a Stockholder Rights Plan (the "Rights Plan") to replace its existing rights plan which expired on February 6, 1996. Under the Rights Plan. each outstanding share of common stock has one preferred stock purchase right attached. Under certain conditions, each right may be exercised to purchase, at an exercise price of \$140 (subject to adjustment), one two-hundredth of a share of junior participating preferred stock. The rights may be exercised only if an Acquiring Person acquires (or obtains the right to acquire) 15 percent or more of Williams common stock; or commences an offer for 15 percent or more of Williams common stock; or the board of directors determines an Adverse Person has become the owner of 10 percent or more of Williams common stock. The rights, which do not have voting rights, expire in 2006 and may be redeemed at a price of \$.01 per right prior to their expiration, or within a specified period of time after the occurrence of certain events. In the event a person becomes the owner of more than 15 percent of Williams common stock or the board of directors determines that a person is an Adverse Person, each holder of a right (except an Acquiring Person or an Adverse Person) shall have the right to receive, upon exercise, common stock having a value equal to two times the exercise price of the right. In the event Williams is engaged in a merger, business combination or 50 percent or more of Williams assets, cash flow or earnings power is sold or transferred, each holder of a right (except an Acquiring Person or an Adverse Person) shall have the right to receive, upon exercise, common stock of the acquiring company having a value equal to two times the exercise price of the right.

During 1995, the board of directors approved the Stock Plan for Non-officer Employees (the 1995 Plan). The 1995 Plan along with the 1990 Stock Plan (the 1990 Plan) permits granting of various types of awards including, but not limited to, stock options, stock-appreciation rights, restricted stock and deferred stock. The 1995 Plan provides for granting of awards to key non-officer employees. The 1990 Plan is used for granting of awards to executive officers of Williams. Such awards may be granted for no consideration other than prior and future services. The purchase price per share for stock options and stock-appreciation rights may not be less than the fair-market value of the stock on the date of grant. Another stock option plan provides for the granting of non-qualified options to non-employee directors. Options under the 1990 Plan generally become exercisable in three annual installments beginning within one year after grant. Options under the 1995 Plan generally become exercisable after five years, subject to accelerated vesting if certain stock prices are achieved. The options expire 10 years after grant.

The following summary reflects option transactions during 1995.

	2,884,008 2,261,058 (81,892) 1,024,250	Optio	n price
	Shares	Per share	Total
			(Millions)
Shares under option:			
December 31, 1994	2,884,008	\$11- 30	\$ 65
Granted	2,261,058	30- 40	80
Canceled or surrendered	(81,892)	14-40	(2)
Exchanged options from Transco Energy acquisition - net	1,024,250	21-172	35
Exercised	(841,491)	11- 40	(25)
December 31, 1995	5,245,933	\$11-172	\$153
Shares exercisable December 31, 1995	4,421,447		

Under the plans, Williams granted 65,445, 127,706 and 97,504 deferred shares in 1995, 1994 and 1993, respectively, to key employees. Deferred shares are valued at the date of award and are generally charged to

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

expense in the year of award. Williams issued 70,122, 45,298 and 191,007 of previously deferred shares in 1995, 1994 and 1993, respectively. Williams also issued 55,300, 44,800 and 62,000 shares of restricted stock in 1995, 1994 and 1993, respectively. Restricted stock is valued on the issuance date, and the related expense is amortized over varying periods of three to 10 years.

During November 1994, Williams entered into a deferred share agreement (the Agreement) in connection with the sale of its network services operations. Under the terms of the Agreement, Williams will distribute up to approximately 2.6 million shares of Williams common stock to key employees of the network services operations over various periods through 1998, less amounts necessary to meet minimum tax withholding requirements. Williams distributed 314,405 and 273,095 shares during 1995 and 1994, respectively.

At December 31, 1995, 9,849,891 shares of common stock were reserved for issuance pursuant to existing and future stock awards, of which 2,698,799 were available for future grants (1,835,014 at December 31, 1994).

The Financial Accounting Standards Board has issued a new accounting standard, FAS No. 123, "Accounting for Stock-Based Compensation," effective for fiscal years beginning after December 15, 1995. As provided for in the standard, Williams will not adopt the recognition provisions and will provide the proforma net income and earnings-per-share disclosures required by the standard in its 1996 annual financial statements.

Williams currently follows Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees." Under this standard, because the exercise price of Williams' fixed plan common stock options equals the market price of the underlying stock on the date of the grant, no compensation expense is recognized.

Note 15 - Financial instruments

Fair-value methods

The following methods and assumptions were used by Williams in estimating its fair-value disclosures for financial instruments:

Cash and cash equivalents and notes payable. The carrying amounts reported in the balance sheet approximate fair value due to the short-term maturity of these instruments.

Notes and other non-current receivables. For those notes with interest rates approximating market or maturities of less than three years, fair value is estimated to approximate historically recorded amounts. For those notes with maturities beyond three years and fixed interest rates, fair value is calculated using discounted cash flow analysis based on current market rates.

Long-term debt: The fair value of Williams' long-term debt is valued using indicative year-end traded bond market prices for publicly traded issues, while private debt is valued based on the prices of similar securities with similar terms and credit ratings. At December 31, 1995 and 1994, 85 percent and 59 percent, respectively, of Williams' long-term debt was publicly traded. Williams used the expertise of an outside investment banking firm to estimate the fair value of long-term debt.

Interest-rate swaps: Fair value is determined by discounting estimated future cash flows using forward interest rates implied by the year-end yield curve. Fair value was calculated by the financial institution that is the counterparty to the swap.

Energy-related trading and hedging: Includes forwards, futures, options, swaps and purchase and sales commitments. Fair value reflects management's best estimate of market prices considering various

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

factors including closing exchange and over-the-counter quotations, the terms of the contract, credit considerations, time value and volatility factors underlying the positions.

Carrying amounts and fair values of Williams' financial instruments

Asset (liability)

	1995				1994				
	Carrying Fair Amount Value		Carrying Amount			Fair alue			
				(Mill	ions)				
Cash and cash equivalents	S	90.4	5	90.4	5	36.1	5	36.1	
Notes and other non-current receivables		25.7		25.8		63.1		62.3	
Investment in Texasgulf Inc		-		\sim		150.0		150.0	
Notes payable		-		-		(507.0)		(507.0)	
Long-term debt, including current portion	(3	.193.1)	(3	,476.7)	(1	,657.6)	(1	,679.9)	
Interest-rate swaps		(.4)		(10.4)		(.3)		1.4	
Energy-related trading:									
Assets		102.5		102.5		22.7		22.7	
Liabilities		(283.1)		(283.1)		(15.8)		(15.8)	
Energy-related hedging:									
Assets		2.9		4.5		3		.3	
Liabilities		(.6)		(3.2)		(8.5)		(8.5)	

The above asset and liability amounts for energy-related hedging represent unrealized gains or losses and do not include the related deferred amounts.

The 1995 average fair value of the energy-related trading assets and liabilities is \$57.3 million and \$144.6 million, respectively. The 1994 average fair value of the energy-related trading assets and liabilities is \$9.2 million and \$8.5 million, respectively.

Williams has recorded liabilities of \$24 million and \$27 million at December 31, 1995 and 1994, respectively, for certain guarantees that qualify as financial instruments. It is not practicable to estimate the fair value of these guarantees because of their unusual nature and unique characteristics.

Off-balance-sheet credit and market risk

Williams is a participant in the following transactions and arrangements that involve financial instruments that have off-balance-sheet risk of accounting loss. It is not practicable to estimate the fair value of these off-balance-sheet financial instruments because of their unusual nature and unique characteristics.

Williams sold, with limited recourse, certain receivables. The aggregate limit under these receivables facilities was \$190 million at December 31, 1995, and \$80 million at December 31, 1994 (1994 balance all related to discontinued operations). Williams received \$196 million of proceeds in 1995, \$110 million in 1994 and none in 1993. At December 31, 1995 and 1994, \$166 million and \$80 million (1994 balance all related to discontinued operations) of such receivables had been sold, respectively. Based on amounts outstanding at December 31, 1995, the maximum contractual credit loss under these arrangements is approximately \$28 million, but the likelihood of loss is remote. Williams had no risk of credit loss for the amount sold at December 31, 1994, because amounts outstanding related to discontinued operations (see Note 3).

In connection with the sale of units in the Williams Coal Seam Gas Royalty Trust (Trust), Williams indemnified the Trust against losses from certain litigation (see Note 17) and guaranteed minimum gas prices through 1997. At December 31, 1995 and 1994, Williams has a recorded liability of \$10 million for these

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

items, representing the maximum amount for the first guarantee and an estimate of the gas price exposure based on historical operating trends and an assessment of market conditions. While Williams' maximum exposure from this guarantee exceeds amounts accrued, it is not practicable to determine such amount because of the unique aspects of the guarantee.

In connection with the sale of Williams' network services operations, Williams has been indemnified by LDDS against any losses related to retained guarantees of \$180 million at December 31, 1995, for lease rental obligations. LDDS has advised that it is negotiating with the guaranteed parties to remove Williams as guarantor.

Williams has issued other guarantees and letters of credit with off-balance-sheet risk that total approximately \$8 million and \$9 million at December 31, 1995 and 1994, respectively. Williams believes it will not have to perform under these agreements because the likelihood of default by the primary party is remote and/or because of certain indemnifications received from other third parties.

Commodity price-risk management services

Williams Energy Services provides price-risk management services associated with the energy industry to its customers. These services are provided through a variety of financial instruments, including forward contracts, futures contracts, option contracts, swap agreements and purchase and sale commitments. See Note 1 for a description of the accounting for these trading activities.

Williams Energy Services enters into forward contracts and purchase and sale commitments which involve physical delivery of an energy commodity. Prices under these contracts are both fixed and variable. Swap agreements call for Williams Energy Services to make payments to (or receive payments from) counterparties based upon the differential between a fixed and variable price or variable prices for different locations. The variable prices are generally based on either industry pricing publications or exchange quotations. Williams Energy Services buys and sells option contracts which give the buyer the right to exercise the options and receive the difference between a predetermined strike price and a market price at the date of exercise. The market prices used for natural-gas-related contracts are generally exchange quotations. Williams Energy Services also enters into futures contracts which are commitments to either purchase or sell a commodity at a future date for a specified price and are generally settled in cash, but may be settled through delivery of the underlying commodity. The market prices for futures contracts are based on exchange quotations.

Williams Energy Services manages risk from financial instruments by making various logistical commitments which manage profit margins through offsetting financial instruments. As a result, price movements can result in losses on certain contracts offset by gains on others.

Williams Energy Services takes an active role in managing and controlling market and counterparty risks and has established formal control procedures which are reviewed on an ongoing basis. Williams Energy Services attempts to minimize credit-risk exposure to trading counterparties and brokers through formal credit policies and monitoring procedures. In the normal course of business, collateral is not required for financial instruments with credit risk.

The notional quantities for all trading financial instruments at December 31, 1995, and December 31, 1994, are as follows:

*	19	195	1	994
	Payor	Receiver	Payor	Receiver
Fixed price:				
Natural gas (TBtu)	873.2	847.3	181.4	179.5
Refined products and crude (MMBbls)	15.9	14.9	11.2	12.5
Variable price:				
Natural gas (TBtu)	1,841.2	1,517.2	85.0	136.3
Refined products and crude (MMBbls)		2.5	2.5	2.5

The net cash flow requirement related to these contracts at December 31, 1995, was \$215 million. At December 31, 1995, the average remaining life of the trading fixed-price portfolio is approximately two years and four years for the trading variable-price portfolio.

In 1995, certain gas marketing operations of Williams Energy Services, along with gas marketing operations from Transco Energy, were combined with the commodity price-risk management and trading activities of Williams Energy Services. Such combination in 1995 involves managing the price and other business risks and opportunities of such physical gas trading activities and any related financial instruments previously accounted for as hedges in common-risk portfolios with Williams Energy Services' other financial instruments. These former marketing activities, consisting of buying and selling natural gas, through 1994 were reported on a "gross" basis in the Consolidated Statement of Income as revenues and profit-center costs. Concurrent with completing the combination of such activities with the commodity price-risk management operations in the third quarter of 1995, the related contract rights and obligations along with any related financial instruments previously accounted for as hedges, were recorded in the Consolidated Balance Sheet on a current-market-value basis and the related income statement presentation was changed to a net basis. Such revenues reported on a gross basis through the first two quarters of 1995 were reclassified to a net basis concurrent with this change in the third quarter of 1995. Following is a summary of Williams Energy Services' revenues:

	1995	1994
Financial instrument and physical trading market gains - net	\$ 65.8 617.7*	\$ 14.2
Gross marketing revenues	10.000.00	-47
Gross marketing costs	(599.2)*	-
Other		3
	\$ 85.8	\$263.7

Through June 30, 1995.

Concentration of credit risk

Williams' cash equivalents consist of high quality securities placed with various major financial institutions with high credit ratings. Williams' investment policy limits its credit exposure to any one financial institution.

At December 31, 1995 and 1994, approximately 62 percent and 40 percent, respectively, of receivables are for the sale or transportation of natural gas and related products or services. Approximately 27 percent and 30 percent of receivables at December 31, 1995 and 1994, respectively, are for telecommunications and related services. Natural gas customers include pipelines, distribution companies, producers, gas marketers and industrial users primarily located in the eastern, northwestern and midwestern United States. Telecommunica-

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

tions customers include numerous corporations. As a general policy, collateral is not required for receivables, but customers' financial condition and credit worthiness are evaluated regularly.

Note 16 - Other financial information

Intercompany revenues (at prices that generally apply to sales to unaffiliated parties) are as follows:

	1995	1994*	1993*
		(Millions)	-
Northwest Pipeline	\$ 1.8	\$ 3.4	\$ 3.6
Williams Natural Gas	9.5	14.2	5.4
Transcontinental Gas Pipe Line	34.2	-	-
Texas Gas Transmission	37.7	-	-
Williams Field Services Group	9.2	30.5	14.5
Williams Energy Services	34.0	20.2	42.1
Williams Pipe Line	32.8	16.7	1.4
Other	3	4	
	\$159.5	\$85.4	\$67.0

^{*} Reclassified as described in Note 1.

Williams Natural Gas had sales to a natural gas distributor that accounted for 15 percent in 1993 of Williams' revenues.

Information for business segments is as follows:

	_	1995	intrain	1lions)	_	993*
Identifiable assets at December 31:						
Northwest Pipeline	5	1,147.5	\$1	028.0	51	,032.6
Williams Natural Gas		709.2		719.8		697.0
Transcontinental Gas Pipe Line		3,159.5		-		-
Texas Gas Transmission		1,151.8				
Williams Field Services Group		2,116.5	1	093.6		967.8
Williams Energy Services		351.9		96.5		84.6
Williams Pipe Line		870.5		680.4		588.3
WilTel		263.0		255.5		169.1
WilTech Group		138.0		60.2		26.6
Investments		307.6		379.1		437.1
General corporate and other		279.3		169.4		122.1
Discontinued operations		-		743.6		895.2
Consolidated	\$1	0,494.8	\$5	,226.1	\$5	,020.4
Additions to property, plant and equipment:		1120.000		00000		
Northwest Pipeline	\$	130.5	5	62.6	S	175.7
Williams Natural Gas		43.5		32.9		54.9
Transcontinental Gas Pipe Line		238.7		-		-
Texas Gas Transmission		32.1		-0000		-
Williams Field Services Group		247.7		163.5		116.7
Williams Pipe Line		87.9		46.6		62.9
WilTel		24.1		4.9		1.9
WilTech Group		8.3		8.0		6.9
General corporate and other	-	14.7	-	7.0		9.3
Consolidated	5	827.5	5	325.5	5	428.3
Depreciation and depletion:						
Northwest Pipeline	5	34.9	5	33.9	5	30.7
Williams Natural Gas		27.3		27.2		27.3
Transcontinental Gas Pipe Line		109.1		-		-
Texas Gas Transmission		38.9				-
Williams Field Services Group		110.2		46.7		43.5
Williams Pipe Line		26.4		22.4		21.4
WilTel		5.9		5.3		4.7
WilTech Group		8.3		7.4		4.0
General corporate and other		8.4		7.4		6.2
Consolidated	5	369.4	\$	150.3	5	117.8

^{*} Reclassified as described in Note 1.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Note 17 - Contingent liabilities and commitments

Rate and regulatory matters and related litigation

Williams' interstate pipeline subsidiaries, including Williams Pipe Line, have various regulatory proceedings pending. As a result of rulings in certain of these proceedings, a portion of the revenues of these subsidiaries has been collected subject to refund. As to Williams Pipe Line, revenues collected subject to refund were \$179 million at December 31, 1995; it is not expected that the amount of any refunds ordered would be significant. Accordingly, no portion of these revenues has been reserved for refund. As to the other pipelines, see Note 12 for the amount of revenues reserved for potential refund as of December 31, 1995.

In 1992, the FERC issued Order 636, Order 636-A and Order 636-B. These orders, which have been challenged in various respects by various parties in proceedings pending in the U.S. Court of Appeals for the D.C. Circuit, require interstate gas pipeline companies to change the manner in which they provide services. Williams Natural Gas implemented its restructuring on October 1, 1993, and Northwest Pipeline, Texas Gas and Transcontinental Gas Pipe Line implemented their restructurings on November 1, 1993. Certain aspects of each pipeline company's restructuring are under appeal.

Contract reformations and gas purchase deficiencies

Each of the natural gas pipeline subsidiaries has undertaken the reformation of its respective gas supply contracts. None of the pipelines has any significant pending supplier take-or-pay, ratable take or minimum take claims.

In 1994, Williams Natural Gas and a producer executed a number of agreements to resolve outstanding issues. Portions of the settlement were subject to regulatory approvals, including the regulatory abandonment of a certain Williams Natural Gas gathering system on terms acceptable to Williams Natural Gas. On May 2, 1995, the FERC issued orders granting the requisite approvals; however, one party has requested rehearing of the decision regarding abandonment of the gathering system.

Current FERC policy associated with Orders 436 and 500 requires interstate gas pipelines to absorb some of the cost of reforming gas supply contracts before allowing any recovery through direct bill or surcharges to transportation as well as sales commodity rates. Under Orders 636, 636-A and 636-B, costs incurred to comply with these rules are permitted to be recovered in full, although 10 percent of such costs must be allocated to interruptible transportation service.

The FERC initially approved a method for Northwest Pipeline to direct bill its contract-reformation costs, but when challenged on appeal, sought a remand to reassess such method. Northwest Pipeline has received an order from the FERC that requires a different allocation of such costs and has rebilled its customers accordingly. While certain customers continue to challenge the FERC methodology, Northwest Pipeline does not expect the reallocation or the challenge to result in a significant financial impact upon the company.

Pursuant to a stipulation and agreement approved by the FERC, Williams Natural Gas has made three filings to direct bill take-or-pay and gas supply realignment costs. The first provided for the offset of certain amounts collected subject to refund against previous take-or-pay direct-billed amounts and, in addition, covered \$24 million in new costs. This filing was approved, and the final direct-billed amount, taking into consideration the offset, was \$15 million. The second filing covered \$18 million in additional costs, and provided for an offset of \$3 million. The third filing covered additional costs of \$8 million which are similar in nature to the costs in the second filing. An intervenor has filed a protest seeking to have the Commission review the prudence of certain of the costs covered by the second and third filings. Williams Natural Gas believes that the second and third filings will most likely be approved. As of December 31, 1995, this subsidiary had an accrual of \$87 million for its then estimated remaining contract-reformation and gas supply

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

realignment costs. This accrual was increased in December 1995 as a result of a ruling by the U.S. Court of Appeals for the Tenth Circuit regarding the terms of certain contracts with producers. Williams Natural Gas will make additional filings under the applicable FERC orders to recover such further costs as may be incurred in the future. Williams Natural Gas has recorded a regulatory asset of approximately \$84 million for estimated future recovery of the foregoing costs.

On September 18, 1995, Texas Gas received FERC approval of a settlement regarding Texas Gas' recovery of gas supply realignment costs. The settlement provides that Texas Gas will recover 100 percent of such costs up to \$50 million, will share in costs incurred between \$50 million and \$80 million, and will absorb any such costs above \$80 million. The settlement also extends Texas Gas' pricing differential mechanism to November 1, 1996, and beyond that date for contracts in litigation as of that date. Through December 31, 1995, Texas Gas has paid approximately \$53 million for gas supply realignment costs, primarily as a result of contract terminations, and has accrued a liability of approximately \$27 million for its estimated remaining gas supply realignment costs. Texas Gas has recovered approximately \$44 million in gas supply realignment costs, and in accordance with the terms of its settlement has recorded a regulatory asset of approximately \$23 million for the estimated future recovery of such costs, which will be collected from customers over the next two years. Ninety percent of the cost recovery is collected through demand surcharges on Texas Gas' firm transportation rates; the remaining 10 percent is recoverable from interruptible transportation service.

In 1983, the FERC issued Order 94-A, which permitted producers to collect certain production related costs from pipelines on a retroactive basis. Pursuant to FERC orders, Texas Gas and Transcontinental Gas Pipe Line direct billed their customers for such costs paid to producers. In 1990, the U.S. Court of Appeals for the D.C. Circuit overturned the FERC's orders authorizing direct billing for such costs. In December 1995, Texas Gas entered into a settlement by which it resolved its final refund obligations as to these costs. Transcontinental Gas Pipe Line has resolved its refund obligations except for an amount of approximately \$7 million. Transcontinental Gas Pipe Line has refunded that amount, reserving the right to recover the amount paid if the ruling is reversed on appeal.

The foregoing accruals are in accordance with Williams' accounting policies regarding the establishment of such accruals which take into consideration estimated total exposure, as discounted and risk-weighted, as well as costs and other risks associated with the difference between the time costs are incurred and the time such costs are recovered from customers. The estimated portion of such costs recoverable from customers is deferred or recorded as a regulatory asset based on an estimate of expected recovery of the amounts allowed by FERC policy. While Williams believes that these accruals are adequate and the associated regulatory assets are appropriate, costs actually incurred and amounts actually recovered from customers will depend upon the outcome of various court and FERC proceedings, the success of settlement negotiations and various other factors, not all of which are presently foreseeable.

Environmental matters

Since 1989, Texas Gas and Transcontinental Gas Pipe Line have had studies underway to test certain of their facilities for the presence of toxic and hazardous substances to determine to what extent, if any, remediation may be necessary. Transcontinental Gas Pipe Line has responded to data requests regarding such potential contamination of certain of its sites. The costs of any such remediation will depend upon the scope of the remediation. At December 31, 1995, these subsidiaries had reserves totaling approximately \$45 million for these costs.

Certain Williams subsidiaries, including Texas Gas and Transcontinental Gas Pipe Line, have been identified as potentially responsible parties (PRP) at various Superfund and state waste disposal sites. Although no assurances can be given, Williams does not believe that the PRP status of these subsidiaries will have a material adverse effect on its financial position, results of operations or net cash flows.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

In February 1995, Transcontinental Gas Pipe Line was served as a defendant in a lawsuit filed in U.S. District Court in Virginia by three individuals for alleged violations of several provisions of both federal and state laws. Since 1991, Transcontinental Gas Pipe Line has worked with the appropriate Virginia authorities to resolve certain emissions issues also raised by the individuals. On October 13, 1995, the court dismissed the lawsuit but provided that the plaintiffs could amend and refile their complaint to allege a state law nuisance claim and they have done so. Transcontinental Gas Pipe Line believes the amended complaint is without merit and is prepared to vigorously defend the suit.

Transcontinental Gas Pipe Line, Texas Gas and Williams Natural Gas have identified polychlorinated biphenyl (PCB) contamination in air compressor systems, soils and related properties at certain compressor station sites. Transcontinental Gas Pipe Line, Texas Gas and Williams Natural Gas have also been involved in negotiations with the U.S. Environmental Protection Agency (EPA) and state agencies to develop screening, sampling and cleanup programs. In addition, negotiations concerning investigative and remedial actions relative to potential mercury contamination at certain gas metering sites have commenced with certain environmental authorities by Williams Natural Gas and Transcontinental Gas Pipe Line. As of December 31, 1995, Williams Natural Gas had recorded a liability for approximately \$26 million, representing the current estimate of future environmental cleanup costs to be incurred over the next six to ten years. Texas Gas and Transcontinental Gas Pipe Line likewise had recorded liabilities for these costs which are included in the \$45 million reserve mentioned above. Actual costs incurred will depend on the actual number of contaminated sites identified, the actual amount and extent of contamination discovered, the final cleanup standards mandated by the EPA and other governmen all authorities and other factors. Texas Gas, Transcontinental Gas Pipe Line and Williams Natural Gas have deferred these costs pending recovery as incurred through future rates and other means.

In connection with the 1987 sale of the assets of Agrico Chemical Company, Williams agreed to indemnify the purchaser for environmental cleanup costs resulting from certain conditions at specified locations, to the extent such costs exceed a specified amount. It appears probable that such costs will exceed this amount. At December 31, 1995, Williams had approximately \$7 million accrued for such excess costs. The actual costs incurred will depend on the actual amount and extent of contamination discovered, the final cleanup standards mandated by the EPA or other governmental authorities, and other factors.

A lawsuit was filed on May 14, 1993, in a state court in Colorado in which certain claims have been made against various defendants, including Northwest Pipeline, contending that gas exploration and development activities in portions of the San Juan Basin have caused air, water and other contamination. The plaintiffs in the case sought certification of a plaintiff class. On June 28, 1994, the lawsuit was dismissed for failure to join an indispensable party over which the state court had no jurisdiction. This decision is being appealed by the plaintiffs. Since June 28, 1994, eight individual lawsuits have been filed against Northwest Pipeline in U.S. District Court in Colorado, making essentially the same claims. Northwest Pipeline is vigorously defending these lawsuits.

Other legal matters

On December 31, 1991, the Southern Ute Indian Tribe (the Tribe) filed a lawsuit against Williams Production Company, a wholly owned subsidiary of Williams, and other gas producers in the San Juan Basin area, alleging that certain coal strata were reserved by the United States for the benefit of the Tribe and that the extraction of coal-seam gas from the coal strata was wrongful. The Tribe seeks compensation for the value of the coal-seam gas. The Tribe also seeks an order transferring to the Tribe ownership of all of the defendants' equipment and facilities utilized in the extraction of the coal-seam gas. On September 13, 1994, the court granted summary judgment in favor of the defendants. The Tribe lodged an interlocutory appeal with the U.S. Court of Appeals for the Tenth Circuit. Williams Production agreed to indemnify the Williams Coal Seam Gas Royalty Trust (Trust) against any losses that may arise in respect of certain properties subject to

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

the lawsuit. In addition, if the Tribe is successful in showing that Williams Production has no rights in the coal-seam gas, Williams Production has agreed to pay to the Trust for distribution to then-current unitholders, an amount representing a return of a portion of the original purchase price paid for the units. While Williams believes that such a payment is not probable, it has reserved a portion of the proceeds from the sale of the units in the Trust.

In October 1990, Dakota Gasification Company (Dakota), the owner of the Great Plains Coal Gasification Plant (Plant), filed suit in the U.S. District Court in North Dakota against Transcontinental Gas Pipe Line and three other pipeline companies alleging that the pipeline companies had not complied with their respective obligations under certain gas purchase and gas transportation contracts. On September 8, 1992, Dakota and the Department of Justice on behalf of the Department of Energy filed an amended complaint adding as defendants in the suit, Transco Energy Company, Transco Coal Gas Company (Transco Energy Company and Transco Coal Gas Company being wholly owned subsidiaries of Williams) and all of the other partners in the partnership that originally constructed the Plant and each of the parent companies of these entities. Dakota and the Department of Justice sought declaratory and injunctive relief and the recovery of damages, alleging that the four pipeline defendants underpaid for gas, collectively, as of June 30, 1992, by more than \$232 million plus interest and for additional damages for transportation services and costs and expenses including attorneys' fees. On March 30, 1994, the parties executed definitive agreements which would settle the litigation subject to final non-appealable regulatory approvals. The settlement is also subject to a FERC ruling that Transcontinental Gas Fipe Line's existing authority to recover in rates certain costs related to the purchase and transportation of gas produced by Dakota will pertain to gas purchase and transportation costs Transcontinental Gas Pipe Line will pay Dakota under the terms of the settlement. On October 18, 1994, the FERC issued an order consolidating Transcontinental Gas Pipe Line's petition for approval of the settlement with similar petitions pending relative to two of the other three pipeline companies (the third pipeline having entered into a settlement) and setting the matter for hearing before an administrative law judge. On December 29, 1995, the administrative law judge issued an initial decision in which he concluded that the settlement was imprudent. If the decision is upheld on appeal, Transcontinental Gas Pipe Line and the other two pipelines would be required to refund to their customers amounts collected in excess of the amounts deemed appropriate by the administrative law judge. The pipelines would be entitled to collect the amount of any such customer refunds from Dakota. The administrative law judge's decision will be appealed; however, in the event that the necessary regulatory approvals are not ultimately obtained and Dakota elects to continue the litigation, Transcontinental Gas Pipe Line, Transco Energy Company and Transco Coal Gas Company intend to vigorously defend the suit.

In connection with agreements to resolve take-or-pay and other contract claims and to amend gas purchase contracts, Transcontinental Gas Pipe Line and Texas Gas each entered into certain settlements with producers which may require the indemnification of certain claims for additional royalties which the producers may be required to pay as a result of such settlements. As a result of such settlements, Transcontinental Gas Pipe Line and Texas Gas have been named as defendants in, respectively, six and two lawsuits in which damages claimed aggregate in excess of \$133 million. Texas Gas has settled its two lawsuits for a total cost of \$3.7 million, all but \$700,000 of which is recoverable as transition costs under Order 636. On July 17, 1995, a judge in a Texas state court granted a motion by Transcontinental Gas Pipe Line for partial summary judgment, rejecting a major portion of the plaintiff's claims in one of its lawsuits. Producers may receive other demands which could result in additional claims. Indemnification for royalties will depend on, among other things, the specific lease provisions between the producer and the lessor and the terms of the settlement between the producer and either Transcontinental Gas Pipe Line or Texas Gas. Texas Gas may file to recover 75 percent of any such additional amounts it may be required to pay pursuant to indemnities for royalties under the provisions of Order 528.

THE WILLIAMS COMPANIES, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Concluded)

On November 14, 1994, Continental Energy Associates Limited Partnership (the Partnership) filed a voluntary petition under Chapter 11 of the Bankruptcy Code with the U.S. Bankruptcy Court, Middle District of Pennsylvania. The Partnership owns a cogeneration facility in Hazleton, Pennsylvania (the Facility). Hazleton Fuel Management Company (HFMC), a subsidiary of Transco Energy, supplies natural gas and fuel oil to the Facility. As of December 31, 1995, it had current outstanding receivables from the Partnership of approximately \$20 million, all of which has been reserved. The construction of the Facility was funded by several banks that have a security interest in all of the Partnership's assets. HFMC has asserted to the Bankruptcy Court that payment of its receivables is superior to the lien of the banks and intends to vigorously pursue the collection of such amounts. HFMC has also filed suit against the lead bank with respect to this and other matters, including the alleged tortious interference with HFMC's contractual relations with the Partnership and other parties. On March 21, 1995, the Bankruptcy Court approved the rejection of the gas supply contract between the Partnership and HFMC. HFMC has in turn asserted force majeure under a contract with a producer under which HFMC purchased natural gas for the Facility.

In addition to the foregoing, various other proceedings are pending against Williams or its subsidiaries incidental to their operations.

Summary

While no assurances may be given, Williams does not believe that the ultimate resolution of the foregoing matters, taken as a whole and after consideration of amounts accrued, insurance coverage, recovery from customers or other indemnification arrangements, will have a materially adverse effect upon Williams' future financial position, results of operations and cash flow requirements.

THE WILLIAMS COMPANIES, INC. QUARTERLY FINANCIAL DATA (Unaudited)

Summarized quarterly financial data are as follows (millions, except per-share amounts). Revenues and costs and operating expenses for the six months ended June 30, 1995, have been reclassified to report natural gas sales net of related gas purchase costs.

1995	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenues	\$ 642.4	\$663.9	\$712.4	\$837.0
Costs and operating expenses	351.1	400.1	438.9	510.6
Net income	1,088.9	83.3	68.5	77.5
Primary earnings per common and common-equivalent				
share	11.57	.79	.58	.70
Fully diluted earnings per common and common-				
equivalent share	11.55	.78	.58	.69
1994				
Revenues	\$ 386.6	\$419.9	\$467.3	\$477.3
Costs and operating expenses	248.5	274.0	335.4	329.8
Income before extraordinary loss	52.8	74.0	55.6	76.5
Net income	52.8	62.9	55.6	75.4
Primary earnings per common and common-equivalent share:				
Income before extraordinary loss	.48	.69	.51	.77
Net income	.48	.58	.51	.76
Fully diluted earnings per common and common- equivalent share:				
Income before extraordinary loss	.48	.69	.51	.77
Net income	.48	.58	.51	.76

The sum of earnings per share for the four quarters may not equal the total earnings per share for the year due to changes in the average number of common shares outstanding.

First-quarter 1995 net income includes the after-tax gain of \$1 billion on the sale of Williams' network services operations (see Note 3 of Notes to Consolidated Financial Statements). The second quarter of 1995 includes a \$16 million after-tax gain from the sale of Williams' 15 percent interest in Texasgulf Inc. (see Note 5 of Notes to Consolidated Financial Statements) and an \$8 million income tax benefit resulting from settlements with taxing authorities. Northwest Pipeline's third-quarter 1995 operating profit includes the approximate \$11 million net favorable effect of two reserve accrual adjustments. In third-quarter 1995, Williams Field Services Group recorded \$20 million of income from the favorable resolution of contingency issues involving previously regulated gathering and processing assets, partially offset by an \$8 million accrual for a future minimum price natural gas purchase commitment.

Second-quarter 1994 includes a \$23 million gain from the sale of assets (see Note 6 of Notes to Consolidated Financial Statements).

QUARTERLY FINANCIAL DATA (Unaudited) (Concluded)

Selected comparative fourth-quarter data are as follows (millions, except per-share amounts). Certain 1994 amounts have been restated as described in Note 1 of Notes to Consolidated Financial Statements.

	1995	1994
Operating profit (loss):		
Williams Interstate Natural Gas Systems:		
Northwest Pipeline	\$ 25.1	\$ 22.7
Williams Natural Gas	15.5	15.1
Transcontinental Gas Pipe Line	47.4	-
Texas Gas Transmission	28.6	-
Williams Field Services Group	43.2	40.4
Williams Energy Services	.3	(3.9)
Williams Pipe Line	19.3	11.9
WilTel	7.2	6.7
WilTech Group	.8	(4.5)
Other	(.2)	
Total operating profit	187.2	88.4
General corporate expenses	(12.1)	(7.0)
Interest expense — net	(69.7)	(39.1)
Investing income	12.7	10.8
Write-off of project costs	(41.4)	-
Other income (expense) — net	5.2	(2.5)
Income from continuing operations before income taxes	81.9	50.6
Provision for income taxes	17.5	16.4
Income from continuing operations	64.4	34.2
Income from discontinued operations	13.1	42.3
Income before extraordinary loss	77.5	76.5
Extraordinary loss		(1.1)
Net income	\$ 77.5	\$ 75.4
Primary earnings per common and common-equivalent share	\$.70	\$.76
Fully diluted earnings per common and common-equivalent share	\$.69	\$.76

Williams Energy Services' fourth-quarter 1995 operating profit includes loss accruals of approximately \$6 million, primarily related to contract disputes. In fourth-quarter 1995, the development of a commercial coal gasification venture in south-central Wyoming was canceled, resulting in a \$41.4 million pre-tax charge (see Note 6 of Notes to Consolidated Financial Statements). Fourth-quarter 1995 income from discontinued operations reflects the after-tax effect of the reversal of accruals established at the time of the sale of the network services operations (see Note 3 of Notes to Consolidated Financial Statements).

In fourth-quarter 1994, Williams Natural Gas recorded a \$7 million reversal of excess contractreformation accruals. Williams Pipe Line's fourth-quarter 1994 operating profit includes \$5 million in costs for evaluating and determining whether to build an oil refinery. Fourth-quarter 1994 discontinued operations includes favorable adjustments of approximately \$15 million relating to bad debt recoveries and accrual reversals.

Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure

None.

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All other schedules have been omitted since the required information is not present or is not present in amounts sufficient to require submission of the schedule, or because the information required is included in the financial statements and notes thereto.

SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF REGISTRANT STATEMENT OF INCOME (PARENT)

	Years ended December 31,		
	1905	1994	1993
	(Millions, e	imounts)	
Investing income	\$ 50.7	\$ 29.4	\$ 27.3
Interest accrued	(189.9)	(91.8)	(95.8)
Gain on sales of assets (Note 3)	21/03/25/03/03	-	51.6
Other income (expense) — net	(12.9)	2.9	(16.9)
Loss from continuing operations before income taxes and equity in			
subsidiaries' income	(152.1)	(59.5)	(33.8)
Equity in consolidated subsidiaries' income	376.5	195.0	189.8
Income from continuing operations before income taxes	224.4	135.5	156.0
Credit for income taxes	(75.0)	(29.4)	(29.4
Income from continuing operations	299.4	164.9	185.4
Income from discontinued operations (Note 2)	1,018.8	94.0	46.4
Income before extraordinary loss	1,318.2	258.9	231.8
Extraordinary loss from early extinguishment of debt		(12.2)	
Net income	1,318.2	246.7	231.8
Preferred stock dividends	15.3	8.8	11.8
Income applicable to common stock	\$1,302.9	\$237.9	\$220.0
Primary earnings per common and common-equivalent share:			
Income from continuing operations	\$ 2.78	\$ 1.52	\$ 1.74
Income from discontinued operations	9.99	.92	46
Income before extraordinary loss	12.77	2.44	2.20
Extraordinary loss	-	_(.12)	
Net income	\$ 12.77	\$ 2.32	\$ 2.20
Fully diluted earnings per common and common-equivalent share:			
Income from continuing operations	\$ 2.76	\$ 1.52	\$ 1.71
Income from discontinued operations	9.72	92	45
Income before extraordinary loss	12.48	2.44	2.16
Extraordinary loss		(.12)	
Net income	\$ 12.48	\$ 2.32	\$ 2.16

See accompanying notes.

SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF REGISTRANT — (Continued) BALANCE SHEET (PARENT)

ASSETS

	Decem	ber 31,
	1995	1994
C	(Mil	lions)
Current assets: Cash and cash equivalents	\$ 57.6	S 16.5
Due from consolidated subsidiaries	131.6	138.4
Receivables	28.9	65.3
Investment in discontinued operations (Note 2)		743.6
Other	15.0	4.9
Total current assets	233.1	968.7
Investments:	233.1	300.7
Equity in consolidated subsidiaries (Note 1)	5,551.4	1,634.8
Receivables from consolidated subsidiaries	68.7	387.8
Trees and the state of the stat	5,620.1	2.022.6
Other	5,020.1	44.0
Other	-	-
Darward and the state of the st	5,620.1 20.6	2,066.6 36.3
Property, plant and equipment—net Other assets and deferred charges	23.9	14.8
-		
Total assets	\$5,897.7	\$3,086.4
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable	s -	\$ 73.8
Due to consolidated subsidiaries	291.9	137.6
Accounts payable and accrued liabilities	100.2	84.1
Long-term debt due within one year (Note 4)	20.0	361.5
Total current liabilities	412.1	657.0
Long-term debt (Note 4)	1,460.0	763.0
Long-term debt due to consolidated subsidiary (Note 4)	360.0	-
Due to consolidated subsidiaries	440.5	-
Other liabilities	38.0	160.9
Stockholders' equity:		
Preferred stock	173.5	100.0
Common stock	105.3	104.4
Capital in excess of par value	1,051.1	991.0
Retained earnings	1,915.6	716.5
Unamortized deferred compensation	(2.3)	(1.3)
0 V0000 10 V000	3,243.2	1,910.6
Less treasury stock (Notes 4 and 5)	(56.1)	(405.1)
Total stockholders' equity	3,187.1	1,505.5
Total liabilities and stockholders' equity	\$5,897.7	\$3,086.4

See accompanying notes.

SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF REGISTRANT — (Continued) STATEMENT OF CASH FLOWS (PARENT)

	Year	s ended December 3	1.
	1995	(Millions)	1993
Operating activities:		(Hillions)	
Net income	\$ 1,318.2	\$ 246.7	\$ 231.8
Adjustments to reconcile to cash provided from operations:			
Equity in subsidiaries' income, net of cash dividends	732.7	153.1	(60.0)
Discontinued operations	(1,018.8)	(94.0)	(46.4)
Extraordinary loss		12.2	-
Depreciation	4.2	4.3	4.2
Provision (credit) for deferred income taxes	13.0	20.8	(1.7)
Gain on sales of property, plant and equipment		-	(52.1)
Changes in receivables	33.3	(59.5)	5.0
Changes in other current assets	5.0	(7.1)	1.4
Changes in accounts payable	(2.7)	3.0	(.7)
Changes in accrued liabilities	(.2)	(12.1)	(18.7)
Other, including changes in non-current assets and		322 57.0	100
liabilities	(7.2)	(2.5)*	58.5
Net cash provided by operating activities	1,077.5	264.9	121.3
Financing activities:			
Proceeds from notes payable	53.4	73.8	
Payments of notes payable	(127.2)		-
Proceeds from long-term debt	85.0	350.0	_
Payments of long-term debt	(549.2)	(181.7)	(128.8)
Proceeds from issuance of common stock	32.0	26.4	63.4
Purchase of treasury stock	(3.7)	(18.4)	-
Dividends paid	(119.0)	(93.9)	(89.4)
Other — net	(3.7)	(*****	(.6)
	-	156.2*	(155.4)
Net cash provided (used) by financing activities	(632.4)	130.2	(133.4)
Investing activities:			
Property, plant and equipment:	(2.0)	(1.11	11.6
Capital expenditures	(2.8)	(1.1)	(1.6)
Proceeds from sales of property, plant and equipment	1.0		115.1
Purchase of note receivable	(75.1)	(71.2)	C 24 C 577 C
Investments in consolidated subsidiaries	(1,248.1)	(71.2)	(75.3)
Changes in advances to subsidiaries	914.7	(354.4)	1.0
Other — net	6.3	(4.0)	(.6)
Net cash provided (used) by investing activities	(404.0)	(430.7)	38.6
Increase (decrease) in cash and cash equivalents	41.1	(9.6)	4.5
Cash and cash equivalents at beginning of year	16.5	26.1	21.6
Cash and cash equivalents at end of year	\$ 57.6	\$ 16.5	\$ 26.1

See accompanying notes.

^{*} Reclassified to conform to current classification.

SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF REGISTRANT — (Continued) NOTES TO FINANCIAL INFORMATION (PARENT)

Note 1. Transco Energy Acquisition

On January 18, 1995, Williams acquired 60 percent of Transco Energy's outstanding common stock in a cash tender offer for \$430.5 million. Williams acquired the remaining 40 percent of Transco Energy's outstanding common stock on May 1, 1995, through a merger by exchanging the remaining Transco Energy common stock for approximately 10.4 million shares of Williams common stock valued at \$334 million. The acquisition is accounted for as a purchase with 60 percent of Transco Energy's results of operations included in Williams' Consolidated Statement of Income for the period January 18, 1995, through April 30, 1995, and 100 percent included beginning May 1, 1955. See Note 2 of Notes to Consolidated Financial Statements for additional information on the Transco Energy acquisition.

Note 2. Discontinued Operations

On January 5, 1995, Williams sold its network services operations to LDDS Communications, Inc. (LDDS) for \$2.5 billion in cash. The sale yielded a gain of \$1 billion (net of income taxes of approximately \$732 million) which is reported as income from discontinued operations. Prior period operating results for the network services operations are reported as discontinued operations. See Note 3 of Notes to Consolidated Financial Statements for additional information on discontinued operations.

Note 3. Sales of Assets

In a 1993 public offering, Williams sold 6.1 million units in the Williams Coal Seam Gas Royalty Trust (Trust), which resulted in net proceeds of \$113 million and a pre-tax gain of \$51.6 million. The Trust owns defined net profits interests in the developed coal-seam properties in the San Juan Basin of New Mexico and Colorado, which were conveyed to the Trust by Williams Production Company. Ownership of an additional 3.6 million units remains with a subsidiary of Williams.

Note 4. Long-term Debt and Leases

During 1995, Williams issued \$360 million in convertible debentures and warrants to a wholly-owned subsidiary in exchange for 12.2 million shares of Williams common stock held by that subsidiary (see Note 5). The convertible debentures bear interest at 6 percent, mature in 2005 and are convertible into 9.3 million shares of Williams common stock at \$38.58 per share. The warrants give the subsidiary the right to purchase 7.5 million shares of Williams common stock at \$46.67 per share.

Long-term debt due within one year at December 31, 1994 includes \$350 million of borrowings under Williams' credit agreement. Amounts were repaid in January 1995.

Aggregate minimum maturities and sinking-fund requirements, excluding lease payments, for each of the next five years are as follows: 1996 — \$20 million; 1997 — none; 1998 — \$310 million; 1999 — \$150 million; and 2000 — \$175 million. See Note 13 of Notes to Consolidated Financial Statements for additional information on long-term debt.

Note 5. Stockholders' Equity

In connection with the May 1, 1995, merger with Transco Energy, Williams exchanged all of Transco Energy's outstanding \$3.50 cumulative convertible preferred stock for 2.5 million shares of Williams' \$3.50 cumulative convertible preferred stock. See Note 14 of Notes to Consolidated Financial Statements for additional information on this exchange.

SCHEDULE I — CONDENSED FINANCIAL INFORMATION OF REGISTRANT — (Concluded) NOTES TO FINANCIAL INFORMATION (PARENT)

During 1995, Williams exchanged 2.8 million shares of its \$2.21 cumulative preferred stock with a carrying value of \$69 million for 9.6 percent debentures. See Note 14 of Notes to Consolidated Financial Statements for additional information on this exchange.

For financial reporting purposes, treasury stock of \$394.8 million held at December 31, 1994, by a whollyowned subsidiary of Williams has been presented as a reduction of stockholders' equity. A portion of this treasury stock was used in the acquisition of Transco Energy (see Note 1).

The Financial Accounting Standards Board has issued a new accounting standard, FAS No. 123, "Accounting for Stock-Based Compensation," effective for fiscal years beginning after December 15, 1995. As provided for in the standard, Williams will not adopt the recognition provisions and will provide the pro forma net income and earnings-per-share disclosures required by the standard in its 1996 annual financial statements.

Williams currently follows Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees." Under this standard, because the exercise price of Williams' fixed plan common stock options equals the market price of the underlying stock on the date of the grant, no compensation expense is recognized.

Note 6. Dividends Received

Cash dividends from subsidiaries and companies accounted for on an equity basis are as follows: 1995 — \$1,110.2 million; 1994 — \$354.2 million; and 1993 — \$142.6 million.

Note 7. Income Tax and Interest Payments

Cash payments for income taxes are as follows: 1995 — \$326 million; 1994 — \$112 million; and 1993 — \$118 million.

Cash payments for interest are as follows: 1995 — \$127.9 million; 1994 — \$90 million; and 1993 — \$96.6 million.

Note 8. Financial Instruments

Disclosure of financial instruments for the parent company are included in the consolidated disclosures. See Note 15 of Notes to Consolidated Financial Statements.

THE WILLIAMS COMPANIES, INC. SCHEDULE II — VALUATION AND QUALIFYING ACCOUNTS(a)

		Additio	0.5		
	Beginning Balance	Charged to Costs and Expenses	Other (Millions)	Deductions(b)	Ending Balance
Allowance for doubtful accounts:					
1995	\$ 7.9	\$3.8	\$1.6(c)	\$2.0	\$11.3
1994	10.2	4.2(d)	_	6.5(c)	7.9
1993	17.3	.5(f)	-	7.6	10.2

- (a) Deducted from related assets.
- (b) Represents balances written off, net of recoveries and reclassifications.
- (c) Relates primarily to acquisition of businesses.
- (d) Excludes \$5.7 million related to discontinued operations.
- (e) Includes the discontinued operations beginning balance reclassification of \$3.6 million.
- (f) Includes \$4.1 million reversal of amounts previously accrued.

PART III

Item 10. Directors and Executive Officers of the Registrant

The information regarding the Directors and nominees for Director of Williams required by Item 401 of Regulation S-K is presented under the heading "Election of Directors" in Williams' Proxy Statement prepared for the solicitation of proxies in connection with the Annual Meeting of Stockholders of the Company for 1996 (the "Proxy Statement"), which information is incorporated by reference herein. A copy of the Proxy Statement is filed as an exhibit to the Form 10-K. Information regarding the executive officers of Williams is presented following Item 4 herein, as permitted by General Instruction G(3) to Form 10-K and Instruction 3 to Item 401(b) of Regulation S-K. Information required by Item 405 of Regulation S-K is included under the heading "Compliance with Section 16(a) of the Securities Exchange Act of 1934" in the Proxy Statement, which information is incorporated by reference herein.

Item 11. Executive Compensation

The information required by Item 402 of Regulation S-K regarding executive compensation is presented under the headings "Election of Directors" and "Executive Compensation and Other Information" in the Proxy Statement, which information is incorporated by reference herein. Notwithstanding the foregoing, the information provided under the headings "Compensation Committee Report on Executive Compensation" and "Stockholder Return Performance Presentation" in the Proxy Statement are not incorporated by reference herein. A copy of the Proxy Statement is filed as an exhibit to the Form 10-K.

Item 12. Security Ownership of Certain Beneficial Owners and Management

The information regarding the security ownership of certain beneficial owners and management required by Item 403 of Regulation S-K is presented under the headings "Security Ownership of Certain Beneficial Owners and Management" in the Proxy Statement, which information is incorporated by reference herein. A copy of the Proxy Statement is filed as an exhibit to the Form 10-K.

Item 13. Certain Relationships and Related Transactions

There is no information regarding certain relationships and related transactions required by Item 404 of Regulation S-K to be reported in response to this Item.

PART IV

Item 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K

- (a) 1 and 2. The financial statements and schedules listed in the accompanying index to consolidated financial statements are filed as part of this annual report.
 - (a) 3 and (c). The exhibits listed below are filed as part of this annual report.

Exhibit 2 -

- *(a) Agreement and Plan of Merger, dated as of December 12, 1994, among Williams, WC Acquisition Corp. and Transco (filed as Exhibit (c)(1) to Schedule 14D-1, dated December 16, 1994).
- *(b) Amendment to Agreement and Plan of Merger, dated as of February 17, 1995 (filed as Exhibit 6 to Amendment No. 8 to Schedule 13D, dated February 23, 1995).

Exhibit 3 -

*(a) Restated Certificate of Incorporation of Williams (filed as Exhibit 4(a) to Form 8-B Registration Statement, filed August 20, 1987).

- *(b) Certificate of Designation with respect to the \$2.21 Cumulative Preferred Stock (filed as Exhibit 4.3 to the Registration Statement on Form S-3, filed August 19, 1992).
- *(c) Certificate of Increase of Authorized Number of Shares of Series A Junior Participating Preferred Stock (filed as Exhibit 3(c) to Form 10-K for the year ended December 31, 1988).
- *(d) Certificate of Amendment of Restated Certificate of Incorporation, dated May 20, 1994 (filed as Exhibit 3(d) to Form 10-K for the fiscal year ended December 31, 1994).
- *(e) Certificate of Designation with respect to the \$3.50 Cumulative Convertible Preferred Stock (filed as Exhibit 3.1(c) to the Prospectus and Information Statement to Amendment No. 2 to the Registration Statement on Form S-4, filed March 30, 1995).
- (f) Certificate of Increase of Authorized Number of Shares of Series A Junior Participating Preferred Stock.
- *(g) Rights Agreement, dated as of February 6, 1996, between Williams and First Chicago Trust Company of New York (filed as Exhibit 4 to Williams Form 8-K, filed January 24, 1996).
- (h) By-laws of Williams (filed as Exhibit 3 to Form 10-Q for the quarter ended September 30, 1993).

Exhibit 4 -

- *(a) Form of Senior Debt Indenture between the Company and Chemical Bank, Trustee, relating to the 104% Debentures, due 2020; the 9½% Debentures, due 2021; the 8½% Notes, due 1998; Medium-Term Notes (8.50%-9.31%), due 1996 through 2001; the 7½% Notes, due 1999, and the 8½% Debentures, due 2012 (filed as Exhibit 4.1 to Form S-3 Registration Statement No. 33-33294, filed February 2, 1990).
- (b) U.S. \$800,000,000 Credit Agreement, dated as of February 23, 1995, among Williams and certain of its subsidiaries and the banks named therein and Citibank, N.A., as agent (filed as Exhibit 4(b) to Form 10-K for the fiscal year ended December 31, 1994).

Exhibit 10(iii) - Compensatory Plans and Management Contracts

- (a) The Williams Companies, Inc. Supplemental Retirement Plan, effective as of January 1,
 1988 (filed as Exhibit 10(iii)(c) to Form 10-K for the year ended December 31, 1987).
- (b) Form of Employment Agreement, dated January 1, 1990, between Williams and certain executive officers (filed as Exhibit 10(iii) (d) to Form 10-K for the year ended December 31, 1989).
- *(c) Form of The Williams Companies, Inc. Change in Control Protection Plan between Williams and employees (filed as Exhibit 10(iii) (e) to Form 10-K for the year ended December 31, 1989).
- *(d) The Williams Companies, Inc. 1985 Stock Option Plan (filed as Exhibit A to Williams' Proxy Statement, dated March 13, 1985).
- *(e) The Williams Companies, Inc. 1988 Stock Option Plan for Non-Employee Directors (filed as Exhibit A to Williams' Proxy Statement, dated March 14, 1988).
- *(f) The Williams Companies, Inc. 1990 Stock Plan (filed as Exhibit A to Williams' Proxy Statement, dated March 12, 1990).
 - (g) The Williams Companies, Inc. Stock Plan for Non-Officer Employees.
- *(h) The Williams Companies, Inc. 1996 Stock Plan (filed as Exhibit A to Williams' Proxy Statement, dated March 27, 1996).
- *(i) The Williams Companies, Inc. 1996 Stock Plan for Non-Employee Directors (filed as Exhibit B to Williams' Proxy Statement, dated March 27, 1996).

- *(j) Indemnification Agreement, effective as of August 1, 1986, between Williams and members of the Board of Directors and certain officers of Williams (filed as Exhibit 10(iii)(e) to Form 10-K for the year ended December 31, 1986).
- Exhibit 11 Computation of Earnings Per Common and Common-equivalent Share.
- Exhibit 12 Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividend Requirements.
- Exhibit 20 Definitive Proxy Statement of Williams for 1996.
- Exhibit 21 Subsidiaries of the registrant.
- Exhibit 23 Consent of Independent Auditors.
- Exhibit 24 Power of Attorney together with certified resolution.
- Exhibit 27 Financial Data Schedule.
- (b) Reports on Form 8-K.

No reports on Form 8-K were filed by Williams with the Securities and Exchange Commission during the fourth quarter of 1995.

- (d) The financial statements of partially-owned companies are not presented herein since none of them individually, or in the aggregate, constitute a significant subsidiary.
- Each such exhibit has heretofore been filed with the Securities and Exchange Commission as part of the filing indicated and is incorporated herein by reference.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE WILLIAMS COMPANIES, INC. (Registrant)

By: /s/ DAVID M. HIGBEE

David M. Higbee

Attorney-in-fact

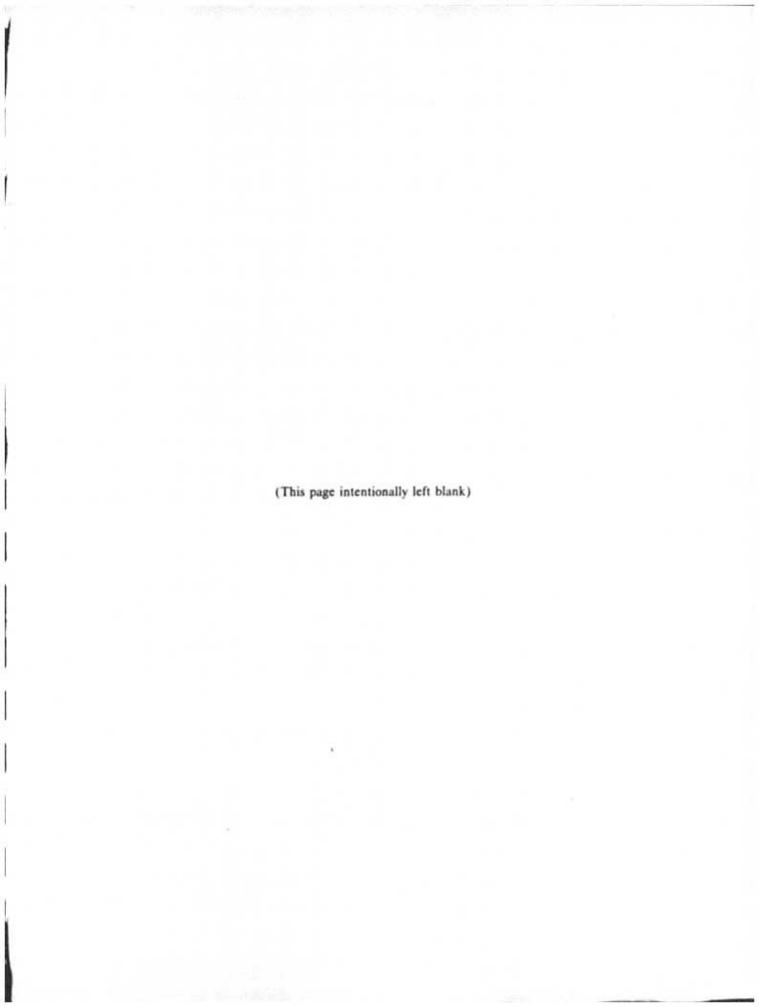
Dated: March 27, 1996

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant in the capacities and on the dates indicated.

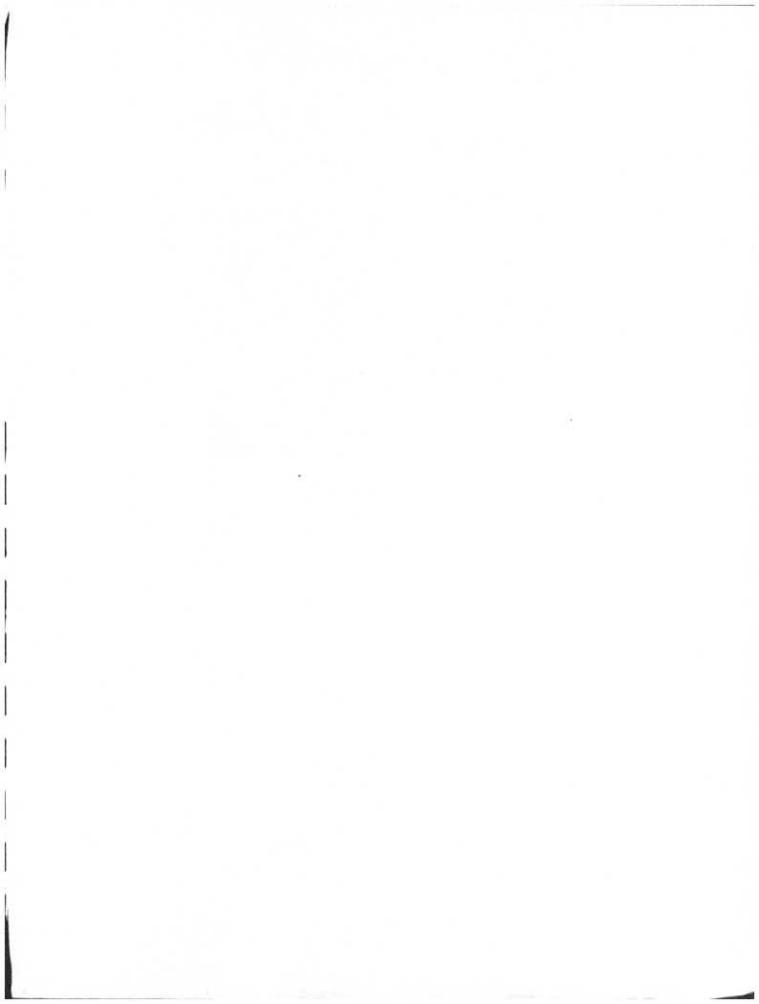
Signature	Title
/s/ Keith E. Bailey* Keith E. Bailey	 Chairman of the Board, President, Chief Executive Officer (Principal Executive Officer) and Director
/s/ JACK D. McCarthy* Jack D. McCarthy	Senior Vice President — Finance (Principal Financial Officer)
/s/ GARY R. BELITZ* Gary R. Belitz	Controller (Principal Accounting Officer)
/s/ HAROLD W. ANDERSEN® Harold W. Andersen	Director
/s/ RALPH E. BAILEY* Ralph E. Bailey	Director
/s/ GLENN A. COX* Glenn A. Cox	Director
/s/ THOMAS H. CRUIKSHANK* Thomas H. Cruikshank	Director
/s/ Ervin S. Duggan* Ervin S. Duggan	Director
/s/ PATRICIA L. HIGGINS* Patricia L. Higgins	Director
/s/ ROBERT J. LAFORTUNE* Robert J. LaFortune	Director
/s/ JAMES C. LEWIS* James C. Lewis	Director

Signature	Title
/s/ JACK A. MACALLISTER*	Director
Jack A. MacAllister	
/s/ James A. McClure*	Director
James A. McClure	
/s/ PETER C. MEINIG*	Director
Peter C. Meinig	
/s/ KAY A. ORR*	Director
Kay A. Orr	
/s/ GORDON R. PARKER*	Director
Gordon R. Parker	
/s/ JOSEPH H. WILLIAMS*	Director
Joseph H. Williams	
*By /s/ DAVID M. HIGBEE	
David M. Higbee	
Attorney-in-fact	

Dated: March 27, 1996







Form 10-K

SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549

(Mark One)

8

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 (FEE REQUIRED)

For the fiscal year ended December 31, 1996

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 (NO FEE REQUIRED)

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 (State or other jurisdiction of incorporation or organization) 73-0569878 (I.R.S. Employer Identification No.)

One Williams Center
Tulsa, Oklahoma
(Address of principal executive offices)

74172 (Zip Code)

Registrant's telephone number, including area code: (918) 588-2000

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Each Class

Common Stock, \$1.00 par value Preferred Stock Purchase Rights

\$2.21 Cumulative Preferred Stock, \$1.00 par value Name of Each Exchange on Which Registered

New York Stock Exchange and the Pacific Stock Exchange

New York Stock Exchange

9.60% Subordinated Deferrable Interest Debentures due 2025

New York Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

None

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 ⊠ No □

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

■

The aggregate market value of the registrant's voting stock held by nonaffiliates as of the close of business on March 21, 1997, was approximately \$7.2 billion.

The number of shares of the registrant's Common Stock outstanding at March 21, 1997, was 158,712,481, excluding 3,637,560 shares held by the Company.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement prepared for the solicitation of proxies in connection with the Annual Meeting of Stockholders of the Company for 1997 are incorporated by reference in Part 111.

THE WILLIAMS COMPANIES, INC. FORM 10-K PART I

Item 1. Business

(a) General Development of Business

The Williams Companies, Inc. (the "Company" or "Williams") was incorporated under the laws of the State of Nevada in 1949 and was reincorporated under the laws of the State of Delaware in 1987. The principal executive offices of the Company are located at One Williams Center, Tulsa, Oklahoma 74172 (telephone (918) 588-2000). Unless the context otherwise requires, references to the "Company" and "Williams" herein include The Williams Companies, Inc. and its subsidiaries.

On January 16, 1996, the Company acquired a 49.9 percent interest from its partner in Kern River Gas Transmission Company giving the Company 99.9 percent ownership of this natural gas pipeline system. The purchase price was \$206 million. See Note 2 of Notes to Consolidated Financial Statements. The Company acquired the remaining 0.1 percent interest in the partnership on February 28, 1997, for \$387,600.

Also in 1996, the Company combined its energy operations, other than its interstate natural gas pipelines, under a newly created, wholly owned, indirect subsidiary, Williams Energy Group, and began reporting such operations for financial reporting purposes on this basis in the fourth quarter of 1996. In addition, the Company organized the reporting for its communications operations under a single communications reporting entity, Williams Communications Group, Inc., and has reported such operations for financial reporting purposes on this basis since the third quarter of 1996.

In January 1995, the Company sold the network services operations of its telecommunications subsidiary to LDDS Communications, Inc. for \$2.5 billion in cash (the "WNS Sale"). The Company has reported the network services operations as discontinued operations for financial eporting purposes. See Note 3 of Notes to Consolidated Financial Statements. The Company used the proceeds from the WNS Sale to pay off short-term credit facilities, to fund the acquisition of Transco Energy Company discussed below, to finance its ongoing capital program and for other uses.

In December 1994, the Company entered into a merger agreement with Transco Energy Company. Under the agreement, the Company acquired approximately 60 percent of Transco Energy Company's common stock through a cash tender offer completed in January 1995. On April 28, 1995, the Transco Energy Company stockholders approved an agreement and plan of merger whereby Transco Energy Company became a wholly owned subsidiary of the Company effective May 1, 1995. Total value of the transaction was more than \$3 billion, including cash, stock and the assumption of Transco Energy Company debt. As of May 1, 1995, the Company caused Transco Energy Company to declare and pay as dividends to the Company all of Transco Energy Company's interest in Transcontinental Gas Pipe Line Corporation and Texas Gas Transmission Corporation. See Note 2 of Notes to Consolidated Financial Statements.

(b) Financial Information About Industry Segments

See Part II, Item 8 - Financial Statements and Supplementary Data.

(c) Narrative Description of Business

The Company, through subsidiaries, engages in the transportation and sale of natural gas and related activities; natural gas gathering, processing, and treating activities; the transportation and terminaling of petroleum products; hydrocarbon exploration and production activities; the production and marketing of ethanol; and energy commodity trading and marketing and provides a variety of other products and services, including price risk management services, to the energy industry. The Company also engages in the communications business. In 1996, the Company's energy subsidiaries owned and operated: (i) five interstate

natural gas pipeline systems; (ii) natural gas production properties; (iii) natural gas gathering and processing facilities; (iv) a common carrier petroleum products and crude oil pipeline system; (v) petroleum products terminals; and (vi) ethanol production facilities. The Company also trades and markets energy commodities and offers price-risk management services. The Company's communications subsidiaries offer: (i) data-voice- and video-related products and services; (ii) advertising distribution services; (iii) video services and other multimedia services for the broadcast industry; (iv) broadcast facsimile and audio- and videoconferencing services for businesses; (v) interactive, computer-based training and services; (vi) customer-premise voice and data equipment, including installation and maintenance; and (vii) network integration and management services nationwide. The Company also has investments in the equity of certain other companies.

Substantially all operations of Williams are conducted through subsidiaries. Williams performs management, legal, financial, tax, consultative, administrative and other services for its subsidiaries. Williams' principal sources of cash are from dividends and advances from its subsidiaries, investments, payments by subsidiaries for services rendered and interest payments from subsidiaries on cash advances. The amount of dividends available to Williams from subsidiaries largely depends upon each subsidiary's earnings and operating capital requirements. The terms of certain subsidiaries' borrowing arrangements limit the transfer of funds to the Company.

To achieve organizational and operating efficiencies, the Company's interstate natural gas pipelines are grouped together and are referred to internally as the interstate natural gas systems. All other operating companies are owned directly by Williams Holdings of Delaware, Inc., a wholly-owned subsidiary of the Company. The energy operations of Williams Holdings of Delaware, Inc. are grouped into a wholly-owned subsidiary, Williams Energy Group, and its communications operations are grouped into a wholly-owned subsidiary, Williams Communications Group, Inc. Item 1 of this report is formatted to reflect this structure.

WILLIAMS INTERSTATE NATURAL GAS SYSTEMS

The Company's interstate natural gas pipeline group owns and operates a combined total of approximately 28,000 miles of pipelines with a total annual throughput of approximately 3,800 TBtu* of natural gas and peak-day delivery capacity of approximately 15 Bcf of natural gas. The interstate natural gas pipeline group consists of Transcontinental Gas Pipe Line Corporation, Northwest Pipeline Corporation, Kern River Gas Transmission Company, Texas Gas Transmission Corporation and Williams Natural Gas Company, owners and operators of interstate natural gas pipeline systems. As previously noted, the Company acquired Transcontinental Gas Pipe Line Corporation and Texas Gas Transmission Corporation in 1995. For the accounting treatment of the acquisition, see Note 2 of Notes to Consolidated Financial Statements. Also as noted above, the Company acquired an additional 49.9 percent interest in Kern River Gas Transmission Company in January 1996 and the remaining 0.1 percent interest in February 1997.

The interstate natural gas pipeline group's transmission and storage activities are subject to regulation by the Federal Energy Regulatory Commission ("FERC") under the Natural Gas Act of 1938 ("Natural Gas Act") and under the Natural Gas Policy Act of 1978 ("NGPA"), and, as such, their rates and charges for the transportation of natural gas in interstate commerce, the extension, enlargement or abandonment of jurisdictional facilities, and accounting, among other things, are subject to regulation. Each pipeline holds certificates of public convenience and necessity issued by FERC authorizing ownership and operation of all pipelines, facilities and properties considered jurisdictional for which certificates are required under the Natural Gas Act. Each pipeline is also subject to the Natural Gas Pipeline Safety Act of 1968, as amended by Title I of the Pipeline Safety Act of 1979, which regulates safety requirements in the design, construction, operation and maintenance of interstate gas transmission facilities.

A business description of each company in the interstate natural gas pipeline group follows.

The term "Mcf" means thousand cubic feet, "MMcf" means million cubic feet and "Bcf" means billion cubic feet. All volumes of
natural gas are stated at a pressure base of 14.73 pounds per square inch absolute at 60 degrees Fahrenheit. The term "Btu" means
British Thermal Unit, "MMBtu" means one million British Thermal Units and "TBtu" means one trillion British Thermal Units.

TRANSCONTINENTAL GAS PIPE LINE CORPORATION (Transco)

Transco is an interstate natural gas transmission company that owns a 10,500-mile natural gas pipeline system extending from Texas, Louisiana, Mississippi and the offshore Gulf of Mexico through the states of Alabama, Georgia, South Carolina, North Carolina, Virginia, Maryland, Pennsylvania and New Jersey to the New York City metropolitan area. The system serves customers in Texas and eleven southeast and Atlantic seaboard states, including major metropolitan areas in Georgia, North Carolina, New York, New Jersey and Pennsylvania. Effective May 1, 1995, Transco transferred the operation of certain production area facilities to Williams Field Services Group, Inc., an affiliated company.

Pipeline System and Customers

At December 31, 1996, Transco's system had a mainline delivery capacity of approximately 3.6 Bcf of gas per day from production areas to its primary markets. Using its Leidy Line and market-area storage capacity. Transco can deliver an additional 2.9 Bcf of gas per day for a system-wide delivery capacity total of approximately 6.5 Bcf of gas per day. Excluding the production area facilities operated by Williams Field Services Group, Inc., Transco's system is composed of approximately 7,300 miles of mainline and branch transmission pipelines, 37 compressor stations and six storage locations. Compression facilities at a sea level-rated capacity total approximately 1.2 million horsepower.

Transco's major gas transportation customers are public utilities and municipalities that provide service to residential, commercial, industrial and electric generation end users. Shippers on Transco's pipeline system include public utilities, municipalities, intrastate pipelines, direct industrial users, electrical generators, marketers and producers. Transco's largest customer in 1996 accounted for approximately 11 percent of Transco's total operating revenues. No other customer accounted for more than 10 percent of total operating revenues. Transco's firm transportation agreements are generally long-term agreements with various expiration dates and account for the major portion of Transco's business. Additionally, Transco offers interruptible transportation services under shorter term agreements.

Transco has natural gas storage capacity in five underground storage fields located on or near its pipeline system and/or market areas and operates three of these storage fields and a liquefied natural gas (LNG) storage facility. The total storage capacity available to Transco and its customers in such storage fields and LNG facility is approximately 216 Bcf of gas. Storage capacity permits Transco's customers to inject gas into storage during the summer and off-peak periods for delivery during peak winter demand periods.

Expansion Projects

In August 1996, Transco filed for FERC approval to expand the offshore portion of its existing Southeast Louisiana Gathering System in two phases to provide a total of 660 MMcf of gas per day of additional firm transportation capacity. Transco estimates the cost of the expansion to be approximately \$129 million and expects to invest approximately \$95 million in 1997.

In November 1996, Transco filed for FERC approval to extend and expand its Mobile Bay lateral. The project will include expansion of Transco's existing 123-mile Mobile Bay lateral and construction of a new 77-mile offshore pipeline extension to an area near the outer continental shelf. The project, which would increase capacity as much as 600 MMcf of gas per day at an estimated cost of \$171 million, is targeted to be in service by the 1998-99 winter heating season. In December, Transco received nominations for 300 MMcf of gas per day of capacity in the project.

In November 1996, Transco completed and placed into service the Southeast Expansion Project. Since late 1994, the project has added 205 MMcf of gas per day of firm transportation capacity to Transco's customers in the southeast. The total cost of the expansion was approximately \$106 million, of which approximately \$22 million was invested in 1996.

In November 1996, FERC approved the Pine Needle LNG storage project. Transco and several of its major customers will construct and own the facility, which will be located near Transco's mainline system in Guilford, North Carolina. The project will have 4 Bcf of storage capacity and 400 MMcf of gas per day of

withdrawal capacity. Transco will operate the facility and have a 35 percent ownership interest. Construction began in February 1997, and the project is expected to be in service by the second quarter of 1999. The FERC application estimates the total cost of the project to be \$107 million.

In December 1996, Transco and several major customers announced the filing with the North Carolina Utilities Commission for approval of the Cardinal Pipeline System project. The project involves the acquisition of an existing 37-mile pipeline in North Carolina and construction of a 67-mile pipeline extension. Transco expects to complete construction of the pipeline extension by the end of 1999. Transco will operate the expanded pipeline system and have a 45 percent ownership interest. Transco expects to make equity investments of approximately \$22 million in this project.

In December 1996, FERC approved the SunBelt Expansion Project, which will provide additional firm transportation capacity to markets in Georgia, South Carolina and North Carolina. The SunBelt Expansion Project will provide a total of 146 MMcf of gas per day of firm transportation capacity to existing and new Transco customers by the 1997-1998 winter heating season. Transco estimates the cost of the expansion to be approximately \$85 million. Transco spent approximately \$12 million on the project in 1996 and expects to invest approximately \$68 million in 1997.

In November 1996, FERC made a preliminary determination that public convenience and necessity requires Transco's SeaBoard Expansion Project but denied Transco's request for rolled-in rate treatment. Transco has spent approximately \$6 million on the project to date. In response to FERC's denial of rolled-in rate treatment, Transco has plans to significantly modify this project.

Operating Statistics. The following table summarizes transportation data for the periods indicated, including periods during which the Company did not own Transco:

the second of th	1996	1995	1994
System Deliveries (TBtu)			
Market-area deliveries:			
Long-haul transportation	948.9	858.4	805.1
Market-area transportation	428.1	467.3	453.6
Total market-area deliveries	1,377.0	1,325.7	1,258.7
Production-area transportation	210.0	165.9	185.9
Total system deliveries	1,587.0	1,491.6	1,444.6
Average Daily Transportation Volumes (TBtu)	4.3	4.1	4.0
Average Daily Firm Reserved Capacity (TBtu)		5.2	4.9

NORTHWEST PIPELINE CORPORATION (Northwest Pipeline)

Northwest Pipeline is an interstate natural gas transmission company that owns and operates a pipeline system for the mainline transmission of natural gas extending from the San Juan Basin in northwestern New Mexico and southwestern Colorado through Colorado, Utah, Wyoming, Idaho, Oregon and Washington to a point on the Canadian border near Sumas, Washington. Northwest Pipeline provides services for markets in California, New Mexico, Colorado, Utah, Nevada, Wyoming, Idaho, Oregon and Washington, directly or indirectly through interconnections with other pipelines.

Pipeline System and Customers

At December 31, 1996, Northwest Pipeline's system, having an aggregate mainline deliverability of approximately 2.5 Bcf of gas per day, was composed of approximately 3,900 miles of mainline and branch transmission pipelines and 40 mainline compressor stations with a combined capacity of approximately 307,000 horsepower.

In 1996, Northwest Pipeline transported natural gas for a total of 143 customers. Transportation customers include distribution companies, municipalities, interstate and intrastate pipelines, gas marketers and

direct industrial users. The three largest customers of Northwest Pipeline in 1996 accounted for approximately 15.5 percent, 15.3 percent and 10.4 percent, respectively, of total operating revenues. No other customer accounted for more than 10 percent of total operating revenues. Northwest Pipeline's firm transportation agreements are generally long-term agreements with various expiration dates and account for the major portion of Northwest Pipeline's business. Additionally, Northwest Pipeline offers interruptible transportation service under agreements that are generally short term.

As a part of its transportation services, Northwest Pipeline utilizes underground storage facilities in Utah and Washington enabling it to balance daily receipts and deliveries. Northwest Pipeline also owns and operates a liquefied natural gas storage facility in Washington that provides a needle-peaking service for the system. These storage facilities have an aggregate delivery capacity of approximately 973 MMcf of gas per day.

Operating Statistics. The following table summarizes transportation data for the periods indicated (in TBtus):

	1996	1995	1994
Transportation Volumes	834	826	679
Average Daily Transportation Volumes		2.3	1.9
Average Daily Firm Reserved Capacity		2.4	2.4

KERN RIVER GAS TRANSMISSION COMPANY (Kern River)

Kern River is an interstate natural gas transmission company that owns and operates a natural gas pipeline system extending from Wyoming through Utah and Nevada to California. Kern River had been jointly owned and operated by Williams Western Pipeline Company, a subsidiary of the Company, and a subsidiary of an unaffiliated company. As previously indicated, the Company acquired an additional 49.9 percent interest in Kern River in January 1996. See Note 2 of Notes to Consolidated Financial Statements. In February 1997, the Company acquired the remaining 0.1 percent interest in Kern River. The transmission system, which commenced operations in February 1992 following completion of construction, delivers natural gas primarily to the enhanced oil recovery fields in southern California. The system also transports natural gas for utilities, municipalities and industries in California, Nevada and Utah.

Pipeline System and Customers

As of December 31, 1996, Kern River's pipeline system was composed of approximately 705 miles of mainline and branch transmission and five compressor stations having an aggregate mainline delivery capacity of 700 MMcf of gas per day. The pipeline system interconnects with the pipeline facilities of another pipeline company at Daggett, California. From the point of interconnection, Kern River and the other pipeline company have a common 219-mile pipeline which is owned 63.6 percent by Kern River and 36.4 percent by the other pipeline company, as tenants in common, and is designed to accommodate the combined throughput of both systems. This common facility has a capacity of 1.1 Bef of gas per day.

Gas is transported for others under firm long-term transportation contracts totaling 682 MMcf of gas per day. In 1996, Kern River transported natural gas for customers in California, Nevada and Utah. Gas was transported for five customers in Kern County, California, for reinjection as a part of enhanced oil recovery operations and for 28 local distribution customers, electric utilities, cogeneration projects and commercial and other industrial customers. The five largest customers of Kern River in 1996 accounted for approximately 14 percent, 13 percent, 12 percent, 11 percent and 11 percent, respectively, of operating revenues. Three of these customers serve the enhanced oil recovery fields. No other customer accounted for more than 10 percent of operating revenues in 1996.

During 1995, Kern River executed a seasonal firm transportation contract to deliver natural gas into the Las Vegas, Nevada, market area during the winter months. Kern River expects to begin deliveries of 10 MMcf of gas per day in December 1997 and to escalate such deliveries to 40 MMcf of gas per day on a seasonal basis in 1999.

Operating Statistics. The following table summarizes transportation data for the periods indicated (in TBtus):

	1996	1995	1994
Transportation Volumes	281	286	278
Average Daily Transportation Volumes	.77	.78	.76
Average Daily Firm Reserved Capacity	.71	.72	.74

TEXAS GAS TRANSMISSION CORPORATION (TXG)

TXG is an interstate natural gas transmission company that owns and operates a natural gas pipeline system originating in the Louisiana Gulf Coast area and in east Texas and running generally north and east through Louisiana, Arkansas, Mississippi, Tennessee, Kentucky, Indiana and into Ohio, with smaller diameter lines extending into Illinois. TXG's direct market area encompasses eight states in the South and Midwest, and includes the Memphis, Tennessee; Louisville, Kentucky; Cincinnati and Dayton, Ohio; and Indianapolis, Indiana, metropolitan areas. TXG also has indirect market access to the Northeast through interconnections with unaffiliated pipelines.

Pipeline System and Customers

At December 31, 1996, TXG's system, having a mainline delivery capacity of approximately 2.8 Bcf of gas per day, was composed of approximately 6,000 miles of mainline and branch transmission pipelines and 32 compressor stations having a sea level-rated capacity totaling approximately 549,000 horsepower.

In 1996, TXG transported gas to customers in Louisiana, Arkansas, Mississippi, Tennessee, Kentucky, Indiana, Illinois and Ohio and to customers in the Northeast served indirectly by TXG. TXG transported gas for 133 distribution companies and municipalities for resale to residential, commercial and industrial users. TXG provided transportation services to approximately 102 industrial customers located along the system. At December 31, 1996, TXG had transportation contracts with approximately 559 shippers. Transportation shippers include distribution companies, municipalities, intrastate pipelines, direct industrial users, electrical generators, marketers and producers. No customer of TXG accounted for more than 10 percent of total operating revenues during 1996. TXG's firm transportation agreements are generally long-term agreements with various expiration dates and account for the major portion of TXG's business. Additionally, TXG offers interruptible transportation services under agreements that are generally short-term.

TXG owns and operates natural gas storage reservoirs in 10 underground storage fields located on or near its pipeline system and/or market areas. The storage capacity of TXG's certificated storage fields is approximately 177 Bcf of gas. TXG's storage gas is used in part to meet operational balancing needs on its system, and in part to meet the requirements of TXG's "no-notice" transportation service, which allows TXG's customers to temporarily draw from TXG's storage gas to be repaid in-kind during the following summer season. A large portion of the gas delivered by TXG to its market area is used for space heating, resulting in substantially higher daily requirements during winter months.

Operating Statistics. The following table summarizes total system transportation volumes for the periods indicated, including periods during which the Company did not own TXG:

	1996	1995	1994
System deliveries (TBtu):			
Long-haul transportation	736.0	635.7	618.8
Short-haul transportation	58.5	57.6	188.6
Total system deliveries	794.5	693.3	807.4
Average Daily Transportation Volumes (TBtu)	2.2	1.9	2.2
Average Daily Firm Reserved Capacity (TBtu)		2.0	2.1

WILLIAMS NATURAL GAS COMPANY (Williams Natural Gas)

Williams Natural Gas is an interstate natural gas transmission company that owns and operates a natural gas pipeline system located in Colorado, Kansas, Missouri, Nebraska, Oklahoma, Texas and Wyoming. The system serves customers in seven states, including major metropolitan areas of Kansas and Missouri, its chief market areas.

Pipeline System and Customers

At December 31, 1996, Williams Natural Gas's system, having a mainline delivery capacity of approximately 2.2 Bcf of gas per day, was composed of approximately 6,000 miles of mainline and branch transmission and storage pipelines and 41 compressor stations having a sea level-rated capacity totaling approximately 227,000 horsepower.

In 1996, Williams Natural Gas transported gas to customers in Colorado, Kansas, Missouri, Nebraska, Oklahoma, Texas and Wyoming. Gas was transported for 78 distribution companies and municipalities for resale to residential, commercial and industrial users in approximately 530 cities and towns. Transportation services were provided to approximately 340 industrial customers, federal and state institutions and agricultural processing plants located principally in Kansas, Missouri and Oklahoma. At December 31, 1996, Williams Natural Gas had transportation contracts with approximately 196 shippers. Transportation shippers included distribution companies, municipalities, intrastate pipelines, direct industrial users, electrical generators, marketers and producers

In 1996, approximately 70 percent (approximately 35 percent each) of total operating revenues were generated from gas transportation services to Williams Natural Gas's two largest customers, Western Resources, Inc. and Missouri Gas Energy Company. Western Resources sells or resells gas to residential, commercial and industrial customers principally in certain major metropolitan areas of Kansas. Missouri Gas Energy sells or resells gas to residential, commercial and industrial customers principally in certain major metropolitan areas of Missouri. No other customer accounted for more than 10 percent of operating revenues during 1996.

Williams Natural Gas provides a significant portion of its transportation services to Western Resources pursuant to a 20-year transportation service agreement. After the initial two-year period which ended in November 1996, the contract allows Western Resources, on twelve-months prior notice, to reduce contracted capacity if Williams Natural Gas does not meet the terms of a competing offer from another natural gas pipeline to serve such capacity. To date, Williams Natural Gas has not received such a notice from Western Resources. Williams Natural Gas provides transportation services to Missouri Gas Energy under contracts primarily varying in terms from two to five years. These contracts do not have competitive out provisions as described in connection with the Western Resources' contract. During 1995, these two customers entered into contracts with a competitor as part of a litigation settlement. Following a decision by the Kansas Court of Appeals, the Western Resources contracts were deemed approved by operation of law. Subsequently, the competitor assigned the contracts with Western Resources and Missouri Gas Energy to another competitor of Williams Natural Gas. The two competitors are engaged in the acquisition of right-of-way and other acts to

begin construction under the contracts with Western Resources and Missouri Gas Energy. Up to 25 percent of the firm capacity now transported by Williams Natural Gas into the Kansas City market could be at risk if the pipeline contemplated by the contracts is built. Certain landowners whose property must be condemned to complete the project are challenging completion of the facilities. The contracts may be subject to termination if certain completion dates are not met.

Williams Natural Gas operates nine underground storage fields with an aggregate working gas storage capacity of approximately 43 Bcf and an aggregate delivery capacity of approximately 1.2 Bcf of gas per day. Williams Natural Gas's customers inject gas in these fields when demand is low and withdraw it to supply their peak requirements. During periods of peak demand, approximately two-thirds of the firm gas delivered to customers is supplied from these storage fields. Storage capacity enables the system to operate more uniformly and efficiently during the year.

In 1996, Williams Natural Gas entered firm transportation contracts to serve two electrical generation plants in the Kansas City area for potential daily usage of up to 100,000 MMBtu per day.

Operating Statistics. The following table summarizes transportation data for the periods indicated (in TBtus):

	1996	1995	1994
Transportation Volumes	341	334	346
Average Daily Transportation Volumes	.9	.9	.9
Average Daily Firm Reserved Capacity		2.0	2.0

Regulatory Matters

In 1992, FERC issued Order 636, which required interstate pipeline companies to restructure their tariffs to eliminate traditional on-system sales services. In addition, the Order required implementation of various changes in forms of service, including unbundling of gathering, transmission and storage services; terms and conditions of service; rate design; gas supply realignment cost recovery; and other major rate and tariff revisions. Kern River implemented its restructuring on August 1, 1993; Williams Natural Gas implemented its restructuring on October 1, 1993; and Transco, Northwest Pipeline and TXG implemented their restructurings on November 1, 1993. Certain aspects of four pipeline company's Order 636 restructurings are under appeal.

Each interstate natural gas pipeline has various regulatory proceedings pending. Rates are established primarily through FERC's ratemaking process. Key determinants in the ratemaking process are (1) costs of providing service, including depreciation rates, (2) allowed rate of return, including the equity component of the capital structure, and (3) volume throughput assumptions. FERC determines the allowed rate of return in each rate case. Rate design and the allocation of costs between the demand and commodity rates also impact profitability. As a result of such proceedings, the pipeline companies have collected a portion of their revenues subject to refund. See Note 12 of Notes to Coasolidated Financial Statements for the amount of revenues reserved for potential refund as of December 31, 1996.

Each interstate natural gas pipeline company, except Kern River, has undertaken the reformation of its respective gas supply contracts. None of the pipelines have any significant pending supplier take-or-pay, ratable-take or minimum-take claims. For information on outstanding issues with respect to contract reformation, gas purchase deficiencies and related regulatory issues, see Note 17 of Notes to Consolidated Financial Statements.

Competition

Competition for natural gas transportation has intensified in recent years due to customer access to other pipelines, rate competitiveness among pipelines, customers' desire to have more than one transporter and regulatory developments. FERC's stated purpose for implementing Order 636 was to improve the competitive

structure of the natural gas pipeline industry. Future utilization of pipeline capacity will depend on competition from other pipelines, use of alternative fuels, the general level of natural gas demand and weather conditions. Electricity and distillate fuel oil are primary competitive forms of energy for residential and commercial markets. Coal and residual fuel oil compete for industrial and electric generation markets. Nuclear and hydroelectric power and power purchased from grid arrangements among electric utilities also compete with gas-fired power generation in certain markets.

As mentioned, when restructured tariffs became effective under Order 636, all suppliers of natural gas were able to compete for any gas markets capable of being served by the pipelines using nondiscriminatory transportation services provided by the pipelines. As the Order 636 regulated environment has matured, many pipelines have faced reduced levels of subscribed capacity as contractual terms expire and customers opt to reduce firm capacity under contract in favor of alternative sources of transmission and related services. This situation, known in the industry as "capacity turnback," is forcing the pipelines to evaluate the consequences of major demand reductions on system utilization and cost structure to remaining customers.

The Company is aware that several state jurisdictions have been involved in implementing changes similar to the changes that have occurred at the federal level under Order 636. Such activity, frequently referred to as "LDC unbundling," has been most pronounced in the states of New York, New Jersey and Pennsylvania. New York and New Jersey enacted regulations regarding LDC unbundling in 1995. Pennsylvania is expected to enact an LDC unbundling program in 1997. In addition, Maryland currently has a pilot unbundling program for industrial, commercial, and residential end-users and may take additional steps toward unbundling in 1997. Georgia may also act in 1997 to implement an LDC unbundling program. Management expects these regulations to encourage greater competition in the natural gas marketplace.

Ownership of Property

Each of the Company's interstate natural gas pipeline subsidiaries generally owns its facilities in fee. However, a substantial portion of each pipeline's facilities is constructed and maintained pursuant to rights-ofway, easements, permits, licenses or consents on and across properties owned by others. Compressor stations, with appurtenant facilities, are located in whole or in part either on lands owned or on sites held under leases or permits issued or approved by public authorities. The storage facilities are either owned or contracted under long-term leases or easements.

Environmental Matters

Each interstate natural gas pipeline is subject to the National Environmental Policy Act and federal, state and local laws and regulations relating to environmental quality control. Management believes that, with respect to any capital expenditures and operation and maintenance expenses required to meet applicable environmental standards and regulations, FERC would grant the requisite rate relief so that, for the most part, the pipeline subsidiaries could recover such expenditures in their rates. For this reason, management believes that compliance with applicable environmental requirements by the interstate pipelines is not likely to have a material effect upon the Company's earnings or competitive position.

For a discussion of specific environmental issues involving the interstate pipelines, including estimated cleanup costs associated with certain pipeline activities, see "Environmental" under Management's Discussion and Analysis of Financial Condition and Results of Operations and Note 17 of Notes to Consolidated Financial Statements.

WILLIAMS HOLDINGS OF DELAWARE, INC. (Williams Holdings)

In 1994, the Company established Williams Holdings to be a holding company for its assets other than its interstate natural gas pipelines and related assets. Virtually all of Williams Holdings' assets were operated by other subsidiaries of the Company prior to January 1, 1995.

Williams Holdings' energy subsidiaries are engaged in exploration and production; natural gas gathering and processing; petroleum products transportation and terminaling; ethanol production; and energy commodity marketing and trading and price risk management services. In addition, these subsidiaries provide a variety of other products and services to the energy industry. Williams Holdings' communications subsidiaries offer data-, voice-, and video-related products and services and customer premise voice and data equipment, including installation and maintenance, nationwide. Williams Holdings also has certain other equity investments.

WILLIAMS ENERGY GROUP (Williams Energy)

In 1996, Williams Holdings reorganized its energy operations under a newly created, wholly owned subsidiary, Williams Energy, and began reporting such operations for financial reporting purposes on this basis in the fourth quarter of 1996. Management believes the new structure will better position it to offer customers a full range of energy products and services by capitalizing on synergies of the combined business units.

Williams Energy is comprised of four major business units: Exploration and Production. Field Services. Petroleum Services, and Merchant Services. Through its business units, Williams Energy engages in energy production and exploration activities; natural gas gathering, processing, and treating: petroleum liquids transportation and terminal services; ethanol production; and energy commodity marketing and trading.

Williams Energy, through its subsidiaries, owns 531 Bcf of proved natural gas reserves located primarily in the San Juan Basin of Colorado and New Mexico and owns and operates approximately 11,000 miles of gathering pipelines, eight gas treating plants, 10 gas processing plants, 57 petroleum products terminals, and approximately 9,300 miles of liquids pipeline. Physical and notional volumes traded by Williams Energy's merchant services unit approximated 6,552 TBtu equivalents in 1996. Williams Energy, through its subsidiaries, employs approximately 2,500 employees.

Revenues and operating profit for Williams Energy by business unit are reported in Note 4 of Notes to Consolidated Financial Statements herein.

A business description of each of Williams Energy's business units follows.

EXPLORATION AND PRODUCTION

Williams Energy, through its wholly owned subsidiary Williams Production Company (Williams Production), owns and operates producing gas leasehold properties in Colorado, Louisiana, New Mexico, Texas, Utah, Wyoming, and offshore in the Gulf of Mexico.

In December 1996, Williams Production entered into an agreement with an unaffiliated exploration company for the joint exploration of 27,000 acres in the Houma Embayment Area of southern Louisiana. Williams Production will earn a 50 percent working interest in the leasehold block by drilling up to eight exploratory wells within a 125-square mile 3-D seismic survey during the next 12-18 months. Williams Production also purchased 50 percent of this company's working interest in 23 producing wells and associated facilities in the area with daily production of approximately 9,000 MMBtus per day. Also in 1996, Williams Production acquired leasehold interests in the East Texas Haynesville Cotton Valley Reef and now controls, along with unaffiliated partners, in excess of 135,000 gross acres in this area.

Gas Reserves. As of December 31, 1996, 1995, and 1994, Williams Production had proved developed natural gas reserves of 323 Bef, 292 Bef, 269 Bef, respectively, and proved undeveloped reserves of 208 Bef, 222 Bef, and 220 Bef, respectively. Of Williams Production's total proved reserves, 87 percent are located in the San Juan Basin of Colorado and New Mexico. No major discovery or other favorable or adverse event has caused a significant change in estimated gas reserves since year end.

Customers and Operations. As of December 31, 1996, the gross and net developed leasehold acres owned by Williams Production totaled 263,869 and 114,183, respectively, and the gross and net undeveloped acres owned were 339,540 and 76,722, respectively. As of such date, Williams Production owned interests in 2,911 gross producing wells (523 net) on its leasehold lands. The following table summarizes drilling activity for the periods indicated:

		Development	
Completed During	Gross Wells	Net Wells	
1996	65	11	
1995	61	22	
1994	66	19	

The majority of Williams Production's gas production is currently being sold in the spot market at market prices. Total net production sold during 1996, 1995, and 1994 was 26.8 Bcf, 26.3 Bcf, and 23.2 Bcf, respectively. The average production costs, including production taxes, per Mcf of gas produced were \$.27, \$.26, and \$.30, in 1996, 1995, and 1994, respectively. The average wellhead sales price per Mcf was \$.98, \$.88, and \$1.19, respectively, for the same periods.

In 1993, Williams Production conveyed a net profits interest in certain of its properties to the Williams Coal Seam Gas Royalty Trust. Williams subsequently sold Trust Units to the public in an underwritten public offering. Williams Holdings holds 3,568,791 Trust Units representing 36.8 percent of outstanding Units. Substantially all of the production attributable to the properties conveyed to the Trust was from the Fruitland coal formation and constituted coal seam gas. Proved developed coal seam gas reserves at December 31, 1996, attributed to the properties conveyed were 149 Bcf. Production information reported herein includes Williams Production's interest in such Units.

FIELD SERVICES

Williams Energy, through Williams Field Services Group, Inc. and its subsidiaries (Field Services), owns and operates nonregulated natural gas gathering, processing, and treating facilities located in northwestern New Mexico, southwestern Colorado, southwestern Wyoming, northwestern Oklahoma, southwestern Kansas, and also in areas offshore and onshore in Texas and Louisiana. Field Services also operates regulated gathering facilities owned by Transco, an affiliated company. In February 1996, Field Services and Transco filed applications with FERC to spindown all of Transco's gathering facilities to Field Services. FERC subsequently denied these requests and Field Services and Transco have filed a request for rehearing of this denial. Gathering services provided include the gathering of gas and the treating of coal seam gas.

Expansion Projects. Field Services expanded its gulf coast operations in 1996 primarily through acquisitions. In July, Field Services acquired a 70 MMcf per day processing plant in south-central Louisiana. In November, Field Services signed a letter of intent to acquire the remaining 50 percent interest in a 500 MMcf per day processing plant in southwestern Louisiana and acquired a majority portion in a south Texas gathering system. In addition, Field Services expanded its gathering system in the San Juan Basin, completed construction of a 50 MMcf per day CO₂ treating facility in the Oklahoma Panhandle, and acquired the remaining 50 percent interest in a 60 MMcf per day processing plant in southern Texas.

Customers and Operations. Facilities owned and operated by Field Services consist of approximately 11,000 miles of gathering pipelines, eight gas treating plants and 10 gas processing plants (five of which are partially owned). The aggregate daily inlet capacity is approximately 7.9 Bcf and 6.9 Bcf of gas for the gathering systems and gas processing, treating, and dehydration facilities, respectively. Gathering and processing customers have direct access to interstate pipelines, including affiliated pipelines, which provide access to multiple markets.

During 1996. Field Services gathered natural gas for 314 customers. The largest gathering customer accounted for approximately 15 percent of total gathered volumes. During 1996, Field Services processed natural gas for a total of 119 customers. The three largest customers accounted for approximately 25 percent, 12 percent, and 10 percent, respectively, of total processed volumes. No other customer accounted for more than 10 percent of gathered or processed volumes. Field Services' gathering and processing agreements with

large customers are generally long-term agreements with various expiration dates. These long-term agreements account for the majority of the gas gathered and processed by Field Services.

Operating Statistics. The following table summarizes gathering, processing, and natural gas liquid sales volumes for the periods indicated. The information includes operations attributed to facilities owned by affiliated entities but operated by Field Services:

	1996	1995	1994
Gas volumes (TBtu, except liquids sales):			
Gathering	2,155	1,806	895
Processing	484	406	392
Natural gas liquid sales (millions of gallons)	391	284	281

PETROLEUM SERVICES

Williams Energy, through wholly owned subsidiaries in its Petroleum Services unit, owns and operates a petroleum products and crude oil pipeline, two ethanol production plants (one of which is partially owned), and petroleum products terminals and provides services and markets products related thereto.

Transportation. A subsidiary in the Petroleum Services unit, Williams Pipe Line Company (Williams Pipe Line), owns and operates a petroleum products and crude oil pipeline system which covers an 11-state area extending from Oklahoma in the south to North Dakota and Minnesota in the north and Illinois in the east. The system is operated as a common carrier offering transportation and terminaling services on a nondiscriminatory basis under published tariffs. The system transports refined products, LP-gases, lube extracted fuel oil, and crude oil.

At December 31, 1996, the system traversed approximately 7,300 miles of right-of-way and included approximately 9,300 miles of pipeline in various sizes up to 16 inches in diameter. The system includes 82 pumping stations, 23 million barrels of storage capacity, and 47 delivery terminals. The terminals are equipped to deliver refined products into tank trucks and tank cars. The maximum number of barrels which the system can transport per day depends upon the operating balance achieved at a given time between various segments of the system. Because the balance is dependent upon the mix of products to be shipped and the demand levels at the various delivery points, the exact capacity of the system cannot be stated.

Operating Statistics. The operating statistics set forth below relate to the system's operations for the periods indicated:

	1996	1994	1994
	1770	1993	1444
Shipments (thousands of barrels):			
Refined products:			
Gasolines	134,296	125,060	120,682
Distillates	68,628	61,238	61,129
Aviation fuels	11,189	12,535	9,523
LP-Gases	15,618	12,839	10,849
Lube extracted fuel oil	8,555	4,462	0
Crude oil	891	860	1,062
Total Shipments	239,177	216,994	203,245
Daily average (thousands of barrels)	655	595	557
Average haul (miles)	259	269	284
Barrel miles (millions)	61,969	58,326	57,631

Environmental regulations and changing crude supply patterns continue to affect the refining industry. The industry's response to environmental regulations and changing supply patterns will directly affect volumes and products shipped on the Williams Pipe Line system. Environmental Protection Agency ("EPA") regulations, driven by the Clean Air Act, require refiners to change the composition of fuel manufactured. A pipeline's ability to respond to the effects of regulation and changing supply patterns will determine its ability

to maintain and capture new market shares. Williams Pipe Line has successfully responded to changes in diesel fuel composition and product supply and has adapted to new gasoline additive requirements. Reformulated gasoline regulations have not yet significantly affected Williams Pipe Line. Williams Pipe Line will continue to attempt to position itself to respond to changing regulations and supply patterns, but the Company cannot predict how future changes in the marketplace will affect Williams Pipe Line's market areas.

Ethanol. Williams Energy, through its wholly owned subsidiary Williams Energy Ventures, Inc. (WEV), is engaged in the production and marketing of ethanol. WEV owns and operates two ethanol plants of which corn is the principal feedstock. The Pekin, Illinois, plant, which WEV purchased in 1995, has an annual production capacity of 100 million gallons of fuel-grade and industrial ethanol and also produces various coproducts. The Aurora, Nebraska, plant (in which WEV owns a 75 percent interest) began operations in November 1995 and has an annual production capacity of 30 million gallons. WEV also markets ethanol produced by third parties.

The sales volumes set forth below include ethanol produced by third parties as well as by WEV for the periods indicated:

	1996	1995	1994
Ethanol sold (thousands of gallons)	119,800	53,500	n/a
Coproducts sold (thousands of tons)	398	159	n/a

Terminals and Services Williams Energy, through its subsidiary WEV, operates petroleum products terminals in the western and southeastern United States and provides services including performance additives and ethanol blending. In September 1996, WEV acquired a 45.5 percent interest in eight petroleum products terminals located in the southeast United States. During the last four months of the year, these terminals loaded 7.8 million barrels of refined products.

MERCHANT SERVICES

Williams Energy, through subsidiaries, primarily Williams Energy Services Company and its subsidiaries ("WESCO"), offers a full suite of energy products and services throughout North America and serves over 2,000 companies. WESCO's business includes natural gas and energy commodity marketing activities, at both the wholesale and retail levels. In addition, WESCO offers a comprehensive array of price-risk management products and services and capital services to the diverse energy industry.

WESCO markets natural gas throughout North America and grew its total volumes (physical and notional) to an average of 15.9 TBtu per day in 1996. The core of WESCO's business has traditionally been the Gulf Coast and eastern regions, using the pipeline systems owned by the Company, but also includes marketing on approximately 30 non-Williams' pipelines. WESCO's natural gas customers include producers, industrials, local distribution companies, utilities, and other marketers.

During 1996, WESCO also marketed natural gas liquids, crude, refined products, and liquefied natural gas with total volumes (physical and notional) averaging 2.0 TBtu per day.

WESCO entered the power marketing and trading business in 1996. During its first year of operations, WESCO's power group marketed over 4 million megawatt hours (physical and notional) of power.

WESCO provides price risk management services through a variety of financial instruments including option and swap agreements related to various energy commodities. Through its capital financing services, WESCO also provides participants in the energy industry with capital for energy-related projects including acquisitions of proved reserves and re-working of wells.

In 1996, WESCO established a retail energy services group. As a part of this strategy, WESCO acquired a 50 percent interest in Volunteer Energy Corporation, a natural gas marketing company with experience in end-use markets. WESCO has also aligned with Boston Edison Company to form EnergyVision, an enterprise designed to provide access to retail energy markets in the New England area.

Operating Statistics. The following table summarizes operating profit and marketing volumes for the periods indicated (dollars in million, volumes in TBtu equivalents):

	1996	1995	1994
Operating profit	\$ 66.4	\$ 33.2	\$ 3.4
Total marketing volumes (physical and notional)	6,552	3,822	1,642

Regulatory Matters

Field Services. Historically, an issue has existed as to whether FERC has authority under the Natural Gas Act to regulate gathering and processing prices and services. During 1994, after reviewing its legal authority in a Public Comment Proceeding, FERC determined that while it retains some regulatory jurisdiction over gathering and processing performed by interstate pipelines, pipeline-affiliated gathering and processing companies are outside its authority under the Natural Gas Act. An appellate court has affi...ed FERC's determination. As a result of these FERC decisions, several of the individual states in which Field Services conducts its operations may consider whether to impose regulatory requirements on gathering companies. No state currently regulates Field Services' gathering or processing rates or services.

Petroleum Services. Williams Pipe Line, as an interstate common carrier pipeline, is subject to the provisions and regulations of the Interstate Commerce Act. Under this Act, Williams Pipe Line is required, among other things, to establish just, reasonable and nondiscriminatory rates, to file its tariffs with FERC, to keep its records and accounts pursuant to the Uniform System of Accounts for Oil Pipeline Companies, to make annual reports to FERC and to submit to examination of its records by the audit staff of FERC. Authority to regulate rates, shipping rules, and other practices and to prescribe depreciation rates for common carrier pipelines is exercised by FERC. The Department of Transportation, as authorized by the 1992 Pipeline Safety Reauthorization Act, is the oversight authority for interstate liquids pipelines. Williams Pipe Line is also subject to the provisions of various state laws applicable to intrastate pipelines.

On December 31, 1989, a rate cap, which resulted from a settlement with several shippers, effectively freezing Williams Pipe Line's rates for the previous five years, expired. Williams Pipe Line filed a revised tariff on January 16, 1990, with FERC and the state commissions. The tariff set an average increase in rates of 11 percent and established volume incentives and proportional rate discounts. Certain shippers on the Williams Pipe Line system and a competing pipeline carrier filed protests with FERC alleging that the revised rates are not just and reasonable and are unlawfully discriminatory. Williams Pipe Line elected to bifurcate this proceeding in accordance with the then-current FERC policy. Phase I of FERC's bifurcated proceeding provides a carrier the opportunity to justify its rates and rate structure by demonstrating that its markets are workably competitive. Any issues unresolved in Phase I require cost justification in Phase II.

FERC's Presiding Judge issued the Initial Decision in Phase II on May 29, 1996. The Judge ruled that Williams Pipe Line failed to demonstrate that the rates at issue for the 12 less competitive markets were just and reasonable and that Williams Pipe Line must roll back those rates to pre-1990 levels and pay refunds with interest to its shippers. The Initial Decision held that Williams Pipe Line's individual rates must be judged on the basis of cost allocations, although Williams Pipe Line was given no notice of this particular basis of judgment and the Commission expressly declined to adopt such standards in its Opinion No. 391. Moreover, the Commission clarified its final order in Phase I (Opinion No. 391-A) by stating that Williams Pipe Line was not required to defend its rates with cost allocations. Primarily on this basis, Williams Pipe Line sought a review of the Initial Decision by the full Commission by filing a brief on exceptions on June 28, 1996. The review of the Phase II Initial Decision is pending before the Commission, and a shipper's appeal of the Phase I order in the United States Court of Appeals for the District of Columbia Circuit has been stayed pending the completion of Phase II. Williams Pipe Line is not required to comply with the Initial Decision in Phase II prior to the Commission's issuance of a final order. Williams Pipe Line continues to believe that its revised tariffs will ultimately be found lawful. See Note 17 of Notes to Consolidated Financial Statements.

Merchant Services. Management believes that WESCO's activities are conducted in substantial compliance with the marketing affiliate rules of FERC Order 497. Order 497 imposes certain nondiscrimination, disclosure, and separation requirements upon interstate natural gas pipelines with respect to their natural gas trading affiliates. WESCO has taken steps to ensure it does not share employees with affiliated interstate natural gas pipelines and does not receive information from such affiliates that is not also available to unaffiliated natural gas trading companies.

Competition

Exploration and Production. Williams Energy's exploration and production unit competes with a wide variety of independent producers as well as integrated oil and gas companies for markets for its production.

Field Services. Williams Energy competes for gathering and processing business with interstate and intrastate pipelines, producers, and independent gatherers and processors. Numerous factors impact any given customer's choice of a gathering or processing services provider, including rate, term, timeliness of well connections, pressure obligations, and the willingness of the provider to process for either a fee or for liquids taken in-kind.

Petroleum Services. Williams Energy's petroleum services operations are subject to competition because Williams Pipe Line operates without the protection of a federal certificate of public convenience and necessity that might preclude other entrants from providing like service in its area of operations. Further, Williams Pipe Line must plan, operate and compete without the operating stability inherent in a broad base of contractually obligated or owner-controlled usage. Because Williams Pipe Line is a common carrier, its shippers need only meet the requirements set forth in its published tariffs in order to avail themselves of the transportation services offered by Williams Pipe Line.

Competition exists from other pipelines, refineries, barge traffic, railroads, and tank trucks. Competition is affected by trades of products or crude oil between refineries that have access to the system and by trades among brokers, traders and others who control products. Such trades can result in the diversion from the Williams Pipe Line system of volume that might otherwise be transported on the system. Shorter, lower revenue hauls may also result from such trades. Williams Pipe Line also is exposed to interfuel competition whereby an energy form shipped by a liquids pipeline, such as heating fuel, is replaced by a form not transported by a liquids pipeline, such as electricity or natural gas. While Williams Pipe Line faces competition from a variety of sources throughout its marketing areas, the principal competition is other pipelines. A number of pipeline systems, competing on a broad range of price and service levels, provide transportation service to various areas served by the system. The possible construction of additional competing products or crude oil pipelines, conversions of crude oil or natural gas pipelines to products transportation, changes in refining capacity, refinery closings, changes in the availability of crude oil to refineries located in its marketing area, or conservation and conversion efforts by fuel consumers may adversely affect the volumes available for transportation by Williams Pipe Line.

Williams Energy's ethanol operations compete in local, regional, and national fuel additive markets with one large ethanol producer, numerous smaller ethanol producers, and other fuel additive producers, such as refineries.

Merchant Services. Williams Energy's merchant services operations directly compete with large independent energy marketers, marketing affiliates of regulated pipelines and utilities, electric wholesalers and retailers, and natural gas producers. The financial trading business competes with other energy-based companies offering similar services as well as certain brokerage houses. This level of competition contributes to a business environment of constant pricing and margin pressure.

Ownership of Property

The majority of Williams Energy's ownership interests in exploration and production properties are held as working interests in oil and gas leaseholds.

Williams Energy's gathering and processing facilities are owned in fee. Gathering systems are constructed and maintained pursuant to rights-of-way, easements, permits, licenses, and consents on and across properties owned by others. The compressor stations and gas processing and treating facilities are located in whole or in part on lands owned by subsidiaries of Williams Energy or on sites held under leases or permits issued or approved by public authorities.

Williams Energy's petroleum pipeline system is owned in fee. However, a substantial portion of the system is operated, constructed and maintained pursuant to rights-of-way, easements, permits, licenses, or consents on and across properties owned by others. The terminals, pump stations, and all other facilities of the system are located on lands owned in fee or on lands held under long-term leases, permits, or contracts. Management believes that the system is in such a condition and maintained in such a manner that it is adequate and sufficient for the conduct of business.

The primary assets of Williams Energy's merchant services unit are its term contracts, employees, and related systems and technological support.

Environmental Matters

Williams Energy is subject to various federal, state, and local laws and regulations relating to environmental quality control. Management believes that Williams Energy's operations are in substantial compliance with existing environmental legal requirements. Management expects that compliance with such existing environmental legal requirements will not have a material adverse effect on the capital expenditures, earnings, and competitive position of Williams Energy.

The EPA has named Williams Pipe Line as a potentially responsible party as defined in Section 107(a) of the Comprehensive Environmental Response, Compensation, and Liability Act, for a site in Sioux Falls, South Dakota. The EPA placed this site on the National Priorities List in July 1990. In April 1991, Williams Pipe Line and the EPA executed an administrative consent order under which Williams Pipe Line agreed to conduct a remedial investigation and feasibility study for this site. The EPA issued its "No Action" Record of Decision in 1994, concluding that there were no significant hazards associated with the site subject to two additional years of monitoring for arsenic in certain existing monitoring wells. Williams Pipe Line should complete monitoring in the second quarter of 1997.

WILLIAMS COMMUNICATIONS GROUP, INC. (Williams Communications Group)

The Company organized the reporting for its communications operations under a single communications reporting entity in 1996 and has reported such operations for financial reporting purposes on a consolidated basis since the third quarter of 1996. Management believes that the new structure will better position it to provide total enterprise network solutions and superior customer service on a global basis. In addition, management believes this structure will facilitate growth and diversification while recognizing the convergence of customers, markets and product offerings of its communications entities. Management also believes the combination creates a vehicle to better establish name recognition and presence in the communications industry.

The new entity, Williams Communications Group, Inc. ("Williams Communications Group"), is comprised of four major business units: Williams Telecommunications Systems, Inc.; Vyvx, Inc.; Global Access Telecommunications Services, Inc. (formerly known as ITC mediaConferencing Company); and Williams Learning Network, Inc. Through its business units, Williams Communications Group provides customer-premise voice and data equipment, including installation and maintenance; advertising distribution; network integration and management services; video services and other multimedia services for the broadcasting industry; broadcast facsimile, audio- and videoconferencing services for businesses; and interactive, computer-based training programs and services for a variety of industries.

In March 1997, Williams Communications Group acquired the stock of Critical Technologies, Incorporated, a network systems integrator that designs, builds, implements, and maintains large-scale business communications systems.

Williams Communications Group, through its subsidiaries, owns approximately 11,000 fiber miles of fiber-optic network, approximately 53 television switching centers, more than 1,300 fully equipped service vehicles, and 120 sales and services locations nationwide plus international offices serving Europe, South America and the Pacific Rim. In addition, Williams Communications Group owns or manages five teleports in the United States and has rights to capacity on domestic and international satellite transponders. Williams Communications Group employed approximately 4,300 employees as of December 31, 1996.

Consolidated revenues by business unit and operating profit for Williams Communications Group for 1996 were as follows (dollars in millions):

Revenues:

WilTel	
WilTel Voice	
WilTel Data	
Ууух	100.0
Williams Learning Network	17.9
Global Access	7.6
Other	17.7
Total	\$711.3
Operating profit	\$ 6.6

A business description of each of Williams Communications Group's business units follows.

WILLIAMS TELECOMMUNICATIONS SYSTEMS, INC. (WilTel)

WilTel provides data, voice and video communications products and services to a wide variety of customers nationally. WilTel serves its customers through more than 100 sales and service locations throughout the United States, over 3,100 employees and over 1,300 stocked service vehicles. WilTel employs more than 1,400 technicians and more than 500 sales representatives and sales support personnel to serve an estimated 41,000 commercial, governmental and institutional customer sites. WilTel's customer base ranges from large, publicly-held corporations and the federal government to small privately-owned entities.

WilTel offers its customers a full array of data, multimedia, voice and video network interconnect products including digital key systems (generally designed for voice applications with fewer than 100 lines), private branch exchange (PBX) systems (generally designed for voice applications with greater than 100 lines), voice processing systems, interactive voice response systems, automatic call distribution applications, call accounting systems, network monitoring and management systems, desktop video, routers, channel banks, intelligent hubs and cabling. WilTel's services also include the design, configuration and installation of voice and data networks and the management of customers' telecommunications operations and facilities. WilTel's National Technical Resource Center provides customers with on-line order entry and trouble reporting services, advanced technical assistance and training. Other service capabilities include Local Area Network and PBX remote monitoring and toll fraud detection.

In 1994, WilTel acquired BellSouth's customer premise equipment sales and service operations in 29 states outside of BellSouth's local operating region in the nine southeastern-most states and Jackson Voice Data, a New York City-based customer premise equipment company. In 1996, WilTel acquired Comlink, Inc., a Mariborough, Massachusetts, based voice and network systems integrator. Comlink services approximately 5,000 customers in Vermont, New Hampshire, Maine, Massachusetts, Rhode Island and Connecticut. Also in 1996, WilTel acquired SoftIRON Systems, Inc., a network systems integrator based in California. SoftIRON works with organizations to design, procure, install and support complex data systems. SoftIRON maintains more than 200 sites with high-speed data switches, 5,000 remote access ports and extensive networks managing more than 15,000 devices. These acquisitions have enabled WilTel to capitalize on its existing infrastructure, strengthen its national market presence and geographic customer density and has provided more diversity in product offerings.

Operating Statistics. The following table summarizes the results of operations for the periods indicated (dollars and ports in millions):

	1996	1995	1994
Revenues	\$568.1	\$494.9	\$396.6
Percentage of revenues by type of service:			
New system sales	40%	34%	33%
System modifications		39	36
Maintenance	24	25	24
Other	2	2	7
Backlog	\$112.2	\$ 85.0	\$ 92.4
Total ports	5.1	4.7	4.1

A port is defined as an electronic address resident in a customer's PBX or key system that supports a station, trunk or data port.

In 1996, WilTel derived approximately 59.7 percent of its revenues from its existing customer base and approximately 40.3 percent from the sale of new telecommunications systems. WilTel's three largest suppliers accounted for approximately 86 percent of equipment sold in 1996. A single manufacturer supplied 73 percent of all equipment sold. In this case, WilTel is the largest independent distributor in the United States of certain of this company's products. About 63 percent of WilTel's active customer base consists of this manufacturer's products. The distribution agreement with this supplier is scheduled to expire at the end of 2000. Management believes there is minimal risk as to the availability of products from suppliers.

VYVX, INC. (Vyvx)

Vyvx offers broadcast-quality television and multimedia transmission services nationwide by means of its 11,000-mile fiber optic cable system, satellite uplink/downlink facilities and satellite transponder capacity. Vyvx fiber primarily provides backhaul or point-to-point transmission of sports, news and other programming between two or more customer locations. With satellite facilities, Vyvx provides point-to-multipoint transmission service. Vyvx's customers include all of the major broadcast and cable networks. Vyvx is also engaged in the business of advertising distribution and is exploring other multimedia communication opportunities through its fiber optic network.

In 1996, Vyvx acquired four teleports (including satellite earth station facilities) from ICG Wireless Services. The teleports are located in Atlanta, Denver, Los Angeles and New York (Carteret, New Jersey). Also in 1996, Vyvx acquired Global Access Telecommunications Services, Inc., a reseller of worldwide video transmission services, which resulted in the management of a fifth teleport in Kansas City. The business television operations were transferred to ITC mediaConferencing, and Vyvx continues to operate the satellite and transponder facilities of the former Global Access. As discussed below, ITC mediaConferencing has adopted the Global Access name. These acquisitions enabled Vyvx to become a full-service fiber-optic and satellite video transmission provider.

In November and December, 1996, respectively, Vyvx acquired the assets of Cycle-Sat, Inc. and Viacom MGS Services Inc., both distributors of television advertising. These acquisitions provide connectivity and presence in more than 550 television broadcast stations around the country.

Under an agreement with IXC Communications entered into in the fourth quarter 1996, Vyvx will build a 1,600-mile fiber-optic network from Houston to Washington, D.C., in proximity to pipeline right-of-way owned by an affiliated company. Vyvx will then exchange rights to use a portion of the unlit fiber for usage rights to IXC's existing 4,500-mile Los Angeles-to-New York route. It is estimated that by mid-1998, Vyvx will have added 6,100 miles of new, unrestricted network to its existing 11,000-mile system, which is limited to multimedia applications.

WILLIAMS LEARNING NETWORK, INC. (Williams Learning Network)

Williams Learning Network, formerly Williams Knowledge Systems, provides multimedia-based training products for the chemical, refining, utility and manufacturing industries. Williams Learning Network serves approximately 6,500 customers in these industries.

In December 1996, Williams Learning Network announced the formation of a joint venture with the Public Broadcast Service to utilize Internet, video-on-demand, fiber-optic and satellite technologies to bring professional development and training services to the business community. The 20-year agreement provides for a management committee to operate the new entity.

GLOBAL ACCESS TELECOMMUNICATIONS SYSTEMS, INC. (Global Access) (formerly ITC mediaConferencing Company)

In October 1995, a business unit of Williams Communications Group acquired a 22 percent interest in ITC mediaConferencing Company ("ITC") and acquired the remaining interest in ITC in 1996. ITC, which has changed its name to Global Access, offers multi-point videoconferencing, audioconferencing and enhanced fax services as well as single point to multi-point business television services. The acquisition enables Williams Communications Group to provide customers with integrated media conferences, bringing together voice, video and facsimile by utilizing Williams Communications Group's existing fiber-optic and satellite services.

In March 1997, Global Access acquired Satellite Management, Inc., a systems integrator for business television and provider of other satellite-based services.

Regulatory Matters

The equipment WilTel sells must meet the requirements of Part 68 of the Federal Communications Commission (FCC) rules governing the equipment registration, labeling and connection of equipment to telephone networks. WilTel relies on the equipment manufacturers' compliance with these requirements for its own compliance regarding the equipment it distributes. A subsidiary of WilTel, which provides intrastate microwave communications services for a Federal agency, is subject to FCC regulations as a common carrier microwave licensee. These regulations have a minimal impact on WilTel's operations.

Vyvx is subject to FCC regulations as a common carrier with regard to certain of its transmission services and is subject to the laws of certain states governing public utilities. An FCC rulemaking to eliminate domestic, common carrier tariffs has been stayed pending judicial review. In the interim, the FCC is requiring such carriers to operate under traditional tariff rules. Operations of satellite earth stations and certain other related transmission facilities are also subject to FCC licensing and other regulations. These regulations do not significantly impact Vyvx's operations.

Competition

WilTel has many competitors ranging from Lucent Technologies and the Regional Bell Operating Companies to small individually-owned companies that sell and service customer premise equipment. Competitors include companies that sell equipment comparable or identical to that sold by WilTel. There are virtually no barriers to entry into this market.

Vyvx's video and multimedia transmission operations compete primarily with companies offering video or multimedia transmission services by means of satellite facilities and to a lesser degree with companies offering transmission services via microwave facilities or fiber-optic cable.

Federal telecommunications reform legislation enacted in February 1996 is designed to increase competition both in the long distance market and local exchange market by significantly liberalizing current restrictions on market entry. In particular, the legislation establishes procedures permitting Regional Bell Operating Companies to provide long distance services including, but not limited to, video transmission services, subject to certain restrictions and conditions precedent. Moreover, electric and gas utilities may

provide telecommunications services, including long distance services, through separate subsidiaries. The legislation also calls for tariff forbearance and relaxation of regulation over common carriers. At this time, management cannot predict the impact such legislation may have on the operations of Williams Communications Group.

Ownership of Property

Vyvx owns part of its fiber-optic transmission facilities and leases the remainder. Vyvx carries signals by means of its own fiber-optics facilities, as well as carrying signals over fiber-optic facilities leased from third-party interexchange carriers and the various local exchange carriers. Vyvx holds its satellite transponder capacity under various agreements. Vyvx owns part of its teleport facilities and holds the remainder under either a management agreement or long-term facilities leases.

Environmental Matters

Williams Communications Group is subject to federal, state and local laws and regulations relating to the environmental aspects of its business. Management believes that Williams Communications Group's operations are in substantial compliance with existing environmental legal requirements. Management expects that compliance with such existing environmental legal requirements will not have a material adverse effect on the capital expenditures, earnings and competitive position of Williams Communications Group.

OTHER INFORMATION

Williams believes that it has adequate sources and availability of raw materials to assure the continued supply of its services and products for existing and anticipated business needs. Williams' pipeline systems are all regulated in various ways resulting in the financial return on the investments made in the systems being limited to standards permitted by the regulatory bodies. Each of the pipeline systems has ongoing capital requirements for efficiency and mandatory improvements, with expansion opportunities also necessitating periodic capital outlays.

A plant site in Pensacola, Florida, that was previously operated by a former subsidiary of Williams, has been placed on the National Priorities List. This former subsidiary has also been identified as a potentially responsible party at a National Priorities List cleanup site in Michigan. A third site, located in Lakeland, Florida, which was formerly owned and operated by this subsidiary, is under investigation by the Florida Department of Environmental Protection and cleanup is anticipated. Williams does not believe that the ultimate resolution of the foregoing matters, taken as a whole and after consideration of insurance coverage, contribution or other indemnification arrangements, will have a material adverse financial effect on the Company. See Note 17 of Notes to Consolidated Financial Statements.

At December 31, 1996, the Company had approximately 11,000 full-time employees, of whom approximately 1,200 were represented by unions and covered by collective bargaining agreements. The Company considers its relations with its employees to be generally good.

Forward-Looking Information

Certain matters discussed in this report, excluding historical information, include forward-looking statements. Although the Company believes such forward-looking statements are based on reasonable assumptions, no assurance can be given that every objective will be reached. Such statements are made in reliance on the safe harbor protections provided under the Private Securities Litigation Reform Act of 1995.

As required by such Act, the Company hereby identifies the following important factors that could cause actual results to differ materially from any results projected, forecasted, estimated or budgeted by the Company in forward-looking statements: (i) risks and uncertainties impacting the Company as a whole primarily relate to changes in general economic conditions in the United States; changes in laws and regulations to which the Company is subject, including tax, environmental and employment laws and regulations; the cost and effects of legal and administrative claims and proceedings against the Company or its

subsidiaries or which may be brought against the Company or its subsidiaries; conditions of the capital markets utilized by the Company to access capital to finance operations; and, to the extent the Company increases its investments and activities abroad, such investments and activities will be subject to foreign economies, laws, and regulations; (ii) for the Company's regulated businesses, risks and uncertainties primarily relate to the impact of future federal and state regulation of business activities, including allowed rates of return; and (iii) risks and uncertainties associated with the Company's unregulated businesses primarily relate to the ability of such entities to develop expanded markets and product offerings as well as maintaining existing markets. It is also possible that certain aspects of the Company's businesses that are currently unregulated may be subject to both federal and state regulation in the future. In addition, future utilization of pipeline capacity will depend on energy prices, competition from other pipelines and alternate fuels, the general level of natural gas and petroleum product demand and weather conditions, among other things. Further, gas prices which directly impact transportation and gathering and processing throughput and operating profits may fluctuate in unpredictable ways as may corn prices, which directly affect the Company's ethanol business. It is also not possible to predict which of many possible future products and service offerings will be important to maintaining a competitive position in the communications business or what expenditures will be required to develop and provide such products and services.

(d) Financial Information about Foreign and Domestic Operations and Export Sales

Williams has no significant foreign operations.

Item 2. Properties

See Item 1(c) for description of properties.

Item 3. Legal Proceedings

Other than as described under Item 1 — Business and in Note 17 of Notes to Consolidated Financial Statements, there are no material pending legal proceedings. Williams is subject to ordinary routine litigation incidental to its businesses.

Subsequent Developments. On February 27, 1997, FERC issued Order 636-C in response to the court's remand affirming that pipelines may recover all of their gas supply realignment costs but requiring pipelines to individually propose the percentage of such costs to be allocated to interruptible transportation services, instead of a uniform 10 percent allocation. The order also prospectively relaxes the eligibility requirements for receiving no-notice service and reduces the right of first refusal matching period from 20 years to five years. Order 636-C is still subject to potential rehearing at FERC.

Item 4. Submission of Matters to a Vote of Security Holders

Not applicable.

Executive Officers of Williams

The names, ages, positions and earliest election dates of the executive officers or Williams are:

Name	Age	Positions and Offices Heid	Held Office Since
Keith E. Bailey	54	Chairman of the Board, President, Chief Executive Officer and Director (Principal Executive Officer)	05-19-94
John C. Bumgarner, Jr	54	Senior Vice President — Corporate Development and Planning, President — Williams International Company	01-01-79
James R. Herbster	55	Senior Vice President - Administration	01-01-92
Jack D. McCarthy	54	Senior Vice President — Finance (Principal Financial Officer)	01-01-92
William G. von Glahn	53	Senior Vice President and General Counsel	08-01-96
Gary R. Belitz	47	Controller (Principal Accounting Officer)	01-01-92
Stephen L. Cropper	47	President — Williams Energy Group	10-01-96
Henry C. Hirsch	54	Vice Chairman and Chief Executive Officer — Williams Communications Group	02-11-97
Howard E. Janzen	42	President and Chief Operating Officer — Williams Communications Group	02-11-97
Brian E. O'Neill	61	President — Transco, Northwest Pipeline, Kern River, TXG and Williams Natural Gas	01-01-88

All of the above officers have been employed by Williams or its subsidiaries as officers or otherwise for more than five years and have had no other employment during such period.

PART II

Item 5. Market for the Registrant's Common Equity and Releted Stockholder Matters

Williams' Common Stock is listed on the New York and Pacific Stock Exchanges under the symbol "WMB." At the close of business on December 31, 1996, Williams had 12,386 holders of record of its Common Stock. The daily closing price ranges (composite transactions) and dividends declared by quarter for each of the past two years (adjusted to reflect the three-for-two stock split discussed below) are as follows:

		1996			1995		
Quarter	High	Low	Dividend	High	Low	Dividend	
lst	\$34	\$281/2	\$.227	\$20%	\$167/12	5.18	
2nd	\$351/12	\$311/4	5.227	\$231/12	\$20%	5.18	
3rd	\$341/12	\$301/2	\$.227	\$261/12	\$231/12	\$.18	
4th	\$3815	\$321/2	5.26	\$2975	\$251/17	\$.18	

On December 30, 1996, the Company distributed one share of Common Stock of the Company, \$1 par value, for every two shares of Common Stock outstanding on December 6, 1996, pursuant to a three-for-two stock split.

Terms of certain subsidiaries' borrowing arrangements limit transfer of funds to Williams. These terms have not impeded, nor are they expected to in the future, Williams' ability to meet its cash obligations.

Item 6. Selected Financial Data

The following financial data are an integral part of, and should be read in conjunction with, the consolidated financial statements and notes thereto. Information concerning significant trends in the financial condition and results of operations is contained in Management's Discussion and Analysis of Financial Condition and Results of Operations on pages F-1 through F-9 of this report.

	1996	1995	1994	1993	1992	
	100 271 100	(Millions, ex	(Millions, except per-share amounts)			
Revenues	\$ 3,531.2	\$ 2,855.7	\$1,751.1	\$1,793.4	\$1,983.5	
Income from continuing operations*	362.3	299.4	164.9	185.4	103.1	
Income from discontinued operations**	10.9	1,018.8	94.0	46.4	25.2	
Fully diluted earnings per share:***						
Income from continuing operations	2.14	1.84	1.02	1.14	.65	
Income from discontinued operations	-	6.48	.61	.30	.19	
Cash dividends per common share ***	.94	.72	.56	.52	.51	
Total assets at December 31	12,418.8	10,561.2	5,226.1	5,020.4	4,982.3	
Long-term obligations at December 31	4,376.9	2,874.0	1,307.8	1,604.8	1,683.2	
Stockholders' equity at December 31	3,421.0	3,187.1	1,505.5	1,724.0	1,518.3	

- See Note 6 of Notes to Consolidated Financial Statements for discussion of significant asset sales and write-off of project costs in 1996, 1995 and 1994. Income from continuing operations in 1993 includes a pre-tax gain of \$51.6 million as a result of the sale of 6.1 million units in the Williams Coal Seam Gas Royalty Trust and a pre-tax gain of \$45.9 million as a result of the sale of its intrastate natural gas pipeline system and other related assets in Louisiana.
- ** See Note 3 of Notes to Consolidated Financial Statements for discussion of the 1995 gain on the sale of discontinued operations. Amounts prior to 1995 reflect operating results for the network services operations.
- *** Per-share amounts have been restated to reflect the effect of the December 30, 1996, 3-for-2 common stock split and distribution as discussed in Note 14 of Notes to Consolidated Financial Statements.

Item 7. Management's Discussion and Analysis of Financial Conditions and Results of Operations Results of Operations

1996 vs. 1995

Northwest Pipeline's revenues increased \$14.5 million, or 6 percent, due primarily to increased transportation rates, effective February 1, 1996, associated with the expansion of mainline capacity placed into service on December 1, 1995. In addition, \$9 million of revenue in 1996 associated with reserve reversals and favorable regulatory decisions was more than offset by the effect of the 1995 reversal of approximately \$16 million of accrued liabilities for estimated rate refund accruals. Total throughput increased 8 TBtu, or 1 percent. Operating profit increased \$9.2 million, or 8 percent, due primarily to increased transportation rates associated with the expansion of mainline capacity, and the reserve reversals and favorable regulatory decisions. Partially offsetting were higher depreciation expense associated with the mainline expansion and the approximate \$11 million net favorable effect of two 1995 reserve accrual adjustments. The 1995 reserve accrual adjustments included a \$16 million favorable adjustment of rate refund accruals based on a favorable rate case order, partially offset by a loss accrual (included in other income — net) in connection with a lawsuit involving a former transportation customer.

Williams Natural Gas' revenues increased \$4.1 million, or 2 percent, due primarily to increased transportation revenue resulting from new fariff rates that became effective August 1, 1995. Total throughput increased 6.9 TBtu, or 2 percent. Operating profit was substantially the same as the prior year as the effect of a \$4 million 1995 reversal of a regulatory accrual was offset by new tariff rates that became effective August 1, 1995.

Transcontinental Gas Pipe Line's (Transco) revenues increased \$35.1 million, or 5 percent, due primarily to higher natural gas transportation revenues and liquids and liquefiable transportation revenues of \$20 million and \$9 million, respectively. Additionally, revenue for 1996 reflects a full year of operations compared with 1995, which reflected operations from January 18, 1995, when Williams acquired a majority interest in Transco Energy. Revenues associated with the period January 1 through January 17, 1995, were approximately \$36 million. Offsetting these increases were lower revenues resulting from lower transportation costs charged to Transco by others and passed through to customers as provided in Transco's rates. Transportation revenues increased due primarily to increased long-haul throughput, which benefitted from a two-phase system expansion placed in service in late 1996 and late 1995, and new rates effective September 1, 1995, which allowed the passthrough of increased costs. Total throughput increased 176.1 TBtu, or 12 percent, due primarily to a full year of operations in 1996 compared to a partial year in 1995. Operating profit increased \$29.6 million, or 18 percent, due primarily to increased transportation revenues, lower general and administrative expenses and a full year of operations in 1996, partially offset by higher operation and maintenance expenses and higher taxes other than income taxes.

Texas Gas Transmission's revenues and operating profit increased \$29.8 million, or 11 percent, and \$21.1 million, or 33 percent, respectively, due primarily to new rates that became effective April 1, 1995, and an adjustment to regulatory accruals based upon a recent rate case settlement. Also, 1995 reflected operations from January 18, when Williams acquired a majority interest in Transco Energy. Revenues associated with the period January 1 through January 17, 1995, were \$16 million. Total throughput increased 141.1 TBtu, or 22 percent, due primarily to a full year of operations in 1996 compared to a partial year in 1995 and the impact of a colder winter in 1996.

Kern River Gas Transmission's (Kern River) remaining interest was acquired by Williams on January 16, 1996. Revenues and operating profit amounts for 1996 include the operating results of Kern River since the acquisition date. Kern River's revenues were \$160.6 million for 1996, while costs and operating expenses were \$35 million, selling, general and administrative expenses were \$13 million and operating profit was \$113 million. Prior to the acquisition, Williams accounted for its 50 percent ownership in Kern River using the equity method of accounting, with its share of equity earnings recorded in investing income. Throughput was 269.9 TBtu during 1996 (for the period subsequent to the acquisition date). Throughput for 1996 is comparable to 1995.

Field Services' revenues increased \$83.4 million, or 16 percent, due primarily to higher natural gas liquids sales revenues of \$64 million combined with higher gathering and processing revenues of \$6 million and \$13 million, respectively. Natural gas liquids sales revenues increased due to a 36 percent increase in volumes combined with higher average prices. Gathering and processing volumes each increased 19 percent while average gathering rates decreased. Costs and operating expenses increased \$52 million, or 15 percent, due primarily to higher fuel and replacement gas purchases, expanded facilities and increased operations. Other income — net for 1996 includes a \$20 million gain from the property insurance coverage associated with construction of replacement gathering facilities and \$6 million of gains from the sale of two small gathering systems, partially offset by \$5 million of environmental remediation accruals. Other income — net for 1995 includes \$20 million in operating profit from a favorable resolution of contingency issues involving previously regulated gathering and processing assets. Operating profit increased \$26.4 million, or 16 percent, due primarily to higher natural gas liquids margins and higher gathering and processing revenues, partially offset by higher costs and operating expenses. Operating profit was favorably impacted in both 1996 and 1995 by approximately \$20 million of other income.

Merchant Services' revenues increased \$107.6 million, or 70 percent, due primarily to higher natural gas and gas liquids marketing, price-risk management activities and petroleum product marketing of \$77 million, \$24 million and \$18 million, respectively, partially offset by lower contract origination revenues of \$10 million. Natural gas and gas liquids marketing revenues increased due to higher marketing volumes and prices. In addition, net physical trading revenues increased \$3 million, due to a 19 percent increase in natural gas physical trading volumes from 754 TBtu to 896 TBtu largely offset by lower physical trading margins. Costs and operating expenses increased \$73 million, or 94 percent, due primarily to higher natural gas purchase volumes and prices. Operating profit increased \$33.2 million, or 100 percent, due primarily to higher price-risk

management revenues, a reduction of development costs associated with its information products business and increased natural gas marketing volumes. Partially offsetting were higher selling, general and administrative expenses and lower contract origination revenues resulting from the impact of profits realized from certain long-term natural gas supply obligations in 1995. Merchant Services' price-risk management and trading activities are subject to risk from changes in energy commodity market prices, the portfolio position of its financial instruments and physical commitments, and credit risk. Merchant Services manages risk by maintaining its portfolio within established trading policy guidelines.

Petroleum Services' revenues increased \$165.2 million, or 50 percent, due primarily to an increase in transportation activities and ethanol sales of \$31 million and \$133 million, respectively. Revenues from transportation activities increased due primarily to a 10 percent increase in shipments and a \$14 million increase in product sales. Shipments increased as a result of new business and the 1995 impacts of unfavorable weather conditions and a fire at a truck-loading rack. Average length of haul and transportation rate per barrel were slightly below 1995 due primarily to shorter haul movements. Ethanol revenues increased following the August 1995 acquisition of Pekin Energy and the fourth-quarter 1995 completion of the Aurora plant. Costs and operating expenses increased \$155 million, or 68 percent, due primarily to a full year of ethanol production activities. Operating profit increased \$6.5 million, or 9 percent, due primarily to increased shipments, partially offset by lower ethanol margins and production levels as a result of record high corn prices.

Exploration and Production's revenues increased \$19.5 million, or 31 percent, due primarily to higher revenues from the marketing of production from the Williams Coal Seam Gas Royalty Trust (Royalty Trust) and increased production revenues of \$9 million and \$8 million, respectively. The increase in marketing revenues reflects both increased volumes and higher average gas prices. The increase in production revenues reflects higher average gas prices. Costs and operating expenses increased \$18 million due primarily to higher Royalty Trust natural gas purchase costs. Other income — net in 1995 includes an \$8 million loss accrual for a future minimum price natural gas commitment. Operating profit increased \$8.7 million to \$2.8 million in 1996 due primarily to the effect of the \$8 million 1995 loss accrual.

Williams Communications Group's revenues increased \$172.4 million, or 32 percent, due primarily to the 1996 acquisitions which contributed revenues of \$95 million. Additionally, increased business activity resulted in a \$36 million revenue increase in new systems sales and a \$16 million increase in digital fiber television services. The number of ports in service at December 31, 1996, increased 8 percent and billable minutes from occasional service increased 16 percent. Dedicated service voice-grade equivalent miles at December 31, 1996, decreased 6 percent as compared with December 31, 1995, which in part reflects a shift to occasional service. Costs and operating expenses increased \$126 million, or 31 percent, and selling, general and administrative expenses increased \$63 million, or 62 percent, due primarily to the overall increase in business activity and higher expenses for developing additional products and services, including the cost of integrating the most recent acquisitions. Operating profit decreased \$18.4 million, or 74 percent, due primarily to the expenses of developing additional products and services along with integrating the most recent acquisitions.

General corporate expenses increased \$3.7 million, or 10 percent, due primarily to higher employee compensation expense and consulting fees, partially offset by the effect of a \$5 million contribution in 1995 to The Williams Companies Foundation. Interest accrued increased \$82 million, or 30 percent, due primarily to higher borrowing levels including debt associated with the January 1996 acquisition of the remaining interest in Kern River (see Note 2), slightly offset by lower average interest rates. Interest capitalized decreased \$7.6 million, or 53 percent, due primarily to lower capital expenditures for gathering and processing facilities and the 1995 completion of Northwest Pipeline's mainline expansion. Investing income decreased \$75.1 million, or 80 percent, due primarily to the effect of interest earned in 1995 on the invested portion of the cash proceeds from the sale of Williams' network services operations, a \$15 million dividend in 1995 from Texasgulf Inc. (sold in 1995), and \$31 million lower equity earnings from Williams' 50 percent ownership in Kern River. Kern River's 1996 operating results are included in operating profit since the acquisition date (see Note 2). The 1996 gain on sales of assets results from the sale of the 15 percent interest in Texasgulf Inc. The 1995 write-off of project costs results from the cancellation of an underground coal gasification project in Wyoming (see Note 6). The \$12 million favorable change in other income (expense) — net in 1996 is due primarily to the 1995 effect of

approximately \$10 million of minority interest expense associated with the Transco merger and approximately \$10 million of reserve reversals in 1996, partially offset by higher environmental accruals of \$4 million and additional expense of international activities.

The \$81.1 million, or 79 percent, increase in the provision for income taxes on continuing operations is primarily a result of higher pre-tax income and a higher effective income tax rate. The increase in the effective income tax rate is the result of the 1995 recognition of \$29.8 million of previously unrecognized tax benefits realized as a result of the sale of Texasgulf Inc. (see Note 6). The effective income tax rate in 1996 is less than the federal statutory rate due primarily to income tax credits from research activities and coal-seam gas production, partially offset by the effects of state income taxes. In addition, 1996 includes recognition of favorable adjustments totaling \$13 million related to previously provided deferred income taxes on certain regulated capital projects and state income tax adjustments related to 1995. The effective income tax rate in 1995 is less than the federal statutory rate due primarily to income tax credits from coal-seam gas production, partially offset by the effects of state income taxes and minority interest. In addition, 1995 includes the previously unrecognized tax benefits related to the sale of Texasgulf Inc. (see Note 6) and recognition of an \$8 million income tax benefit resulting from settlements with taxing authorities (see Note 7).

On January 5, 1995, Williams sold its network services operations to LDDS Communications, Inc. for \$2.5 billion in cash. The sale yielded an after-tax gain of approximately \$1 billion, which is reported as income from discontinued operations (see Note 3).

Preferred stock dividends decreased \$4.9 million, or 32 percent, due primarily to the 1995 effect of a difference in the fair value of subordinated debentures issued and the carrying value of the exchanged \$2.21 cumulative preferred stock (see Note 14).

1995 vs. 1994

Northwest Pipeline's revenues increased \$16.7 million, or 7 percent, due primarily to the \$16 million reversal of a portion of certain rate refund accruals and increased transportation rates put into effect in November 1994, partially offset by the completion in 1994 of billing contract-reformation surcharges. Mainline throughput increased 22 percent; however, revenues were not significantly affected due to the effects of the straight-fixed-variable rate design prescribed by the Federal Energy Regulatory Commission. Operating profit increased \$11.6 million, or 11 percent, due primarily to higher transportation rates and the approximate \$11 million net effect of two reserve accrual adjustments, partially offset by \$5 million, or 13 percent, higher operations and maintenance expenses. The reserve accrual adjustments involved a \$16 million adjustment to rate refund accruals because of favorable rate case developments, partially offset by a loss accrual (included in other income — net) in connection with a lawsuit involving a former transportation customer.

Williams Natural Gas' revenues decreased \$57 million, or 25 percent, and costs and operating expenses decreased \$62 million, or 40 percent, due primarily to \$36 million lower direct billing of purchased gas adjustments and lower contract-reformation recovery of \$21 million. Operating profit decreased \$3.8 million, or 8 percent, due primarily to the effect of the 1994 reversal of excess contract-reformation accruals of \$7.4 million (included in other income — net) and \$3.2 million from lower 1995 average firm reserved capacity, partially offset by \$4.6 million resulting from higher average firm reserved capacity rates, effective August 1, 1995, and higher storage revenues of \$3.7 million.

Transcontinental Gas Pipe Line's revenues were \$725.3 million in 1995, while costs and expenses were \$560 million and operating profit was \$165 million. Throughput was 1,410.9 TBtu in 1995 (for the period subsequent to the acquisition date). Transcontinental Gas Pipe Line placed new, higher rates into effect September 1, 1995, subject to refund. Market-area deliveries in 1995 and 1994 were approximately the same.

Texas Gas Transmission's revenues were \$276.3 million in 1995, while costs and expenses were \$212 million and operating profit was \$64 million. Throughput was 653.4 TBtu in 1995 (for the period subsequent to the acquisition date). Texas Gas placed new, higher rates into effect April 1, 1995, subject to refund.

Field Services' revenues increased \$204.2 million, or 62 percent, due primarily to \$172 million higher gathering revenues. Gathering revenues increased due primarily to a 102 percent increase in gathering volumes, including \$131 million attributable to Transco Energy's Gulf Coast gathering operations, combined with an increase in average gathering prices, excluding Gulf Coast operations. Liquids and processing volumes increased 6 percent and 4 percent, respectively. Costs and operating expenses increased \$149 million, or 78 percent, and selling, general and administrative expenses increased \$25 million, or 91 percent, with Transco Energy's activities contributing \$102 million and \$13 million, respectively. In addition, costs and operating expenses increased due to expanded facilities. Other income — net for 1995 includes \$20 million in operating profit from the favorable resolution of contingency issues involving previously regulated gathering and processing assets. Operating profit increased \$48.1 million, or 43 percent, primarily resulting from the \$20 million in other income and a doubling of gathering volumes, primarily a result of Transco Energy's gathering activities. Operating profit in 1994 included approximately \$7 million in favorable settlements and adjustments of certain prior period accruals, including income of \$4 million from an adjustment to operating taxes.

Merchant Services' revenues and costs and operating expenses decreased \$228.2 million and \$289 million, respectively. The addition of Transco Energy's gas trading activities was more than offset by the reporting of 1995 natural gas marketing activities on a net-margin basis (see Note 15) and \$72 million in lower petroleum services operations resulting from adverse market conditions. Natural gas physical trading volumes increased to 754 TBtu in 1995 compared to 148 TBtu in 1994, primarily from the effect of the Transco Energy acquisition. Selling, general and administrative expenses increased \$28 million due primarily to the increase in trading activity. Operating profit increased \$29.8 million from \$3.4 million in 1994. Trading activities' operating profit increased \$34 million, attributable primarily to income recognition from long-term natural gas supply obligations and no-notice service provided to local distribution companies. Included in trading activities is a price-risk management adjustment of \$4 million from the valuation of certain natural gas supply and sales contracts previously excluded from trading activities. These increases were partially offset by \$6 million of loss provisions, primarily accruals for contract disputes, and increased costs of supporting its information services business.

Petroleum Services' revenues increased \$111.2 million, or 51 percent, due to an increase in transportation activities and ethanol sales of \$33 million and \$84 million, respectively. Revenue from transportation activities increased due primarily to higher shipments and a \$15 million increase in product sales. Shipments, while 7 percent higher than 1994, were reduced by the November 1994 fire at a truck-loading rack and unfavorable weather conditions in the first half of 1995. The average transportation rate per barrel and average length of haul were slightly below 1994 due primarily to shorter haul movements. Ethanol revenues increased following the acquisition of Pekin Energy in August 1995. Costs and operating expenses increased \$93 million, or 69 percent, due primarily to increased operating expenses associated with transportation and ethanol activities. Operating profit increased \$17.3 million, or 33 percent, due primarily to increased shipments, higher product sales margins of \$4 million, \$3 million related to the operations of Pekin Energy and the effect of \$5 million of costs in 1994 for evaluating and determining whether to build an oil refinery near Phoenix.

Exploration and Production's revenues increased \$23.7 million, or 61 percent, due primarily to \$35 million higher revenue from the marketing of production from the Royalty Trust and a 14 percent increase in production volumes, partially offset by a decrease in average gas sales prices. Costs and operating expenses increased \$33 million due primarily to higher Royalty Trust natural gas purchase costs. Other income — net in 1995 includes an \$8 million loss accrual for a future minimum price natural gas commitment. Operating profit decreased \$19.5 million to a \$5.9 million operating loss in 1995 due primarily to the \$8 million loss accrual, lower average gas sales prices and \$3 million higher selling, general and administrative expenses.

Williams Communications Group's revenues increased \$122.3 million, or 29 percent, due primarily to \$30 million from new systems, \$28 million from existing system enhancements, \$37 million from contract maintenance, moves, adds and changes, and \$15 million in digital fiber television services. These amounts include the effect of the acquisitions of BellSouth Communications Systems in March 1994 and Jackson Voice Data, completed in October 1994. The number of ports in service at December 31, 1995, increased 14 percent, billable minutes from occasional service increased 110 percent and dedicated service voice-grade

equivalent miles at December 31, 1995, increased 50 percent as compared with December 31, 1994. Costs and operating expenses increased \$84 million, or 26 percent, and selling, general and administrative expenses increased \$21 million, or 27 percent, due primarily to the overall increase in volume of sales and services and higher expenses for developing additional products and services. Operating profit increased \$17.4 million from \$7.6 million in 1994 due primarily to increased activity in new system sales, enhancements to existing systems, maintenance, digital television services and the full-year 1995 impact of two 1994 acquisitions.

General corporate expenses increased \$9.7 million, or 35 percent, due primarily to a \$6.4 million increase in charitable contributions, including \$5 million to The Williams Companies Foundation. Interest accrued increased \$132.1 million, or 91 percent, due primarily to the \$2 billion outstanding debt assumed as a result of the Transco Energy acquisition. Interest capitalized increased \$8.5 million, or 143 percent, due primarily to increased expenditures for gathering and processing facilities and Northwest Pipeline's expansion projects. Investing income increased \$44.3 million, or 89 percent, due primarily to interest earned on the invested portion of the cash proceeds from the sale of Williams' network services operations in addition to an \$11 million increase in the dividend from Texasgulf Inc. The 1995 loss on sales of assets results from the sale of the 15 percent interest in Texasgulf Inc. The 1994 gain on sales of assets results from the sale of 3,461,500 limited partner common units in Northern Border Partners, L.P. The 1995 write-off of project costs results from the cancellation of an underground coal gasification project in Wyoming (see Note 6). Other income (expense) - net in 1995 includes approximately \$10 million of minority interest expense associated with the Transco Energy merger, \$4 million of dividends on subsidiary preferred stock and \$4 million of losses on sales of receivables, partially offset by \$11 million of equity allowance for funds used during construction (AFUDC). Other income (expense) - net in 1994 includes a redit for \$4.8 million from the reversal of previously accrued liabilities associated with certain Royalty Trust contingencies that expired. Also included is approximately \$4 million of expense related to Statement of Financial Accounting Standards (FAS) No. 112, "Employers' Accounting for Postemployment Benefits," which relates to postemployment benefits being paid to employees of companies previously sold.

The \$20.3 million, or 25 percent, increase in the provision for income taxes on continuing operations is primarily a result of higher pre-tax income, partially offset by a lower effective income tax rate resulting from \$29.8 million of previously unrecognized tax benefits realized as a result of the sale of Texasgulf Inc. (see Note 6) and an \$8 million income tax benefit resulting from settlements with taxing authorities. The effective income tax rate in 1995 is significantly less than the federal statutory rate, due primarily to the previously unrecognized tax benefits realized as a result of the sale of the investment in Texasgulf Inc., income tax credits from coal-seam gas production and recognition of an \$8 million income tax benefit resulting from settlements with taxing authorities, partially offset by the effects of state income taxes and minority interest. The effective income tax rate in 1994 is lower than the statutory rate primarily because of income tax credits from coal-seam gas production, partially offset by state income taxes (see Note 7).

On January 5, 1995, Williams sold its network services operations to LDDS Communications, Inc. for \$2.5 billion in cash. The sale yielded an after-tax gain of approximately \$1 billion, which is reported as income from discontinued operations. Prior period operating results for the network services operations are reported as discontinued operations (see Note 3).

The 1994 extraordinary loss results from the early extinguishment of debt (see Note 8).

Preferred stock dividends increased \$6.5 million as a result of the May 1995 issuance of 2.5 million shares of Williams \$3.50 cumulative convertible preferred stock in exchange for Transco Energy's \$3.50 cumulative convertible preferred stock (see Note 14) in addition to the \$3.5 million premium on exchange of \$2.21 cumulative preferred stock for debentures.

Financial Condition and Liquidity

Liquidity

Williams considers its liquidity to come from two sources: internal liquidity, consisting of available cash investments, and external liquidity, consisting of borrowing capacity from available bank-credit facilities,

which can be utilized without limitation under existing loan covenants. At December 31, 1996, Williams had access to \$550 million of liquidity representing the available portion of its \$1 billion bank-credit facility plus cash-equivalent investments. This compares with liquidity of \$656 million at December 31, 1995, and \$495 million at December 31, 1994. The decrease in 1996 is due primarily to additional borrowings under the bank-credit facility, partially offset by a \$200 million increase in the capacity of the bank-credit facility (see Note 13). At December 31, 1996, \$200 million in current debt obligations have been classified as non-current obligations based on Williams' intent and ability to refinance on a long-term basis. At December 31, 1996, the amount available on the \$1 billion bank-credit facility of \$500 million is sufficient to complete these refinancings. In January 1997, Williams filed a \$200 million shelf registration statement with the Securities and Exchange Commission to issue trust preferred securities. During 1996, Williams Holdings of Delaware, Inc., a wholly-owned subsidiary of Williams, filed a \$400 million shelf registration statement with the Securities and Exchange Commission and issued \$250 million of debt securities. During 1993, Williams filed a \$300 million shelf registration statement with the Securities and Exchange Commission, increasing the total amount available to \$400 million. The registration statement may be used to issue Williams common or preferred stock, preferred stock purchase rights, debt securities, warrants to purchase Williams common stock or warrants to purchase debt securities. In addition, short-term uncommitted bank lines are utilized in managing liquidity. Williams believes any additional financing arrangements can be obtained on reasonable terms if required.

Williams had a net working-capital deficit of \$309 million at December 31, 1996, compared with \$715 million at December 31, 1995. Williams manages its borrowings to keep cash and cash equivalents at a minimum and has relied on bank-credit facilities to provide flexibility for its cash needs. As a result, it historically has reported negative working capital. The decrease in the working-capital deficit at December 31, 1996, as compared to the prior year-end is primarily a result of higher 1996 levels of receivables.

Terms of certain borrowing agreements limit transfer of funds to Williams from its subsidiaries. The restrictions have not impeded, nor are they expected to impede, Williams' ability to meet its cash requirements in the future.

During 1997, Williams expects to finance capital expenditures, investments and working-capital requirements through cash generated from operations and the use of the available portion of its \$1 billion bank-credit facility, short-term uncommitted bank lines or public debt/equity offerings.

Operating Activities

Cash provided by operating activities was: 1996 — \$710 million; 1995 — \$829 million; and 1994 — \$349 million. The increase in receivables, commodity trading assets and accounts payable is due primarily to increased trading activities by Williams Energy Group's Merchant Services. The increase in property, plant and equipment primarily reflects the consolidation of Kern River following the January 1996 acquisition (see Note 2).

Financing Activities

Net cash provided (used) by financing activities was: 1996 — \$734 million; 1995 — (\$1.4) billion; and 1994 — \$50 million. Long-term debt proceeds, net of principal payments were \$609 million during 1996. Long-term debt principal payments net of debt proceeds were \$610 million during 1995. Long-term debt proceeds, net of principal payments and early extinguishment of debt were \$24 million during 1994. The increase in net new borrowings during 1996 was primarily to fund capital expenditures, investments and acquisitions of businesses.

The majority of the proceeds from issuance of common stock in 1996 resulted from Williams benefit plan stock purchases and exercise of stock options under Williams' stock plan. The 1995 proceeds from issuance of common stock includes \$46.2 million from the sale of 1.8 million shares of Williams common stock, held by a subsidiary of Williams and previously classified as treasury stock in the Consolidated Balance Sheet, in addition to Williams benefit plan stock purchases and exercise of stock options under Williams' stock plans.

The majority of the proceeds from issuance of common stock in 1994 resulted from Williams benefit plan stock purchases and exercise of stock options under Williams' stock plan (see Note 14).

The 1996 purchases of Williams' treasury stock include 957,750 shares of common stock on the open market for \$31 million. The Williams board of directors has authorized up to \$800 million of such purchases. During 1994, Williams and one of its subsidiaries purchased 20.7 million shares of Williams common stock on the open market for \$407 million. Substantially all of the purchases were financed with a \$400 million bank-credit agreement. In 1995, the outstanding amounts under the credit agreement were repaid from the proceeds of the sale of Williams' network services operations, and the credit agreement was terminated. Williams also repurchased 96,300, 142,800 and 258,800 shares of its \$2.21 cumulative preferred stock on the open market for \$3 million, \$4 million and \$6 million in 1996, 1995 and 1994, respectively.

On January 18, 1995, Williams acquired 60 percent of Transco Energy's outstanding common stock in a cash tender offer for \$430.5 million. Williams acquired the remaining 40 percent of Transco Energy's outstanding common stock on May 1, 1995, through a merger by exchanging the remaining Transco Energy common stock for approximately 15.6 million shares of Williams common stock valued at \$334 million. Additionally, \$2.3 billion in preferred stock and debt obligations of Transco Energy was assumed by Williams. Williams made payments to retire and/or terminate approximately \$700 million of Transco Energy's borrowings, preferred stock, interest-rate swaps and sale of receivable facilities. As part of the merger, Williams exchanged Transco Energy's \$3.50 cumulative convertible preferred stock for Williams' \$3.50 cumulative convertible preferred stock (see Note 2). The cash portion of the acquisition and the payments to retire and/or terminate various Transco Energy facilities were financed with the proceeds from the sale of Williams' network services operations (see Note 3).

During 1995, Williams exchanged 2.8 million shares of its \$2.21 cumulative preferred stock with a carrying value of \$69 million for 9.6 percent debentures with a fair value of \$72.5 million (see Note 14).

Long-term debt at December 31, 1996, was \$4.4 b.llion, compared with \$2.9 billion at December 31, 1995, and \$1.3 billion at December 31, 1994. At December 31, 1996, \$200 million in current debt obligations have been classified as non-current obligations based on Williams' intent and ability to refinance on a long-term basis. The 1996 increase in long-term debt is due primarily to the \$643 million outstanding debt assumed with the acquisition of Kern River (see Note 2), \$300 million in additional borrowings under the \$1 billion bank-credit facility and \$250 million of debt issued by Williams Holdings. The 1995 increase in long-term debt is due primarily to the \$2 billion outstanding debt assumed as a result of the Transco Energy acquisition. The long-term debt to debt-plus-equity ratio was \$6.1 percent at year-end, compared with 47.4 percent and 46.5 percent at December 31, 1995 and 1994, respectively. Included in long-term debt due within one year at December 31, 1994, was \$350 million outstanding under Williams' revolving credit facility.

See Note 8 for information regarding early extinguishment of debt by Williams and one of its subsidiaries during 1994.

Investing Activities

Net cash provided (used) by investing activities was: 1996 — (\$1.4) billion; 1995 — \$585 million; and 1994 — (\$427) million. Capital expenditures of pipeline subsidiaries, primarily to expand and modernize systems, were \$441 million in 1996; \$445 million in 1995; and \$96 million in 1994. Expenditures in 1996 include Transcontinental Gas Pipe Line and Northwest Pipeline's expansions; and expenditures in 1994 include Northwest Pipeline's additional mainline expansion. Capital expenditures of Williams Energy Group, primarily to expand and modernize gathering and processing facilities, were \$292 million in 1996; \$336 million in 1995; and \$214 million in 1994. Capital expenditures for discontinued operations were \$143 million in 1994, primarily to expand and enhance Williams' network services operations network. Budgeted capital expenditures and investments for 1997 are approximately \$1.7 billion, primarily to expand pipeline systems, gathering and processing facilities and the fiber-optic network.

On January 16, 1996, Williams acquired the remaining interest in Kern River for \$206 million in cash (see Note 2). In addition, during 1996 Williams acquired various communications technology businesses totaling \$165 million in cash. During 1995, in addition to the Transco Energy acquisition (see Note 2), Williams acquired the Gas Company of New Mexico's natural gas gathering and processing assets in the San Juan and Permian basins for \$154 million (including approximately 10 percent of which was immediately sold to a third party) and Pekin Energy Co., the nation's second largest ethanol producer, for \$167 million in cash.

During 1996, Williams received proceeds of \$23 million from the sale of certain communications rights. During 1995, Williams received proceeds of \$124 million from the sale of its 15 percent interest in Texasgulf Inc. During 1994, Williams received net proceeds of \$80 million from the sale of limited partner units in Northern Border Partners, L.P. (see Note 6).

Effects of Inflation

Williams has experienced increased costs in recent years due to the effects of inflation. However, approximately 62 percent of Williams' property, plant and equipment was acquired or constructed during 1996 and 1995. A substantial portion of Williams' property, plant and equipment is subject to regulation, which limits recovery to historical cost. While Williams believes it will be allowed the opportunity to earn a return based on the actual cost incurred to replace existing assets, competition or other market factors may limit the ability to recover such increased costs.

Environmental

Williams is a participant in certain environmental activities in various stages involving assessment studies, cleanup operations and/or remedial processes. The sites, some of which are not currently owned by Williams (see Note 17), are being monitored by Williams, other potentially responsible parties, the U.S. Environmental Protection Agency (EPA), or other governmental authorities in a coordinated effort. In addition, Williams maintains an active monitoring program for its continued remediation and cleanup of certain sites connected with its refined products pipeline activities. Williams has both joint and several liability in some of these activities and sole responsibility in others. Current estimates of the most likely costs of such cleanup activities, after payments by other parties, are approximately \$80 million, all of which is accrued at December 31, 1996. Williams expects to seek recovery of approximately \$42 million of the accrued costs through future natural gas transmission rates. Williams will fund these costs from operations and/or available bank-credit facilities. The actual costs incurred will depend on the final amount, type and extent of contamination discovered at these sites, the final cleanup standards mandated by the EPA or other governmental authorities, and other factors.

Item 8. Financial Statements and Supplementary Data

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REPORT OF INDEPENDENT AUDITORS

To The Stockholders of The Williams Companies, Inc.

We have audited the accompanying consolidated balance sheet of The Williams Companies, Inc. as of December 31, 1996 and 1995, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 1996. Our audits also included the financial statement schedule listed in the Index at Item 14(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Williams Companies, Inc. at December 31, 1996 and 1995, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 1996, in conformity with generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, whon considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

ERNST & YOUNG LLP

Tulsa, Oklahoma February 10, 1997

THE WILLIAMS COMPANIES, INC. CONSOLIDATED STATEMENT OF INCOME

	Years	ber 31,		
	1996	1995*	1994*	
		Millions, exce r-share amoun		
Revenues:				
Williams Interstate Natural Gas Systems (Note 4)	\$1,675.2	\$1,431.1	\$ 469.8	
Williams Energy Group (Note 4)	1,453.1	1,077.4	966.5	
Williams Communications Group	711.3	538.9	416.6	
Other	48.0	17.4		
Intercompany eliminations (Note 16)	(356.4)	(209.1)	(101.8)	
Total revenues	3,531.2	2,855.7	1,751.1	
Profit-center costs and expenses:				
Costs and operating expenses	2,064.1	1,700.7	1,187.7	
Selling, general and administrative expenses	585.5	488.8	229.2	
Other income — net	(19.8)	(4.5)	(8.1)	
Total profit-center costs and expenses	2,629.8	2,185.0	1,408.8	
Operating profit:				
Williams Interstate Natural Gas Systems (Note 4)	562.4	389.7	152.9	
Williams Energy Group (Note 4)	332.3	257.5	181.8	
Williams Communications Group	6.6	25.0	7.6	
Other	1	(1.5)	_	
Total operating profit	901.4	670.7	342.3	
General corporate expenses	(41.4)	(37.7)	(28.0)	
Interest accrued	(359.9)	(277.9)	(145.8)	
Interest capitalized	6.9	14.5	6.0	
Investing income (Note 5)	18.8	93.9	49.6	
Gain (loss) on sales of assets (Note 6)	15.7	(12.6)	22.7	
Write-off of project costs (Note 6)	_	(41.4)	-	
Other income (expense) — net	3.9	(8.1)	(.2)	
Income from continuing operations before income taxes	545.4	401.4	246.6	
Provision for income taxes (Note 7)	183.1	102.0	81.7	
Income from continuing operations	362.3	299.4	164.9	
Income from discontinued operations (Note 3)		1,018.8	94.0	
Income before extraordinary loss	362.3	1,318.2	258.9	
Extraordinary loss (Note 8)	_	_	(12.2)	
Net income	362.3	1,318.2	246.7	
Preferred stock dividends (Note 14)	10.4	15.3	8.8	
Income applicable to common stock	\$ 351.9	\$1,302.9	\$ 237.9	
The state of the s			-	

^{*} Certain amounts have been restated or reclassified as described in Note 1.

THE WILLIAMS COMPANIES, INC. CONSOLIDATED STATEMENT OF INCOME (Concluded)

	Years Ended December 31		
	1996	1995*	1994*
Primary earnings per common and common-equivalent share (Notes 1, 3 and 8):			
Income from continuing operations	\$2.17	\$1.86 6.65	\$1.02
Income before extraordinary loss Extraordinary loss		8.51	(.08)
Net income	\$2.17	\$8.51	\$1.55
Fully diluted earnings per common and common-equivalent share (Notes 1, 3 and 8):			
Income from continuing operations	\$2.14	\$1.84	\$1.02
Income from discontinued operations		6.48	61
Income before extraordinary loss	2.14	8.32	1.63
Extraordinary loss			(.08)
Net income	\$2.14	\$8.32	\$1.55

[·] Amounts have been restated as described in Note 1.

THE WILLIAMS COMPANIES, INC. CONSOLIDATED BALANCE SHEET

ASSETS

	Dece	mber 31,
	1996	1995
		millions, except e amounts)
Current assets:		
Cash and cash equivalents		\$ 90.4
Receivables less allowance of \$9.7 (\$11.3 in 1995)		525.0
Transportation and exchange gas receivable	. 117.7	152.3
Inventories (Note 10)	204.6	189.0
Commodity trading assets (Note 15)	147.2	66.8
Deferred income taxes (Note 7)	199.5	213.9
Other		140.3
Total current assets		1,377,7
Investments (Note 5)	F. W. P. C.	307.6
Property, plant and equipment — net (Note 11)	9.386.3	8.014.7
Other assets and deferred charges		861.2
Total assets		\$10,561.2
Total assets	\$12,410.0	\$10,501.2
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable (Note 13)		s —
Accounts payable (Note 12)		472.0
Transportation and exchange gas payable		127.8
Accrued liabilities (Note 12)		1,086.2
Commodity trading liabilities (Note 15)		87.2
Long-term debt due within one year (Note 13)	59.6	319.9
Total current liabilities	2,199.3	2,093.1
Long-term debt (Note 13)		2,874.0
Deferred income taxes (Note 7)	1,626.6	1,568.2
Other liabilities		838.8
Contingent liabilities and commitments (Note 17)		
Stockholders' equity (Note 14): Preferred stock, \$1 par value, 30,000,000 shares authorized, 3,241,552 shares		
issued in 1996 and 3,739,452 shares issued in 1995	161.0	173.5
Common stock, \$1 par value, 240,000,000 shares authorized, 160,214,163	161.0	173.3
shares issued in 1996 and 158,006,922 shares issued in 1995	160.2	158.0
		998.4
Capital in excess of par value		0.0000
Retained earnings		1,915.6
Unamortized deferred compensation		(2.3
Less treasury stock (at cost), 2,737,337 shares of common stock in 1996.	3,486.2	3,243.2
2.359,804 shares of common stock in 1995 and 401,600 shares of preferred		
stock in 1995		(56.1)
Total stockholders' equity	THE RESIDENCE AND ADDRESS OF THE PARTY.	3,187.1
		\$10,561.2

^{*} Reclassified to conform to current classifications.

THE WILLIAMS COMPANIES, INC. CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

	Preferred Stock	Common Stock	Capital in Excess of Par Value	Retained Earnings	Unamortized Deferred Compensation	Treasury Stock	Total
	1000		(Dollars in mi	llions, except	per-share amounts)		
Balance, December 31, 1993	\$100.0	\$154.6	\$ 907.6	\$ 563.7	\$(1.9)	s -	\$1,724.0
Net income — 1994	W-2	-		246.7		_	246.7
Cash dividends —				(85.1)		_	(85.1)
Common stock (\$.56 per share) Preferred stock (Note 14)	- 4	=		(8.8)		_	(8.8)
Issuance of shares — 2,394,613 common	_	2.0	29.4	-	(1.3)	8.1	38.2
Purchase of treasury stock — 20,685,133 common		_	7-1	-	_	(406.8)	(406.8)
258,800 preferred		-		-		(6.4)	(6.4)
Tax benefit of stock-based awards Amortization of deferred			1.8				1.8
compensation	-	-	_	-	1.9		1.9
Balance, December 31, 1994	100.0	156.6	938.8	716.5	(1.3)	(405.1)	1,505.5
Net income — 1995	-	=		1,318.2	out N =	_	1,318.2
Common stock (\$.72 per share)	-	_		(107.2)	1	-	(107.2)
Preferred stock (Note 14)	-	-	-	(11.9)	_	-	(11.9)
19.319.881 common	1	1.4	58.3	_	(1.7)	352.7	410.7
2,500,000 preferred	142.5	-	_	-	_	-	142.5
Exchange of shares for debentures —							1000000
2,760,548 preferred (Note 14)	(69.0)	-	(3.5)	_	_	-	(72.5)
Purchase of treasury stock — 142,800 preferred	130	The state of		_		(3.7)	(3.7)
Tax benefit of stock-based awards		_	4.8		-	_	4.8
Amortization of deferred				_	7	_	.7
compensation	172.5	150.0	000.4	10166	(2.2)	(56.1)	3,187.1
Balance, December 31, 1995	173.5	158.0	998.4	1,915.6	(2.3)	(50.1)	362.3
Net income — 1996 Cash dividends —		_	-	362.3	_	_	
Common stock (\$.94 per share)	-		-	(148.0)	-		(148.0)
Preferred stock (Note 14)	_	-		(10.4)	· —	77	(10.4)
Issuance of shares — 2,787,458 common	_ =	2.2	33.6	_	(.6)	12.0	47.2
Purchase of treasury stock — 957,750 common	-	-	_		-	(31.3)	(31.3)
96,300 preferred	_	_		_	_	(2.0)	(2.0)
Retirement of treasury stock — 497,900 preferred	(12.5)	_	(.3)	-	_	12.8	_
Tax benefit of stock-based awards	-	-	16.0	_	-	-	16.0
Amortization of deferred compensation					.7		7
Balance, December 31, 1996	\$161.0	\$160.2	\$1,047.7	\$2,119.5	\$(2.2)	\$ (65.2)	\$3,421.0
Danist, Developer 21, 1270 11111	2101.0				nohuman'	meanforcement *	Background

Note: Certain amounts have been restated to reflect the December 30, 1996 three-for-two common stock split and distribution.

THE WILLIAMS COMPANIES, INC. CONSOLIDATED STATEMENT OF CASH FLOWS

	Years F	Years Ended December	
	1996	1995	1994
Complex Automotive Complex Com		(Millions)	-
Operating Activities:			
Adjustments to reconcile to cash provided from operations:	\$ 362.3	\$ 1,318.2	\$ 246.7
Discontinued operations	_	(1.018.8)	(94.0)
Extraordinary loss	-	_	12.2
Depreciation and depletion	411.4	369.4	150.3
Provision for deferred income taxes	72.4	125.4	25.8
Write-off of project costs	9.00	41.4	_
(Gain) loss on dispositions of property, plant and equipment	(30.7)	(2.1)	.9
(Gain) loss on sale of assets		12.6	(22.7)
Changes in receivables sold	(13.1)	55.9	
Changes in receivables	(214.2)	33.2	(175.0)
Changes in inventories	(16.1)	11.9	10.2
Changes in other current assets	3.8	1.1.	13.8*
Changes in accounts payable	204.0	(6.5)	20.7
Changes in accrued liabilities	(24.9)	(33.4)*	
Changes in current commodity trading assets and liabilities	(29.7)	28.1*	(15.9)*
Changes in non-current commodity trading assets and liabilities Other, including changes in non-current assets and liabilities	(37.7)	(82.1)*	(2.4)
	THE RESERVE THE PARTY OF THE PA	(25.6)	1.7
Net cash provided by continuing operations Net cash provided by discontinued operations	710.4	828.7	179.6
Net cash provided by operating activities		828.7	349.0
Financing Activities:			
Proceeds from notes payable	356.8	116.8	507.0
Payments of notes payable	(87.3)	(623.8)	
Proceeds from long-term debt	1,996.7	399.0	480.0
Payments of long-term debt	(1,387.7)	(1,009.4)	(456.5)
Proceeds from issuance of common stock	54.3	78.1	26.4
Purchases of treasury stock	(33.9)	(3.7)	(413.2)
Dividends paid	(158.4)	(119.1)	(93.9)
Subsidiary preferred stock redemptions	_	(193.7)	_
Other — net	(6.3)	(3.5)	-
Net cash provided (used) by financing activities	734.2	(1,359.3)	49.8
Investing Activities: Property, plant and equipment:			
Capital expenditures:			
Continuing operations	(818.9)	(827.5)	(325.5)
Discontinued operations	_	_	(142.8)
Proceeds from dispositions	60.2	28.2	1.6
Acquisition of businesses, aet of cash acquired	(366.2)	(858.9)	(56.5)
Proceeds from sales of businesses ,	-	2,588.3	-
Income tax and other payments related to discontinued operations	(261.7)	(350.4)	(1.5)
Proceeds from sales of assets	23.0	125.1	80.6
Purchase of investments/advances to affiliates	(76.9)	(49.7)	(3.3)
Purchase of note receivable Other — net	20.8	(75.1)	20.4
Net cash provided (used) by investing activities		584.9	(427.0)
Increase (decrease) in cash and cash equivalents	24.9	54.3	(28.2)
Cash and cash equivalents at beginning of year	90.4	36.1	64.3
Cash and cash equivalents at end of year	The second second second	\$ 90.4	\$ 36.1
		-	-0.1

[·] Reclassified to conform to current classifications.

Note 1 — Summary of significant accounting policies

Nature of operations

Operations of The Williams Companies, Inc. (Williams) are located in the United States and are organized into three operating groups as follows: Williams Interstate Natural Gas Systems, which is comprised of five interstate natural gas pipelines located in the eastern, midsouth, Gulf Coast, midwest and northwest regions; Williams Energy Group, which is comprised of natural gas gathering and processing facilities in the Rocky Mountain, midwest and Gulf Coast regions, energy commodity trading and price-risk management activities throughout the United States, a petroleum products pipeline in the midwest region, and hydrocarbon exploration and production activities in the Rocky Mountain and Gulf Coast regions; and Williams Communications Group, which includes Williams' national data, voice, video and Internet communication products and network integration services and fiber-optic and satellite multimedia transmission services. Additional information about these businesses is contained throughout the following notes.

Basis of presentation

Williams Energy Group is comprised of four units. Field Services includes Williams' natural gas gathering and processing activities previously reported in Williams Field Services Group. Merchant Services includes Williams' energy commodity trading and price-risk management activities previously reported in Williams Energy Services. Certain natural gas and natural gas liquids marketing operations formerly reported in Williams Field Services Group are also included in Merchant Services. Petroleum Services includes Williams' interstate petroleum products pipeline, ethanol-producing facilities and petroleum terminals previously reported in Williams Pipe Line. Exploration and Production includes exploration for and production of hydrocarbons previously reported as a component of Williams Field Services Group. Williams Communications Group is the combination of WilTel and WilTech Group, previously reported separately. Revenues and operating profit amounts for 1995 and 1994 have been reclassified to conform to current year classifications.

Revenues and operating profit amounts include the operating results of Kern River Gas Transmission Company (Kern River) since the January 16, 1996, acquisition by Williams of the remaining interest (see Note 2). Prior to this acquisition, Williams accounted for its 50 percent ownership in Kern River using the equity method of accounting, with its share of equity earnings recorded in investing income.

Revenues and operating profit amounts include the operating results of Transco Energy Company (Transco Energ.) since its January 18, 1995, acquisition by Williams (see Note 2). The transportation operations from Transco Energy's two interstate natural gas pipelines are reported separately within Williams Interstate Natural Gas Systems. Transco Energy's gas gathering operations are included in Field Services, and its gas marketing operations are included in Merchant Services.

Principles of consolidation

The consolidated financial statements include the accounts of Williams and its majority-owned subsidiaries. Companies in which Williams and its subsidiaries own 20 percent to 50 percent of the voting common stock, or otherwise exercise sufficient influence over operating and financial policies of the company, are accounted for under the equity method.

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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.

Cash and cash equivalents

Cash and cash equivalents include demand and time deposits, certificates of deposit and other marketable securities with maturities of three months or less when acquired.

Transportation and exchange gas imbalances

In the course of providing transportation services to customers, the natural gas pipelines may receive different quantities of gas from shippers than the quantities delivered on behalf of those shippers. Additionally, the pipelines and other Williams subsidiaries transport gas on various pipeline systems which may deliver different quantities of gas on their behalf than the quantities of gas received. These transactions result in gas transportation and exchange imbalance receivables and payables which are recovered or repaid in cash or through the receipt or delivery of gas in the future. Settlement of imbalances requires agreement between the pipelines and shippers as to allocations of volumes to specific transportation contracts and timing of delivery of gas based on operational conditions. Transcontinental Gas Pipe Line's imbalances predating August 1, 1991, are being recovered or repaid in cash or through the receipt or delivery of gas upon agreements of allocation.

Inventory valuation

Inventories are stated at cost, which is not in excess of market, except for those held by Merchant Services, which are primarily stated at market. Inventories of natural gas are determined using the last-in, first-out (LIFO) method by Transcontinental Gas Pipe Line and the average-cost method by other subsidiaries. Except for Merchant Services, inventories of petroleum products are determined using average cost. The cost of materials and supplies inventories is determined using the first-in, first-out method (FIFO) by Williams Communications Group and principally using the average-cost method by other subsidiaries.

Property, plant and equipment

Property, plant and equipment is recorded at cost. Depreciation is provided primarily on the straight-line method over estimated useful lives. Gains or losses from the ordinary sale or retirement of property, plant and equipment for regulated pipeline subsidiaries are credited or charged to accumulated depreciation; other gains or losses are recorded in net income.

Treasury stock

Treasury stock purchases are accounted for under the cost method whereby the entire cost of the acquired stock is recorded as treasury stock. Gains and losses on the subsequent reissuance of shares are credited or charged to capital in excess of par value using the average-cost method.

Revenue recognition

Revenues generally are recorded when services have been performed or products have been delivered. Petroleum Services bills customers when products are shipped and defers the estimated revenues for shipments in transit. Williams interstate natural gas pipelines recognize revenues based upon contractual terms and the related transportation volumes through month-end. These pipelines are subject to Federal Energy Regulatory Commission (FERC) regulations and, accordingly, certain revenues are subject to possible refunds pending final FERC orders. Williams records rate refund accruals based on management's estimate of the expected outcome of these proceedings.

Commodity price-risk management activities

Merchant Services has trading operations that enter into energy-related financial instruments (forward contracts, futures contracts, option contracts and swap agreements) to provide price-risk management services

THE WILLIAMS COMPANIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

to its third-party customers. This operation also enters into short- and long-term energy-related purchase and sale commitments as part of its trading business. All of these investments and commitments are valued at market and are recorded in commodity trading assets, other assets and deferred charges, commodity trading liabilities and other liabilities in the Consolidated Balance Sheet. The change in unrealized market gains and losses is recognized in income currently and is recorded as revenues in the Consolidated Statement of Income. Such market values are subject to change in the near term and reflect management's best estimate of market prices considering various factors including closing exchange and over-the-counter quotations, the terms of the contract, credit considerations, time value and volatility factors underlying the positions. Merchant Services reports its trading operations sales of natural gas, refined products and crude oil net of the related costs to purchase such items, consistent with mark-to-market accounting for such trading activities.

Certain Merchant Services' natural gas, natural gas liquids and refined product marketing revenues previously reported in Williams Field Services Group and/or Williams Pipe Line were not included in trading operations and therefore are not reported net of related costs to purchase such items.

Other Williams operations enter into energy-related financial instruments (primarily futures contracts, option contracts and swap agreements) to hedge against market price fluctuations of certain commodity inventories and sales and purchase commitments. Unrealized and realized gains and losses on these hedge contracts are deferred and recognized in income when the related hedged item is recognized. These contracts are regularly evaluated to determine that there is a high correlation between changes in the market value of the hedge contract and fair value of the hedged item.

Capitalization of interest

Williams capitalizes interest on major projects during construction. Interest is capitalized on borrowed funds and, where regulation by the FERC exists, on internally generated funds. The rates used by regulated companies are calculated in accordance with FERC rules. Rates used by unregulated companies approximate the average interest rate on related debt. Interest capitalized on internally generated funds is included in other income (expense) — net.

Employee stock-based awards

Employee stock-based awards are accounted for under Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations. Williams' fixed plan common stock options do not result in compensation expense, because the exercise price of the stock options equals the market price of the underlying stock on the date of grant.

Income taxes

Williams includes the operations of its subsidiaries in its consolidated federal income tax return. Deferred income taxes are computed using the liability method and are provided on all temporary differences between the financial basis and the tax basis of Williams' assets and liabilities.

Earnings per share

Primary earnings per share are based on the sum of the average number of common shares outstanding and common-share equivalents resulting from stock options and deferred shares. Fully diluted earnings per share for 1996 and 1995 assumes conversion of the \$3.50 convertible preferred stock into common stock effective May 1, 1995. Shares used in determination of primary earnings per share are as follows (in thousands): 1996—162,118; 1995—153,069; and 1994—153,704. Shares used in determination of fully diluted earnings per share are as follows (in thousands): 1996—168,199; 1995—157,280; and 1994—

153,753. The number of shares for 1995 and 1994 have been restated to reflect the effect of a three-for-two common stock split and distribution (see Note 14).

Note 2 - Acquisitions

On January 16, 1996, Williams acquired the remaining interest in Kern River for \$206 million in cash. The acquisition was accounted for as a purchase, and the acquired assets and liabilities have been recorded based on an allocation of the purchase price, with substantially all of the cost in excess of Kern River's historical carrying value allocated to property, plant and equipment.

On January 18, 1995, Williams acquired 60 percent of Transco Energy's outstanding common stock in a cash tender offer for \$430.5 million. Williams acquired the remaining 40 percent of Transco Energy's outstanding common stock on May 1, 1995, through a merger by exchanging the remaining Transco Energy common stock for approximately 15.6 million shares of Williams common stock valued at \$334 million. The acquisition was accounted for as a purchase with 60 percent of Transco Energy's results of operations included in Williams' Consolidated Statement of Income for the period January 18, 1995, through April 30, 1995, and 100 percent included beginning May 1, 1995. The purchase price, including transaction fees and other related costs, was approximately \$800 million, excluding \$2.3 billion in preferred stock and debt obligations of Transco Energy. The acquired assets and liabilities were recorded based on an allocation of the purchase price with substantially all of the cost in excess of Transco Energy's historical carrying amounts allocated to property, plant and equipment of the two interstate natural gas pipeline systems. The cash portion of the acquisition was financed with the proceeds from the sale of Williams' network services operations (see Note 3).

Transco Energy was engaged primarily in the natural gas pipeline and natural gas marketing businesses. Williams has sold substantially all of Transco Energy's coal operations, coalbed methane properties and certain pipeline and gathering operations. Results of operations and changes in the carrying amount of these businesses during the holding period and from the ultimate dispositions are reflected in the purchase price and are not material.

In connection with the acquisition, Williams made payments to retire and/or terminate approximately \$700 million of Transco Energy borrowings, preferred stock, interest-rate swaps and sale of receivable facilities. As a part of the merger, Williams exchanged Transco Energy's \$3.50 preferred stock for Williams' \$3.50 preferred stock.

The following unaudited pro forma information combines the results of operations of Williams and Transco Energy as if the purchase of 100 percent of Transco Energy occurred January 1, 1994.

	Unac	dited
	1995	1994
	(Million per-share	s, except amounts)
Revenues	\$2,916.4	\$2,660.3
Income from continuing operations	314.4	191.0
Income before extraordinary loss	1,333.2	285.0
Net income	1,333.2	272.8
Primary earnings per share:		19/10/000
Income from continuing operations	1.95	1.18
Income before extraordinary loss	8.61	1.79
Net income	8.61	1.71
Fully diluted earnings per share:		
Income from continuing operations	1.93	1.18
Income before extraordinary loss	8.41	1.79
Net income	8.41	1.71
	2000	

Pro forma financial information is not necessarily indicative of results of operations that would have occurred if the acquisition had occurred on January 1, 1994, or of future results of operations of the combined companies.

Note 3 - Discontinued operations

On January 5, 1995, Williams sold its network services operations to LDDS Communications, Inc. for \$2.5 billion in cash. The sale yielded a gain of \$1 billion (net of income taxes of approximately \$732 million) which is reported as income from discontinued operations. Operating results for 1994 for the network services operations are reported as discontinued operations. Under the terms of the agreement, Williams retained Williams Telecommunications Systems, Inc., a national telecommunications equipment supplier and service company, and Vyvx, Inc., which operates a national video network specializing in broadcast television applications and satellite transmission. These operations are included in Williams Communications Group.

Summarized operating results of discontinued operations for 1994 were as follows:

	(Millions)
Revenues	\$921.8
Operating profit	163.1
Provision for income taxes	60.9
Income from discontinued operations	94.0

Note 4 - Revenues and operating profit

Revenues and operating profit of Williams Interstate Natural Gas Systems and Williams Energy Group for the years ended December 31, 1996, 1995 and 1994, are as follows:

	Resenues		Operating profi		le	
	1996	1995*	1994*	1996	1995*	1994*
			(Millio	ns)		
Williams Interstate Natural Gas Systems:				Sec.		
Northwest Pipeline	\$ 269.7	\$ 255.2	\$238.5	\$124.9	\$115.7	\$104.1
Williams Natural Gas	178.4	174.3	231.3	44.8	45.0	48.8
Transcontinental Gas Pipe Line	760.4	725.3	_	194.6	165.0	-
Texas Gas Transmission	306.1	276.3	_	85.1	64.0	-
Kern River Gas Transmission	160.6	-		113.0		
	\$1,675.2	\$1,431.1	\$469.8	\$562.4	\$389.7	\$152.9
Williams Energy Group:						
Field Services	\$ 616.3	\$ 532.9	\$328.7	\$187.4	\$161.0	\$112.9
Merchant Services	261.1	153.5	381.7	66.4	33.2	3.4
Petroleum Services	493.3	328.1	216.9	75.7	69.2	51.9
Exploration and Production	the state of the s	62.9	39.2	2.8	(5.9)	13.6
	\$1,453.1	\$1,077.4	\$966.5	\$332.3	\$257.5	\$181.8

Certain amounts have been reclassified as described in Note 1.

Note 5 - Investing activities

	1996	1995
	(Mill	ions)
Investments: Kern River Gas Transmission Company, at equity (50%) (see Note 2) Other, at equity Cost	\$ — 105.9 84.7	\$178.6 84.2 44.8
	\$190.6	\$307.6

At December 31, 1996, certain equity investments, with a carrying value of \$36 million, have a market value of \$126 million.

In 1996, Williams acquired the remaining interest in Kern River (see Note 2). Summarized financial position and results of operations for Kern River for 1995 and 1994 are presented below.

	1995	1994
	(Mil	lions)
Current assets Non-current assets, principally natural gas transmission plant Current liabilities Long-term debt Other non-current liabilities	\$ 55.4 994.5 (47.3) - (620.5) (124.1)	\$ 98.3 1,026.3 (86.9) (643.2) (109.5)
Partners' equity	\$ 258.0	\$ 285.0
Revenues Costs and expenses Net income	\$ 187.0 65.7 38.0	\$ 179.0 54.9 38.1

Investing income from continuing operations:

	1996	1995	1994
		(Millions)	
Interest	\$11.1	\$37.2	\$ 5.5
Dividends	1.6	16.1	4.5
Equity earnings	6.1	40.6	39.6
	\$18.8	\$93.9	\$49.6

Dividends and distributions received from companies carried on an equity basis were \$7 million in 1996; \$44 million in 1995; and \$43 million in 1994.

Note 6 - Asset sales and write-off of project costs

In the fourth quarter of 1996, Williams recognized a pre-tax gain of \$15.7 million from the sale of certain communication rights for approximately \$38 million.

In 1995, the development of a commercial coal gasification venture in south-central Wyoming was canceled, resulting in a \$41.4 million pre-tax charge. This amount includes what management believes to be a reasonable estimate of future costs of \$4 million to reclaim the site, of which approximately \$3 million remains to be incurred over a five-year period. Williams continues to perform the reclamation of the site in coordination with various governmental agencies and expects to receive necessary environmental releases and approvals upon completion of the reclamatica.

In 1995, Williams sold its 15 percent interest in Texasgulf Inc. for approximately \$124 million in cash, which resulted in an after-tax gain of approximately \$16 million because of previously unrecognized tax benefits included in the provision for income taxes.

In 1994, Williams sold 3,461,500 limited partner common units in Northern Border Partners, L.P. Net proceeds from the sale were approximately \$80 million, and the sale resulted in a pre-tax gain of \$22.7 million. As a result of the sale, Williams' original 12.25 percent interest in Northern Border partnerships has been reduced to 3.2 percent.

Note 7 - Provision for income taxes

The provision (credit) for income taxes from continuing operations includes:

	1996	1995	1994
		(Millions)	
Current:			
Federal	\$ 96.3	\$(26.5)	\$45.8
State	14.4	3.1	10.1
	110.7	(23.4)	55.9
Deferred:			
Federal	61.9	114.2	23.7
State	10.5	11.2	2.1
	72.4	125.4	25.8
Total provision	\$183.1	\$102.0	\$81.7

Reconciliations from the provision for income taxes from continuing operations at the statutory rate to the provision for income taxes are as follows:

A STATE OF THE STA	1996	1995	1994
		(Millions)	
Provision at statutory rate	\$190.9	\$140.5	\$ 86.3
Increases (reductions) in taxes resulting from:	HERSHED	100414	1000
State income taxes	16.1	13.5	8.0
Income tax credits	(19.0)	(18.7)	(14.9)
Decrease in valuation allowance for deferred tax assets	-	(29.8)	
Reversal of prior tax accruals		(8.0)	-
Other — net	(4.9)	4.5	2.3
Provision for income taxes	\$183.1	\$102.0	\$ 81.7
		-	

Significant components of deferred tax liabilities and assets as of December 31 are as follows:

	1996	1995
	(Mil	lions)
Deferred tax liabilities:		2101-20170001
Property, plant and equipment	\$1,748.3	\$1,669.2
Investments	119.8	96.9
Other	230.6	299.1*
Total deferred tax liabilities	2,098.7	2,065.2
Deferred tax assets:		12/2/21
Deferred revenues	29.1	23.5
Investments	31.1	31.3
Rate refunds	111.4	70.7
Accrued liabilities	183.2	226.4
Minimum tax credits	86.8	93.9
Other	230.0	265.1*
Total deferred tax assets	671.6	710.9
	A STATE OF THE PARTY OF THE PARTY.	description and the factors and
Net deferred tax liabilities	\$1,427.1	\$1,354.3

[·] Reclassified to conform to current classifications.

A valuation allowance for deferred tax assets decreased \$23.4 million during 1995.

Cash payments for income taxes (net of refunds, were \$395 million, \$339 million and \$107 million in 1996, 1995 and 1994, respectively.

Note 8 - Extraordinary loss

The extraordinary loss in 1994 resulted from early extinguishment of debt. Williams and one of its subsidiaries paid \$316.7 million to redeem higher interest rate debt for a \$12.2 million net loss (net of a \$7.7 million benefit for income taxes).

Note 9 - Employee benefit plans

Pensions

Williams maintains non-contributory defined-benefit pension plans covering the majority of its employees. Benefits are based on years of service and average final compensation. Pension costs are funded to satisfy minimum requirements prescribed by the Employee Retirement Income Security Act of 1974.

Net pension expense consists of the following:

	1996	1995	1994
		(Millions)	
Service cost for benefits earned during the year	\$ 30.3	\$ 19.5	\$13.9
Interest cost on projected benefit obligation	43.9	40.1	21.8
Actual return on plan assets	(100.6)	(120.3)	3.1
Amortization and deferrals	61.3	82.0	(24.2)
Net pension expense	\$ 34.9	\$ 21.3	\$14.6

Net pension expense increased in 1996 from 1995 as a result of a decrease in the discount rate from 8½ percent to 7¼ percent and an increase in the number of plan participants. Net pension expense increased in 1995 from 1994 as a result of the Transco Energy plans' participants.

The following table presents the funded status of the plans:

	1996	1995
	(Mill	lions)
Actuarial present value of benefit obligations:		
Vested benefits	\$407	\$422
Non-vested benefits	37	21
Accumulated benefit obligations	444	443
Effect of projected salary increases	167	137
Projected benefit obligations	611	580
Assets at market value	637	550
Assets (in excess of) less than projected benefit obligations		30
Unrecognized net gain	37	_
Unrecognized prior-service cost	(8)	(11)
Unrecognized transition asset	3	4
Pension liability		\$ 23

The discount rate used to measure the present value of benefit obligations is 7½ percent (7¼ percent in 1995); the assumed rate of increase in future compensation levels is 5 percent; and the expected long-term rate of return on assets is 10 percent. Plan assets consist primarily of commingled funds and assets held in a master trust. The master trust is comprised primarily of domestic and foreign common and preferred stocks, United States government securities, corporate bonds and commercial paper.

Williams has retained all liabilities and obligations for service of its network services operations' plan participants up to the date of sale (see Note 3).

Postretirement benefits other than pensions

Williams sponsors health care plans that provide postretirement medical benefits to retired Williams employees who were employed full time, hired prior to January 1, 1992 (January 1, 1996, for Transco Energy employees) and have met certain other requirements.

The plans provide for retiree contributions and contain other cost-sharing features such as deductibles and coinsurance. The accounting for the plans anticipates future cost-sharing changes to the written plans that are consistent with Williams' expressed intent to increase the retiree contribution rate annually, generally in line with health care cost increases, except for certain retirees whose premiums are fixed. A portion of the cost has been funded in trusts by Williams' FERC-regulated natural gas pipeline subsidiaries to the extent recovery from customers can be achieved. Plan assets consist of assets held in two master trusts and money market funds. One of the master trusts was previously described, and the other consists primarily of domestic and foreign common stocks, government bonds and commercial paper.

Net postretirement benefit expense consists of the following:

The partition of the second se	1996	(Millions)	1994
Service cost for benefits earned during the year	\$ 6.4 22.7	\$ 7.4 23.9	\$ 3.9 7.8
Actual return on plan assets	(16.4)	(17.9)	(.6) 5.1
Amortization of unrecognized transition obligation	_19.7	23.1	1
Net postretirement benefit expense	\$ 37.4	\$ 41.5	\$16.3

Net postretirement benefit expense increased \$26 million in 1995 from 1994 for the Transco Energy participants.

The following table presents the funded status of the plans:

	1996	1995
	(Milli	ions)
Actuarial present value of postretirement benefit obligation: Retirees	\$200 26	\$227 24
Other active plan participants	89	85
Accumulated postretirement benefit obligation	315	336 124
Assets less than accumulated postretirement benefit obligation	160	212 25
Unrecognized prior-service credit (cost)	. 1	(6) _(71)
Postretirement benefit liability	\$156	\$160

During fourth-quarter 1996, the plans were amended, effective January 1, 1997, to increase the costsharing provisions. This amendment decreased the accumulated postretirement benefit obligation approximately \$10 million. The amount of postretirement benefit costs deferred as a regulatory asset at December 31, 1996 and 1995, is \$118 million and \$133 million, respectively, and is expected to be recovered through rates over approximately 15 years.

THE WILLIAMS COMPANIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

The discount rate used to measure the present value of benefit obligations is 7½ percent (7¼ percent in 1995). The expected long-term rate of return on plan assets is 10 percent (6 percent after taxes). The annual assumed rate of increase in the health care cost trend rate for 1997 is 9 to 10 percent, systematically decreasing to 5 percent by 2004. The health care cost trend rate assumption has a significant effect on the amounts reported. Increasing the assumed health care cost trend rate by 1 percent in each year would increase the aggregate of the service and interest cost components of postretirement benefit expense for the year ended December 31, 1996, by \$4 million and the accumulated postretirement benefit obligation as of December 31, 1996, by \$27 million.

Other

Williams maintains various defined-contribution plans covering substantially all employees. Company contributions are based on employees' compensation and, in part, match employee contributions. Company contributions are invested primarily in Williams common stock. Williams' contributions to these plans were \$23 million in 1996, \$19 million in 1995 and \$14 million in 1994. Contributions to these plans made by discontinued operations were \$3 million in 1994.

Note 10 - Inventories

1995*
llions)
\$ 21.4
6.0
2.2
16.5
23.7
28.2
87.8
3.2
\$189.0

^{*}Certain amounts have been reclassified as described in Note 1.

Inventories valued on the LIFO method at December 31, 1996 and 1995, approximate current average cost.

Note 11 - Property, plant and equipment

1996	1995*
(Millions)	
\$ 1,447.9	\$ 1,403.5
787.4	761.6
	2,756.7
	917.3
	-
2,188.3	2,099.9
5.4	4.3
1.073.1	1,023.3
17.00	225.0
	145.9
	141.2
	9,478.7
	(1,464.0)
\$ 9,386.3	\$ 8,014.7
	\$ 1,447.9 787.4 3,095.7 958.9 990.5 2,188.3 5.4 1,073.1 255.1 257.3

[·] Certain amounts have been reclassified as described in Note 1.

Commitments for construction and acquisition of property, plant and equipment are approximately \$268 million at December 31, 1996.

Effective January 1, 1996, Williams adopted Statement of Financial Accounting Standards No. 121, "Accounting for Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of." Adoption of the standard had no effect on Williams' financial position or results of operations.

Note 12 - Accounts payable and accrued liabilities

Under Williams' cash-management system, certain subsidiaries' cash accounts reflect credit balances to the extent checks written have not been presented for payment. The amounts of these credit balances included in accounts payable are \$95 million at December 31, 1996, and \$136 million at December 31, 1995.

	1996	1995
	(Mi	llions)
Accrued liabilities:		
Rate refunds	\$305.1	\$ 180.6
Employee costs	178.1	135.9
Interest	95.2	72.9
Income taxes payable		371.6
Taxes other than income taxes	66.2	51.2
		274.0*
	\$975.3	\$1,086.2

[·] Reclassified to conform to current classifications.

THE WILLIAMS COMPANIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 13 - Debt, leases and banking arrangements

Notes payable

Williams has entered into various short-term credit agreements with amounts outstanding totaling \$269.5 million at December 31, 1996. The weighted average interest rate on the outstanding short-term borrowings at December 31, 1996, was 7.85 percent.

Debt

	Weighted average	Decem	her 31,
그 그 이번 경에 가장 내가 있다면 하는데 이 때문 그 때문에 다 그 그것	interest rate*	1996	1995
		(Mill	lions)
The Williams Companies, Inc.			
Revolving credit loans	%	s -	\$ 50.0
Debentures, 8.875% 10.25%, payable 2012, 2020, 2021 and 2025	9.6	587.5	587.7
Notes, 7.5% - 9.625%, payable 1998 through 2001	8.8	817.5	842.4
Northwest Pipeline			
Debentures, 7.125% — 10.65%, payable through 2025	9.0	360.0	369.2
Adjustable rate notes, payable through 2002	9.0	10.0	11.7
Williams Natural Gas			
Variable rate notes, payable 1999	8.2	130.0	130.0
Transcontinental Gas Pipe Line			
Debentures, 7.25% and 9.125%, payable 1998 through 2026	8.1	352.4	153.0
Debentures, 7.08%, payable 2026 (subject to debtholder redemption in			
2001)	7.1	200.0	-
Notes, 8.125% and 8.875%, payable 1997 and 2002	8.5	227.7	381.1
Adjustable rate notes	-	-	125.1
Texas Gas Transmission			
Notes, 9.625% and 8.625%, payable 1997 and 2004	9.0	253.6	255.9
Kern River Gas Transmission			
Notes, 6.42% and 6.72%, payable through 2001	6.6	617.7	-
Williams Holdings of Delaware			
Revolving credit loans	6.0	500.0	150.0
Debentures, 6.25%, payable 2006	4.7	248.8	-
Williams Pipe Line			
Notes, 8.95% and 9.78%, payable through 2001	9.4	100.0	110.0
Williams Energy Ventures			
Adjustable rate notes, payable through 2002	8.1	25.6	21.0
Other, payable through 1999	7.7	5.7	6.8
		4,436.5	3,193.9
Current portion of long-term debt		(59.6)	(319.9)
		\$4,376.9	\$2,874.0
		34,370.9	34,074.0

^{*}At December 31, 1996, including the effects of interest-rate swaps.

In December 1996, Williams increased the amounts available under its existing credit agreement to \$1 billion from \$800 million. Under the credit agreement, Northwest Pipeline, Transcontinental Gas Pipe Line, Texas Gas Transmission, Williams Pipe Line and Williams Holdings of Delaware, Inc. (Williams

THE WILLIAMS COMPANIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Holdings) have access to various amounts of the facility, while Williams (parent) has access to all unborrowed amounts. Interest rates vary with current market conditions.

For financial statement reporting purposes at December 31, 1996, \$200 million in current debt obligations have been classified as non-current obligations based on Williams' intent and ability to refinance on a long-term basis. At December 31, 1996, the amount available on the \$1 billion credit agreement of \$500 million is sufficient to complete these refinancings.

During March 1996, the Kern River floating-rate bank loan was refinanced through the issuance of 6.42 percent and 6.72 percent fixed-rate notes. Interest-rate swap agreements entered into by Kern River in prior years, which converted floating-rate debt to fixed-rate debt, remain outstanding. Concurrent with the refinancing, Kern River entered into additional interest-rate swap agreements where Kern River receives a fixed interest rate and pays a floating interest rate. The interest-rate swaps are recorded at market with an offsetting deferral of costs as a regulatory asset that is expected to be recovered in transportation rates. The effect is to adjust the new fixed-rate notes to an effective interest rate of 8.5 percent.

In January 1996, Williams Holdings issued \$250 million of 6.25 percent debentures due 2006. In April 1996, Williams Holdings entered into an interest-rate swap agreement, which effectively converted its 6.25 percent fixed-rate debentures to floating-rate debt (4.66 percent at December 31, 1996). The difference between the fixed and variable rate is included in interest expense.

In conjunction with the issuance of \$130 million of variable rate debt by Williams Natural Gas in November 1994, Williams entered into an interest-rate swap agreement under which Williams pays a 7.78 percent fixed rate in exchange for a variable rate (5.5 percent at December 31, 1996). The difference between the fixed and variable rate is included in interest expense.

Aggregate minimum maturities and sinking-fund requirements, excluding lease payments, for each of the next five years are as follows:

		(Millions)
997	\$ 59	
1998		377
1999		355
2000		252
2001		1,610

Cash payments for interest (net of amounts capitalized) related to continuing operations are as follows: 1996 — \$347 million; 1995 — \$266 million; and 1994 — \$143 million. Cash payments for interest (net of amounts capitalized) related to discontinued operations are \$6 million in 1994.

Leases

Future minimum annual rentals under non-cancelable operating leases related to continuing operations are \$59 million in 1997, \$54 million in 1998, \$48 million in 1999, \$42 million in 2000, \$40 million in 2001 and \$161 million thereafter.

Total rent expense from continuing operations was \$78 million in 1996 and 1995 and \$26 million in 1994.

Total rent expense from discontinued operations was \$70 million in 1994.

Note 14 - Stockholders' equity

On November 21, 1996, the board of directors of Williams declared a three-for-two common stock split and distribution; 53.8 million shares were issued on December 30, 1996. All references in the financial

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

statements and notes to the number of common shares outstanding and per-share amounts reflect the effect of the split.

In the third quarter of 1996, the Williams' board of directors authorized the open-market purchase of up to \$800 million of Williams common stock. At December 31, 1996, 957,750 shares had been purchased at a total cost of approximately \$31 million.

In connection with the 1995 merger with Transco Energy, Williams exchanged all of Transco Energy's outstanding \$3.50 cumulative convertible preferred stock for 2.5 million shares of Williams' \$3.50 cumulative convertible preferred stock. These shares are redeemable by Williams beginning in November 1999, at an initial price of \$51.40 per share. Each share of \$3.50 preferred stock is convertible at the option of the holder into 2.34375 shares of Williams common stock. Dividends per share of \$3.50 and \$2.33 were recorded during 1996 and 1995, respectively.

During 1995, Williams exchanged 2.8 million shares of its \$2.21 cumulative preferred stock with a carrying value of \$69 million for 9.6 percent debentures with a fair value of \$72.5 million. The difference in the fair value of the new securities and the carrying value of the preferred stock exchanged is recorded as a decrease in capital in excess of par value. This amount did not impact net income, but is included in preferred stock dividends on the Consolidated Statement of Income and in the computation of earnings per share. The 741,552 outstanding shares of \$2.21 cumulative preferred stock are redeemable by Williams at a price of \$25 beginning in September 1997. Dividends per share of \$2.21 were recorded each year during 1996, 1995 and 1994.

In January 1996, the board of directors adopted a Stockholder Rights Plan (the Rights Plan) to replace its existing rights plan, which expired on Fabruary 6, 1996. Under the Rights Plan, each outstanding share of common stock has two-thirds of a preferred stock purchase right attached. Under certain conditions, each right may be exercised to purchase, at an exercise price of \$140 (subject to adjustment), one two-hundredth of a share of junior participating preferred stock. The rights may be exercised only if an Acquiring Person acquires (or obtains the right to acquire) 15 percent or more of Williams common stock; or commences an offer for 15 percent or more of Williams common stock; or the board of directors determines an Adverse Person has become the owner of 10 percent or more of Williams common stock. The rights, which do not have voting rights, expire in 2006 and may be redeemed at a price of \$.01 per right prior to their expiration, or within a specified period of time after the occurrence of certain events. In the event a person becomes the owner of more than 15 percent of Williams common stock or the board of directors determines that a person is an Adverse Person, each holder of a right (except an Acquiring Person or an Adverse Person) shall have the right to receive, upon exercise, common stock having a value equal to two times the exercise price of the right. In the event Williams is engaged in a merger, business combination or 50 percent or more of Williams' assets, cash flow or earnings power is sold or transferred, each holder of a right (except an Acquiring Person or an Adverse Person) shall have the right to receive, upon exercise, common stock of the acquiring company having a value equal to two times the exercise price of the right.

Williams has several plans providing for common-stock-based awards to employees and to non-employee directors. The plans permit the granting of various types of awards including, but not limited to, stock options, stock-appreciation rights, restricted stock and deferred stock. Awards may be granted for no consideration other than prior and future services. The purchase price per share for stock options and stock-appreciation rights may not be less than the market price of the underlying stock on the date of grant. Stock options generally become exercisable after five years, subject to accelerated vesting if certain future stock prices are achieved. Stock options expire 10 years after grant. At December 31, 1996, 19,618,842 shares of common stock were reserved for issuance pursuant to existing and future stock awards, of which 7,813,768 shares were available for future grants (4,048,199 at December 31, 1995).

THE WILLIAMS COMPANIES, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following summary reflects stock option activity and related information for 1996:

	Options	Weighted Average Exercise Price
Outstanding — December 31, 1995	7,868,900	\$20.03
Granted	4,101,144	33.41
Exercised	(2,035,349)	18.28
Canceled	(104,516)	42.02
Outstanding — December 31, 1996	9,830,179	25.70
Exercisable — December 31, 1996	5,461,482	\$20.57
Weighted average grant date fair value of options granted during the year	\$7.84	

The following summary provides information about stock options outstanding and exercisable at December 31, 1996:

		Stock Options Outst	Stock Options Exercisable			
Range of Exercise Prices	Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Options	Weighted Average Price Exercise	
\$ 9.25 to \$28.38	5,634,510	\$19.29	7.2 years	5,255,664	\$19.35	
\$32.25 to \$98.67	4,195,669	34.32	9.3 years	205,818	51.76	
Total	9,830,179	\$25.70	8.1 years	5,461,482	\$20.57	

The fair value of the stock options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted average assumptions: expected life of the stock options of five years; volatility of the expected market price of Williams common stock of 24 percent; risk-free interest rate of 6.2 percent; and a dividend yield of 3 percent.

Williams granted 195,376, 98,168 and 191,559 deferred shares in 1996, 1995 and 1994, respectively. The weighted average grant date fair value of the shares issued in 1996 is \$31.55. Deferred shares are valued at the date of award and are generally charged to expense in the year of award. Williams issued 109,516, 105,183 and 67,947 previously deferred shares in 1996, 1995 and 1994, respectively. Williams also issued 19,650, 82,950 and 67,200 shares of restricted stock in 1996, 1995 and 1994, respectively. The weighted average grant date fair value of the shares issued in 1996 is \$29.50. Restricted stock is valued on the issuance date and the related expense is amortized over varying periods of three to 10 years.

Pro forms net income and earnings per share, assuming 'Villiams had applied the fair-value method of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" in measuring compensation cost beginning with 1995 employee stock based awards, are as follows:

	1996		1	995
	Pro forma	Reported	Pro forma	Reported
Net income (millions)	\$359.9	\$362.3	\$1,306.1	\$1,318.2
Primary	\$ 2.16	\$ 2.17	\$ 8.45	\$ 8.51
Fully diluted	\$ 2.13	\$ 2.14	\$ 8.24	\$ 8.32

Pro forma amounts for 1995 reflect total compensation expense from the awards made in 1995 as these awards fully vested as a result of the accelerated vesting provisions. Since compensation expense from stock

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

options is recognized over the future years' vesting period, and additional awards generally are made each year, pro forma amounts for 1996 may not be representative of future years' amounts.

During November 1994, Williams entered into a deferred share agreement (the Agreement) in connection with the sale of its network services operations. Under the terms of the Agreement, Williams has approximately 1.6 million shares of Williams common stock remaining to distribute to key employees of the network services operations over various periods through 2002, less amounts necessary to meet minimum tax withholding requirements. Williams distributed 637,361, 471,608 and 409,643 shares during 1996, 1995 and 1994, respectively.

Note 15 - Financial instruments

Fair-value methods

The following methods and assumptions were used by Williams in estimating its fair-value disclosures for financial instruments:

Cash and cash equivalents and notes payable: The carrying amounts reported in the balance sheet approximate fair value due to the short-term maturity of these instruments.

Notes and other non-current receivables: For those notes with interest rates approximating market or maturities of less than three years, fair value is estimated to approximate historically recorded amounts. For those notes with maturities beyond three years and fixed interest rates, fair value is calculated using discounted cash flow analysis based on current market rates.

Investments — cost: Fair value is estimated to approximate historically recorded amounts as the operations underlying these investments are in their initial phases.

Long-term debt: The fair value of Williams' long-term debt is valued using indicative year-end traded bond market prices for publicly traded issues, while private debt is valued based on the prices of similar securities with similar terms and credit ratings. At December 31, 1996 and 1995, 69 percent and 85 percent, respectively, of Williams' long-term debt was publicly traded. Williams used the expertise of an outside investment banking firm to estimate the fair value of long-term debt.

Interest-rate swaps: Fair value is determined by discounting estimated future cash flows using forward interest rates implied by the year-end yield curve. Fair value was calculated by the financial institutions that are the counterparties to the swaps.

Energy-related trading and hedging: Includes forwards, futures, options, swaps and purchase and sales commitments. Fair value reflects management's best estimate of market prices considering various factors including closing exchange and over-the-counter quotations, the terms of the contract, credit considerations, time value and volatility factors underlying the positions.

THE WILLIAMS COMPANIES, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Carrying amounts and fair values of Williams' financial instruments

Asset (liability)

		19	96			19	95																																					
	Carrying Amount																														Fair Value													Fair Value
			7	(Mill	ions)																																							
Cash and cash equivalents	5	115.3	S	115.3	S	90.4	S	90.4																																				
Notes and other non-current receivables		27.4		27.4		25.7		25.8																																				
Investments — cost		71.2		71.2		31.3		31.3																																				
Notes payable		(269.5)		(269.5)																																								
Long-term debt, including current portion	(4,435.1)	(4,594.4)	(3,193.1)	1	(3,476.7)																																				
Interest-rate swaps		(54.8)		(63.7)		(.4)		(10.4)																																				
Energy-related trading:																																												
Assets		253.6		253.6		171.4		171.4																																				
Liabilities		(339.1)		(359.1)		(343.6)		(343.6)																																				
Energy-related hedging:																																												
Assets		.9		11.2		_		1.7																																				
Liabilities		(1.3)		(12.2)		-		(2.6)																																				

The preceding asset and liability amounts for energy-related hedging represent unrealized gains or losses and do not include the related deferred amounts.

The 1996 average fair value of the energy-related trading assets and liabilities is \$196 million and \$322 million, respectively. The 1995 average fair value of the energy-related trading assets and liabilities is \$97 million and \$181 million, respectively.

Williams has recorded liabilities of \$18 million and \$24 million at December 31, 1996 and 1995, respectively, for certain guarantees that represent the estimated fair value of these financial instruments.

Off-balance-sheet credit and market risk

Williams is a participant in the following transactions and arrangements that involve financial instruments that have off-balance-sheet risk of accounting loss. It is not practicable to estimate the fair value of these off-balance-sheet financial instruments because of their unusual nature and unique characteristics.

Williams sold certain receivables. The aggregate limit under revolving receivables facilities was \$135 million at December 31, 1996 and 1995. Williams received \$47 million of proceeds in 1996, \$196 million in 1995 and \$110 million in 1994. At December 31, 1996 and 1995, \$152 million and \$166 million of receivables had been sold, respectively, under the revolving receivables facilities and another arrangement. Based on amounts outstanding at December 31, 1996 and 1995, the maximum contractual credit loss under these arrangements is approximately \$28 million, but the likelihood of loss is remote. In January 1997, Williams expanded their revolving receivables facilities and sold \$200 million of receivables. The Financial Accounting Standards Board has issued a new accounting standard FAS No. 125, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," effective for transactions occurring after December 31, 1996. The adoption of this standard is not expected to impact Williams' consolidated results of operations, financial position or cash flows.

In connection with the sale of units in the Williams Coal Seam Gas Royalty Trust (Trust), Williams indemnified the Trust against losses from certain litigation (see Note 17) and guaranteed minimum gas prices through 1997. At December 31, 1996 and 1995, Williams has a recorded liability of \$5 million and \$10 million, respectively, for these items, representing the maximum amount for the first guarantee and an

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

estimate of the gas price exposure based on historical operating trends and an assessment of market conditions. While Williams' maximum exposure from this guarantee exceeds amounts accrued, it is not possible to determine such amount because it is dependent on future events.

In connection with the sale of Williams' network services operations, Williams has been indemnified by LDDS against any losses related to retained guarantees of \$158 million and \$180 million at December 31, 1996 and 1995, respectively, for lease rental obligations. LDDS has advised that it is negotiating with the guaranteed parties to remove Williams as guarantor.

Williams has issued other guarantees and letters of credit with off-balance-sheet risk that total approximately \$10 million and \$8 million at December 31, 1996 and 1995, respectively. Williams believes it will not have to perform under these agreements because the likelihood of default by the primary party is remote and/or because of certain indemnifications received from other third parties.

Commodity price-risk management services

Williams, through its Merchant Services group, provides price-risk management services associated with the energy industry to its customers. These services are provided through a variety of financial instruments, including forward contracts, futures contracts, option contracts, swap agreements and purchase and sale commitments. See Note 1 for a description of the accounting for these trading activities.

Merchant Services enters into forward contracts and purchase and sale commitments which involve physical delivery of an energy commodity. Prices under these contracts are both fixed and variable. Swap agreements call for Merchant Services to make payments to (or receive payments from) counterparties based upon the differential between a fixed and variable price or variable prices for different locations. The variable prices are generally based on either industry pricing publications or exchange quotations. Merchant Services buys and sells option contracts which giv: the buyer the right to exercise the options and receive the difference between a predetermined strike price and a market price at the date of exercise. The market prices used for natural-gas-related option contracts are generally exchange quotations. Merchant Services also enters into futures contracts, which are commitments to either purchase or sell a commodity at a future date for a specified price and are generally settled in cash, but may be settled through delivery of the underlying commodity. The market prices for futures contracts are based on exchange quotations.

Merchant Services manages risk from financial instruments by making various logistical commitments and manages profit margins through offsetting financial instruments. As a result, price movements can result in losses on certain contracts offset by gains on others.

Merchant Services takes an active role in managing and controlling market and counterparty risks and has established formal control procedures, which are reviewed on an ongoing basis. Merchant Services attempts to minimize credit-risk exposure to trading counterparties and brokers through formal credit policies and monitoring procedures. In the normal course of business, collateral is not required for financial instruments with credit risk.

The notional quantities for trading financial instruments at December 31, 1996, and December 31, 1995, are as follows:

	15	196	1995	
	Payor	Receiver	Payor	Receiver
Fixed price:				
Natural gas (TBtu)	1,066.6	1,196.8	873.2	847.3
Refined products and crude (MMBbls)	34.4	26.3	15.9	14.9
Variable price:				
Natural gas (TBtu)	1,584.9	1,123.8	1,841.2	1,517.2
Refined products and crude (MMBbls)		3.3	2.8	2.5

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The net cash flow requirement related to these contracts at December 31, 1996 and 1995, was \$117 million and \$215 million, respectively. At December 31, 1996, the cash flow requirements extend primarily through 2006.

In 1995, certain gas marketing operations of Merchant Services, along with gas marketing operations from Transco Energy, were combined with the commodity price-risk management and trading activities of Merchant Services. Such combination in 1995 involves managing the price and other business risks and opportunities of such physical gas trading activities and any related financial instruments previously accounted for as hedges in common-risk portfolios with Merchant Services' other financial instruments. These former marketing activities, consisting of buying and selling natural gas, through 1994 were reported on a "gross" basis in the Consolidated Statement of Income as revenues and profit-center costs. Concurrent with completing the combination of such activities with the commodity price-risk management operations in the third quarter of 1995, the related contract rights and obligations along with any related financial instruments, previously accounted for as hedges, were recorded in the Consolidated Balance Sheet on a current-market-value basis and the related income statement presentation was changed to a net basis. Such revenues reported on a gross basis through the first two quarters of 1995 were reclassified to a net basis concurrent with this change in the third quarter of 1995.

Following is a summary of Merchant Services' revenues:

	1996	1995	1994
Financial instrument and physical trading market gains - net	\$ 99.2	\$ 65.8	\$ 14.2
Gross marketing revenues	-	617.7 •	249.2
Gross marketing costs	-	(599.2)*	
Marketing activities not included in trading operations	161.9	67.7	118.0
Other	-	1.5	3
	\$261.1	\$ 153.5	\$381.7

^{*}Through June 30, 1995.

Concentration of credit risk

Williams' cash equivalents consist of high quality securities placed with various major financial institutions with high credit ratings. Williams' investment policy limits its credit exposure to any one financial institution.

At December 31, 1996 and 1995, approximately 69 percent and 62 percent, respectively, of receivables are for the sale or transportation of natural gas and related products or services. Approximately 23 percent and 27 percent of receivables at December 31, 1996 and 1995, respectively, are for telecommunications and related services. Natural gas customers include pipelines, distribution companies, producers, gas marketers and industrial users primarily located in the eastern, northwestern and midwestern United States. Telecommunications customers include numerous corporations. As a general policy, collateral is not required for receivables, but customers' financial condition and credit worthiness are evaluated regularly.

THE WILLIAMS COMPANIES, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 16 - Other financial information

Intercompany revenues (at prices that generally apply to sales to unaffiliated parties) are as follows:

	_	1996	996 1995* (Millions)		1994*	
Williams Interstate Natural Gas Systems:						
Northwest Pipeline	5	1.1	5	1.8	•	3.4
Williams Natural Gas		9.2		9.5	•	14.2
Transcontinental Gas Pipe Line		34.6		34.2		
Texas Gas Transmission		20.5		37.7		_
Williams Energy Group:				****		
Field Services		26.2		14.0		15.1
Merchant Services	1	30.7		62.2		22.0
Petroleum Services		67.7		44.6		28.6
Exploration and Production		57.1		4.9		18.1
Other		9.3		.2		.4
	100	56.4	\$2	09.1	\$1	01.8

^{*} Certain amounts have been reclassified as described in Note 1.

THE WILLIAMS COMPANIES, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

Information for business segments is as follows:

Information for business segments is as follows:						
- 1- 1- 1- 1- 1- 1- 1- 1- 1- 1- 1- 1- 1-	_	1996	-	illions)	_1	994*
				incoms,		
Identifiable assets at December 31:						
Williams Interstate Natural Gas Systems:		153.0		1.147.5	\$1	028.0
Northwest Pipeline	3 1	704.8		709.2		719.8
Williams Natural Gas		3,305.4	1.0	3,159.5		_
Transcontinental Gas Pipe Line		1,132.2		1,151.8		_
Texas Gas Transmission		.081.6		1,131.0		
Kern River Gas Transmission		0.160,1		-		
Williams Energy Group:		1,995.0		1.939.3		935.9
Field Services		839.1		438.2		114.6
Merchant Services		906.5		863.2		674.6
Petroleum Services				164.6		145.4
Exploration and Production		200.3		401.0		315.7
Williams Communications Group		670.6		10000		379.1
Investments		190.6		307.6		169.4
General corporate and other		238.8		279.3		
Discontinued operations	_		-	3400	-	743.6
Consolidated	\$1	2,418.8	\$1	0,561.2	\$5	,226.1
Additions to property, plant and equipment:						
Williams Interstate Natural Gas Systems:						
Northwest Pipeline	5	62.8	5	130.5	5	62.6
Williams Natural Gas		50.9		43.5		32.9
Transcontinental Gas Pipe Line		272.1		238.7		-
Texas Gas Transmission		50.1		32.1		-
Kern River Gas Transmission		4.7		-		-
Williams Engrey Group						
Field Services		205.7		232.1		150.0
Merchant Services		.6		.4		3.5
Petroleum Services		55.8		87.9		46.6
Exploration and Production		30.3		15.6		13.5
Williams Communications Group		66.9		32.4		12.9
General corporate and other		19.0		14.3		3.5
General corporate and other	S	818.9	s	827.5	5	325.5
Consolidated	-	010.7	i	02112	=	08010
Depreciation and depletion:						
Williams Interstate Natural Gas Systems:	•	43.2	S	34.9	5	33.9
Northwest Pipeline	3	27.5	,	27.3		27.2
Williams Natural Gas		113.7		109.1		
Transcontinental Gas Pipe Line		41.5		38.9		
Texas Gas Transmission				30.3		-
Kern River Gas Transmission		15.5		_		
Williams Energy Group:		94.7		100.4		37.1
Williams Field Services		.6		1.2		.5
Merchant Services		34.1		26.4		22.4
Petroleum Services		10.5		9.8		9.6
Exploration and Production				14.2		12.7
Williams Communications Group		21.3		7.2		6.9
General corporate and other	-	8.8	-	-	-	
Consolidated	<u>s</u>	411.4	\$	369.4	2	150.3

^{*} Certain amounts have been reclassified as described in Note 1.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Note 17 - Contingent liabilities and commitments

Rate and regulatory matters and related litigation

Williams interstate pipeline subsidiaries, including Williams Pipe Line, have various regulatory proceedings pending. As a result of rulings in certain of these proceedings, a portion of the revenues of these subsidiaries has been collected subject to refund. As to Williams Pipe Line, revenues collected subject to refund were \$251 million at December 31, 1996; it is not expected that the amount of any refunds ordered would be significant. Accordingly, no portion of these revenues has been reserved for refund. As to the other pipelines, see Note 12 for the amount of revenues reserved for potential refund as of December 31, 1996.

In 1992, the Federal Energy Regulatory Commission (FERC) issued Order 636, Order 636-A and Order 636-B. These orders, which were challenged in various respects by various parties in proceedings recently ruled on by the U.S. Court of Appeals for the D.C. Circuit, require interstate gas pipeline companies to change the manner in which they provide services. Kern River Gas Transmission implemented its restructuring on August 1, 1993; Williams Natural Gas implemented its restructuring on October 1, 1993; and Northwest Pipeline, Texas Gas and Transcontinental Gas Pipe Line implemented their restructurings on November 1, 1993. Certain aspects of four pipeline companies' restructuring are under appeal.

On July 16, 1996, the U.S. Court of Appeals for the D.C. Circuit issued an order which in part affirmed and in part remanded Order 636. However, the court stated that Order 636 would remain in effect until FERC issued a final order on remand after considering the remanded issues. With the issuance of this decision, the stay on the appeals of individual pipeline's restructuring cases will be lifted. The only appeal challenging Northwest Pipeline's restructuring has been dismissed.

Contract reformations and gas purchase deficiencies

As a result of FERC Order 636, which requires interstate gas pipelines to change the way they do business, each of the natural gas pipeline subsidiaries has undertaken the reformation or termination of its respective gas supply contracts. None of the pipelines has any significant pending supplier take-or-pay, ratable take or minimum take claims.

Current FERC policy associated with Orders 436 and 500 requires interstate gas pipelines to absorb some of the cost of reforming gas supply contracts before allowing any recovery through direct bill or surcharges to transportation as well as sales commodity rates. Under Orders 636, 636-A and 636-B, costs incurred to comply with these rules are permitted to be recovered in full, although 10 percent of such costs must be allocated to interruptible transportation service.

The previously mentioned July 16, 1996, D.C. Circuit Court of Appeals decision concerning Order 636 has remanded to FERC the issues of whether pipelines should absorb any portion of Order 636 transition costs and whether 10 percent of such costs should have been allocated to interruptible transportation services.

Pursuant to a stipulation and agreement approved by the FERC, Williams Natural Gas has made seven filings to direct bill take-or-pay and gas supply realignment costs. The first provided for the offset of certain amounts collected subject to refund against previous take-or-pay direct-billed amounts and, in addition, covered \$24 million in new costs. This filing was approved, and the final direct-billed amount, taking into consideration the offset, was \$15 million. The second filing covered \$18 million in gas supply realignment costs, and provided for an offset of \$3 million. The third filing covered \$6.5 million in gas supply realignment costs. The remaining filings covered additional costs of approximately \$15 million, which are similar in nature to the costs in the second filing. An intervenor has filed a protest seeking to have the Commission review the prudence of certain of the costs covered by these filings. On July 31, 1996, the administrative law judge issued an initial decision rejecting the intervenor's prudency challenge. As of December 31, 1996, this subsidiary had an accrual of \$75 million for its then-estimated remaining contract-reformation and gas supply realignment

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

costs. Williams Natural Gas will make additional filings under the applicable FERC orders to recover such further costs as may be incurred in the future. Williams Natural Gas has recorded a regulatory asset of approximately \$73 million for estimated future recovery of the foregoing costs.

In September 1995, Texas Gas received FERC approval of a settlement regarding Texas Gas' recovery of gas supply realignment costs. The settlement provides that Texas Gas will recover 100 percent of such costs up to \$50 million, will share in costs incurred between \$50 million and \$80 million, and will absorb any such costs above \$80 million. Through December 31, 1996, Texas Gas has paid approximately \$76 million and expects to pay no more than \$80 million for gas supply realignment costs, primarily as a result of contract terminations. Texas Gas has recovered approximately \$59 million, plus interest, in gas supply realignment costs and has recorded a regulatory asset of approximately \$9 million for the estimated future recovery of such costs, most of which will be collected from customers prior to December 31, 1997. Ninety percent of the cost recovery is collected through demand surcharges on Texas Gas' firm transportation rates; the remaining 10 percent is recoverable from interruptible transportation service.

The foregoing accruals are in accordance with Williams' accounting policies regarding the establishment of such accruals, which take into consideration estimated total exposure, as discounted and risk-weighted, as well as costs and other risks associated with the difference between the time costs are incurred and the time such costs are recovered from customers. The estimated portion of such costs recoverable from customers is deferred or recorded as a regulatory asset based on an estimate of expected recovery of the amounts allowed by FERC policy. While Williams believes that these accruals are adequate and the associated regulatory assets are appropriate, costs actually incurred and amounts actually recovered from customers will depend upon the outcome of various court and FERC proceedings, the success of settlement negotiations and various other factors, not all of which are presently foreseeable.

Environmental matters

Since 1989, Texas Gas and Transcontinental Gas Pipe Line have had studies under way to test certain of their facilities for the presence of toxic and hazardous substances to determine to what extent, if any, remediation may be necessary. Transcontinental Gas Pipe Line has responded to data requests regarding such potential contamination of certain of its sites. The costs of any such remediation will depend upon the scope of the remediation. At December 31, 1996, these subsidiaries had reserves totaling approximately \$29 million for these costs.

Certain Williams subsidiaries, including Texas Gas and Transcontinental Gas Pipe Line, have been identified as potentially responsible parties (PRP) at various Superfund and state waste disposal sites. Although no assurances can be given, Williams does not believe that the PRP status of these subsidiaries will have a material adverse effect on its financial position, results of operations or net cash flows.

Transcontinental Gas Pipe Line, Texas Gas and Williams Natural Gas have identified polychlorinated biphenyl (PCB) contamination in air compressor systems, soils and related properties at certain compressor station sites. Transcontinental Gas Pipe Line, Texas Gas and Williams Natural Gas have also been involved in negotiations with the U.S. Environmental Protection Agency (EPA) and state agencies to develop screening, sampling and cleanup programs. In addition, negotiations with certain environmental authorities and other programs concerning investigative and remedial actions relative to potential mercury contamination at certain gas metering sites have been commenced by Williams Natural Gas, Texas Gas and Transcontinental Gas Pipe Line. As of December 31, 1996, Williams Natural Gas had recorded a liability for approximately \$18 million, representing the current estimate of future environmental cleanup costs to be incurred over the next six to 10 years. The Field Services unit of Williams Energy Group has recorded an aggregate liability of approximately \$15 million, representing the current estimate of their future environmental and remediation costs, including approximately \$6 million relating to former Williams Natural Gas facilities. Texas Gas and Transcontinental Gas Pipe Line likewise have recorded liabilities for these costs which are included in the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

529 million reserve mentioned above. Actual costs incurred will depend on the actual number of contaminated sites identified, the actual amount and extent of contamination discovered, the final cleanup standards mandated by the EPA and other governmental authorities and other factors. Texas Gas, Transcontinental Gas Pipe Line and Williams Natural Gas have deferred these costs pending recovery as incurred through future rates and other means.

In connection with the 1987 sale of the assets of Agrico Chemical Company, Williams agreed to indemnify the purchaser for environmental cleanup costs resulting from certain conditions at specified locations, to the extent such costs exceed a specified amount. It appears certain that such costs will exceed this amount. At December 31, 1996, Williams had approximately \$10 million accrued for such excess costs. The actual costs incurred will depend on the actual amount and extent of contamination discovered, the final cleanup standards mandated by the EPA or other governmental authorities, and other factors.

A lawsuit was filed in May 1993, in a state court in Colorado in which certain claims have been made against various defendants, including Northwest Pipeline, contending that gas exploration and development activities in portions of the San Juan Basin have caused air, water and other contamination. The plaintiffs in the case sought certification of a plaintiff class. In June 1994, the lawsuit was dismissed for failure to join an indispensable party over which the state court had no jurisdiction. The Colorado Court of Appeals has affirmed the dismissal and remanded the case to Colorado district court for action consistent with the appeals court's decision. Since June 1994, eight individual lawsuits have been filed against Northwest Pipeline and others in U.S. District Court in Colorado, making essentially the same claims. Northwest Pipeline is vigorously defending these lawsuits.

Other legal matters

In 1991, the Southern Ute Indian Tribe (the Tribe) filed a lawsuit against Williams Production, a wholly owned subsidiary of Williams, and other gas producers in the San Juan Basin area, alleging that certain coal strata were reserved by the United States for the benefit of the Tribe and that the extraction of coal-seam gas from the coal strata was wrongful. The Tribe seeks compensation for the value of the coal-seam gas. The Tribe also seeks an order transferring to the Tribe ownership of all of the defendants' equipment and facilities utilized in the extraction of the coal-seam gas. In September 1994, the court granted summary judgment in favor of the defendants and the Tribe lodged an interlocutory appeal with the U.S. Court of Appeals for the Tenth Circuit. Williams Production agreed to indemnify the Williams Coal Seam Gas Royalty Trust (Trust) against any losses that may arise in respect of certain properties subject to the lawsuit. In addition, if the Tribe is successful in showing that Williams Production has no rights in the coal-seam gas, Williams Production has agreed to pay to the Trust for distribution to then-current unitholders, an amount representing a return of a portion of the original purchase price paid for the units. While Williams believes that such a payment is not probable, it has reserved a portion of the proceeds from the sale of the units in the Trust.

In October 1990, Dakota Gasification Company (Dakota), the owner of the Great Plains Coal Gasification Plant (Plant), filed suit in the U.S. District Court in North Dakota against Transcontinental Gas Pipe Line and three other pipeline companies alleging that the pipeline companies had not complied with their respective obligations under certain gas purchase and gas transportation contracts. In September 1992, Dakota and the Department of Justice on behalf of the Department of Energy filed an amended complaint adding as defendants in the suit, Transco Energy Company, Transco Coal Gas Company and all of the other partners in the partnership that originally constructed the Plant and each of the parent companies of these entities. Dakota and the Department of Justice sought declaratory and injunctive relief and the recovery of damages, alleging that the four pipeline defendants underpaid for gas, collectively, as of June 30, 1992, by more than \$232 million plus interest and for additional damages for transportation services and costs and expenses including attorneys' fees. By order dated December 18, 1996, the FERC approved a settlement of the

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

litigation. No party to the FERC proceeding has sought review of this order. The final settlement terms went into effect February 1, 1997, which will allow Transcontinental Gas Pipe Line to recover its cost.

In connection with agreements to resolve take-or-pay and other contract claims and to amend gas purchase contracts, Transcontinental Gas Pipe Line and Texas Gas each entered into certain settlements with producers, which may require the indemnification of certain claims for additional royalties which the producers may be required to pay as a result of such settlements. As a result of such settlements, Transcontinental Gas Pipe Line and Texas Gas were named as defendants in, respectively, six and two lawsuits. Six of the eight lawsuits have been settled for cash payments aggregating approximately \$9 million, all of which have previously been accrued, and of which approximately \$3 million is recoverable as transition costs under Order 636. Damages, including interest, of approximately \$29 million have been asserted in the remaining cases. Producers have received and may receive other demands, which could result in additional claims. Indemnification for royalties will depend on, among other things, the specific lease provisions between the producer and the lessor and the terms of the settlement between the producer and either Transcontinental Gas Pipe Line or Texas Gas. Texas Gas may file to recover 75 percent of any such additional amounts it may be required to pay pursuant to indemnities for royalties under the provisions of Order 528.

In November 1994, Continental Energy Associates Limited Partnership (the Partnership) filed a voluntary petition under Chapter 11 of the Bankruptcy Code with the U.S. Bankruptcy Court, Middle District of Pennsylvania. The Partnership owns a cogeneration facility in Hazelton, Pennsylvania (the Facility). Hazelton Fuel Management Company (HFMC), a subsidiary of Transco Energy, formerly supplied natural gas and fuel oil to the Facility. As of December 31, 1996, HFMC had current outstanding receivables from the Partnership of approximately \$20 million, all of which have been reserved. The Partnership recently negotiated settlements of its power purchase agreements with two electric utilities. The settlements have been approved by the Bankruptcy Court and Pennsylvania Public Utility Commission. The time for appealing the Pennsylvania Public Utility Commission approval of the settlements expires on February 23, 1997. Assuming no appeals are filed the settlements will become binding. A Plan of Reorganization (the Plan) acceptable to all parties has been negotiated and drafted. The Plan is contingent upon the power purchase agreement settlements being approved. It is anticipated the Plan will be filed with the Bankruptcy Court for approval on or before February 28, 1997. Under the Plan, all litigation involving HFMC will be fully settled, and a net payment in some amount to HFMC is anticipated under the Plan. It is not possible to predict with certainty the amount of such a payment.

On July 18, 1996, an individual filed a lawsuit in the U.S. District Court for the District of Columbia against 70 natural gas pipelines and other gas purchasers or former gas purchasers. All of Williams' natural gas pipeline subsidiaries are named as defendants in the lawsuit. The plaintiff claims, on behalf of the United States under the False Claims Act, that the pipelines have incorrectly measured the heating value or volume of gas purchased by the defendants. The plaintiff claims that the United States has lost royalty payments as a result of these practices. The pipelines are vigorously defending against these claims.

In addition to the foregoing, various other proceedings are pending against Williams or its subsidiaries which are incidental to their operations.

Summary

While no assurances may be given, Williams does not believe that the ultimate resolution of the foregoing matters, taken as a whole and after consideration of amounts accrued, insurance coverage, recovery from customers or other indemnification arrangements, will have a materially adverse effect upon Williams' future financial position, results of operations and cash flow requirements.

QUARTERLY FINANCIAL DATA (Unaudited)

Summarized quarterly financial data are as follows (millions, except per-share amounts). Per-share amounts have been restated to reflect the effect of the three-for-two common stock split and distribution (see Note 14).

1996	First Quarter	Second Quarter	Third Quarter	Fourth Querter
Revenues	\$ 893.7	\$837.5	\$842.2	\$957.8
Costs and operating expenses	499.4	493.9	509.3	561.5
Net income	104.9	80.4	71.0	106.0
Primary earnings per common and common-			7.785	
equivalent share	.63	.48	.42	.64
Fully diluted earnings per common and common-				
equivalent share	.62	.47	.42	.63
1995				
Revenues	\$ 642.4	\$663.9	\$712.4	\$837.0
Costs and operating expenses	351.1	400.1	438.9	510.6
Net income	1,088.9	83.3	68.5	77.5
Primary earnings per common and common-				
equivalent share	7.71	.52	.39	.47
Fully diluted earnings per common and common-				
equivalent share	7.70	.52	.39	.46

The sum of earnings per share for the four quarters may not equal the total earnings per share for the year due to changes in the average number of common shares outstanding.

Second-quarter 1996 net income includes recognition of favorable income tax adjustments totaling \$10 million related to research credits and previously provided deferred income taxes on certain regulated capital projects. Third-quarter 1996 net income includes approximately \$6 million, net of federal income tax effect, from the effects of state income tax adjustments related to 1995.

First-quarter 1995 net income includes the after-tax gain of \$1 billion on the sale of Williams' network services operations (see Note 3 of Notes to Consolidated Financial Statements). The second quarter of 1995 includes a \$16 million after-tax gain from the sale of Williams' 15 percent interest in Texasgulf Inc. (see Note 6 of Notes to Consolidated Financial Statements) and an \$8 million income tax benefit resulting from settlements with taxing authorities. Northwest Pipeline's third-quarter 1995 operating profit includes the approximate \$11 million net favorable effect of two reserve accrual adjustments. In third-quarter 1995, Field Services recorded \$20 million of income from the favorable resolution of contingency issues involving previously regulated gathering and processing assets. In third-quarter 1995, Exploration and Production recorded an \$8 million loss accrual for a future minimum price natural gas purchase commitment.

Selected comparative fourth-quarter data are as follows (millions, except per-share amounts). Certain 1995 amounts have been restated and/or reclassified as described in Note 1 of Notes to Consolidated Financial Statements.

	1996	1995
Operating profit (loss):		
Williams Interstate Natural Gas Systems:		V20022747
Northwest Pipeline	\$ 21.8	\$ 25.1
Williams Natural Gas	10.9	15.5
Transcontinental Gas Pipe Line	61.0	47.4
Texas Gas Transmission	29.5	28.6
Kern River Gas Transmission	29.3	
Williams Energy Group:		
Field Services	56.3	41.6
Merchant Services	13.6	1.6
Petroleum Services	18.3	19.1
Exploration and Production	3.7	.4
Williams Communications Group	.6	8.0
Other	(2.9)	(.1)
Total operating profit	242.1	187.2
General corporate expenses	(11.6)	(12.1)
Interest expense — net	(91.9)	(69.7)
Investing income	4.1	12.7
Gain on sale of asset	15.7	_
Write-off of project costs	-	(41.4)
Other income — net	8.0	5.2
	166.4	81.9
Income from continuing operations before income taxes	60.4	17.5
Provision for income taxes	106.0	64.4
Income from continuing operations	B. 100 100 100	13.1
Income from discontinued operations		-
Net income	\$106.0	\$ 77.5
Primary earnings per common and common-equivalent share	\$.64	\$.47
Fully diluted earnings per common and common-equivalent share		\$.46

Field Services' fourth-quarter 1996 operating profit includes a gain of approximately \$20 million from the property insurance coverage associated with construction of replacement gathering facilities. In addition, 1996 segment operating profit and general corporate expenses together include approximately \$10 million related to an all-employee bonus that was linked to achieving record financial performance. In fourth-quarter 1996, Williams recognized a pre-tax gain of \$15.7 million from the sale of certain communication rights.

Merchant Services' fourth-quarter 1995 operating profit includes loss accruals of approximately \$6 million, primarily related to contract disputes. In fourth-quarter 1995, the development of a commercial coal gasification venture in south-central Wyoming was canceled, resulting in a \$41.4 million pre-tax charge (see Note 6 of Notes to Consolidated Financial Statements). Fourth-quarter 1995 income from discontinued operations reflects the after-tax effect of the reversal of accruals established at the time of the sale of the network services operations (see Note 3 of Notes to Consolidated Financial Statements).

Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure.

None.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS Item 14(a) 1 and 2

	Page
Covered by report of independent auditors:	
Consolidated statement of income for the three years ended December 31, 1996	F-12
Consolidated balance sheet at December 31, 1996 and 1995	F-14
Consolidated statement of stockholders' equity for the three years ended December 31, 1996.	F-15
Consolidated statement of cash flows for the three years ended December 31, 1996	F-16
Notes to consolidated financial statements	F-17
Schedule for the three years ended December 31, 1996:	
II — Valuation and qualifying accounts	F-46
Not covered by report of independent auditors:	
Quarterly financial data (unaudited)	F-43

All other schedules have been omitted since the required information is not present or is not present in amounts sufficient to require submission of the schedule, or because the information required is included in the financial statements and notes thereto.

THE WILLIAMS COMPANIES, INC. SCHEDULE II — VALUATION AND QUALIFYING ACCOUNTS(a)

		Additio	88		
	Beginning Balance	Charged to Costs and Expenses	Other (Millions)	Deductions(b)	Ending Balance
Allowance for doubtful accounts:	\$11.3	\$4.1	\$1.3(c)	\$7.0	\$ 9.7
1996	7.9	3.8	1.6(c)	2.0	11.3
1994	10.2	4.2(d)	=	6.5(c)	7.9

- (a) Deducted from related assets.
- (b) Represents balances written off, net of recoveries and reclassifications.
- (c) Primarily relates to acquisitions of businesses.
- (d) Excludes \$5.7 million related to discontinued operations.
- (e) Includes the discontinued operations beginning balance reclassification of \$3.6 million.

PART III

Item 10. Directors and Executive Officers of the Registrant

The information regarding the Directors and nominees for Director of Williams required by Item 401 of Regulation S-K is presented under the heading "Election of Directors" in Williams' Proxy Statement prepared for the solicitation of proxies in connection with the Annual Meeting of Stockholders of the Company for 1997 (the "Proxy Statement"), which information is incorporated by reference herein. A copy of the Proxy Statement is filed as an exhibit to the Form 10-K. Information regarding the executive officers of Williams is presented following Item 4 herein, as permitted by General Instruction G(3) to Form 10-K and Instruction 3 to Item 401(b) of Regulation S-K. Information required by Item 405 of Regulation S-K is included under the heading "Compliance with Section 16(a) of the Securities Exchange Act of 1934" in the Proxy Statement, which information is incorporated by reference herein.

Item 11. Executive Compensation

The information required by Item 402 of Regulation S-K regarding executive compensation is presented under the headings "Election of Directors" and "Executive Compensation and Other Information" in the Proxy Statement, which information is incorporated by reference herein. Notwithstanding the foregoing, the information provided under the headings "Compensation Committee Report on Executive Compensation" and "Stockholder Return Performance Presentation" in the Proxy Statement are not incorporated by reference herein. A copy of the Proxy Statement is filed as an exhibit to the Form 10-K.

Item 12. Security Ownership of Certain Beneficial Owners and Management

The information regarding the security ownership of certain beneficial owners and management required by Item 403 of Regulation S-K is presented under the headings "Security Ownership of Certain Beneficial Owners and Management" in the Proxy Statement, which information is incorporated by reference herein. A copy of the Proxy Statement is filed as an exhibit to the Form 10-K.

Item 13. Certain Relationships and Related Transactions

There is no information regarding certain relationships and related transactions required by Item 404 of Regulation S-K to be reported.

PART IV

Item 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K

- (a) 1 and 2. The financial statements and schedule listed in the accompanying index to consolidated financial statements are filed as part of this annual report.
 - (a) 3 and (c). The exhibits listed below are filed as part of this annual report.

Exhibit 2 -

- *(a) Stock Purchase Agreement by and among LDDS Communications, Inc., The Williams Companies, Inc., and WTG Holdings, Inc., dated as of August 22, 1994 (filed as Exhibit 2 to Williams Form 8-K, filed August 22, 1994).
- *(b) Agreement and Plan of Merger, dated as of December 12, 1994, among Williams, WC Acquisition Corp. and Transco (filed as Exhibit (c)(1) to Schedule 14D-1, dated December 16, 1994).
- *(c) Amendment to Agreement and Plan of Merger, dated as of February 17, 1995 (filed as Exhibit 6 to Amendment No. 8 to Schedule 13D, dated February 23, 1995).

Exhibit 3 -

- (a) Restated Certificate of Incorporation of Williams (filed as Exhibit 4(a) to Form 8-B Registration Statement, filed August 20, 1987).
- *(b) Certificate of Designation with respect to the \$2.21 Cumulative Preferred Stock (filed as Exhibit 4.3 to the Registration Statement on Form S-3, filed August 19, 1992).
- *(c) Certificate of Amendment of Restated Certificate of Incorporation, dated May 20, 1994 (filed as Exhibit 3(d) to Form 10-K for the fiscal year ended December 31, 1994).
- *(d) Certificate of Designation with respect to the \$3.50 Cumulative Convertible Preferred Stock (filed as Exhibit 3.1(c) to the Prospectus and Information Statement to Amendment No. 2 to the Registration Statement on Form S-4, filed March 30, 1995).
- *(e) Certificate of Increase of Authorized Number of Shares of Series A Junior Participating Preferred Stock (filed as Exhibit 3(f) to Form 10-K for the fiscal year ended December 31, 1995).
- *(f) Rights Agreement, dated as of February 6, 1996, between Williams and First Chicago Trust Company of New York (filed as Exhibit 4 to Williams Form 8-K, filed January 24, 1996).
- (g) By-laws of Williams, as amended (filed, as amended, as Exhibit 3 to Form 10-Q for the quarter ended September 30, 1996).

Exhibit 4 -

- *(a) Form of Senior Debt Indenture between the Company and Chase Manhattan Bank (formerly Chemical Bank), Trustee, relating to the 104% Debentures, due 2020; the 94% Debentures, due 2021; the 84% Notes, due 1998; Medium-Term Notes (8.50%-9.31%), due 1998 through 2001; the 7½% Notes, due 1999, and the 8½% Debentures, due 2012 (filed as Exhibit 4.1 to Form S-3 Registration Statement No. 33-33294, filed February 2, 1990).
- *(b) Form of Subordinated Debt Indenture between the Company and Chase Manhattan Bank (formerly Chemical Bank). Trustee, relating to 9.60% Quarterly Income Capital Securities, due 2025 (filed as Exhibit 4.2 to Form S-3 Registration Statement No. 33-60397, filed June 20, 1995).
- (c) U.S. \$1,000,000,000 Amended and Restated Credit Agreement, dated as of December 20. 1996, among Williams and certain of its subsidiaries and the banks named therein and Citibank, N.A., as agent.

Exhibit 10(iii) - Compensatory Plans and Management Contracts

- *(a) The Williams Companies, Inc. Supplemental Retirement Plan, effective as of January 1, 1988 (filed as Exhibit 10(iii) (c) to Form 10-K for the year ended December 31, 1987).
- *(b) Form of Employment Agreement, dated January 1, 1990, between Williams and certain executive officers (filed as Exhibit 10(iii) (d) to Form 10-K for the year ended December 31, 1989).
- *(c) Form of The Williams Companies, Inc. Change in Control Protection Plan between Williams and employees (filed as Exhibit 10(iii) (e) to Form 10-K for the year ended December 31, 1989).
- *(d) The Williams Companies, Inc. 1985 Stock Option Plan (filed as Exhibit A to Williams' Proxy Statement, dated March 13, 1985).
- *(e) The Williams Companies, Inc. 1988 Stock Option Plan for Non-Employee Directors (filed as Exhibit A to Williams' Proxy Statement, dated March 14, 1988).
- *(f) The Williams Companies, Inc. 1990 Stock Plan (filed as Exhibit A to Williams' Proxy Statement, dated March 12, 1990).

- *(g) The Williams Companies, Inc. Stock Plan for Non-Officer Employees (filed as Exhibit 10(iii) (g) to Form 10-K for the fiscal year ended December 31, 1995).
- *(h) The Williams Companies, Inc. 1996 Stock Plan (filed as Exhibit A to Williams' Proxy Statement, dated March 27, 1996).
- *(i) The Williams Companies, Inc. 1996 Stock Plan for Non-Employee Directors (filed as Exhibit B to Williams' Proxy Statement, dated March 27, 1996).
- *(j) Indemnification Agreement, effective as of August 1, 1986, between Williams and members of the Board of Directors and certain officers of Williams (filed as Exhibit 10(iii)(e) to Form 10-K for the year ended December 31, 1986).
- Exhibit 11 Computation of Earnings Per Common and Common-equivalent Share.
- Exhibit 12 Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividend Requirements.
- Exhibit 20 Definitive Proxy Statement of Williams for 1997 (as filed with the Commission on March 26, 1997).
- Exhibit 21 Subsidiaries of the registrant.
- Exhibit 23 Consent of Independent Auditors.
- Exhibit 24 Power of Attorney together with certified resolution.
- Exhibit 27 Financial Data Schedule.
- Exhibit 27.1 Restated Financial Data Schedule for the year ended December 31, 1995.

(b) Reports on Form 8-K.

On December 30, 1996, the Company filed a report on Form 8-K to report the Company's distribution of one share of Common Stock of the Company, \$1 par value, for every two shares of Common Stock outstanding on December 6, 1996, pursuant to a three-for-two stock split.

(d) The financial statements of partially-owned companies are not presented herein since none of them individually, or in the aggregate, constitute a significant subsidiary.

Each such exhibit has heretofore been filed with the Securities and Exchange Commission as part of the filing indicated and is incorporated herein by reference.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE WILLIAMS COMPANIES, INC. (Registrant)

By: /s/ Shawna L. Barnard
Shawna L. Barnard
Attorney-in-fact

Dated: March 26, 1997

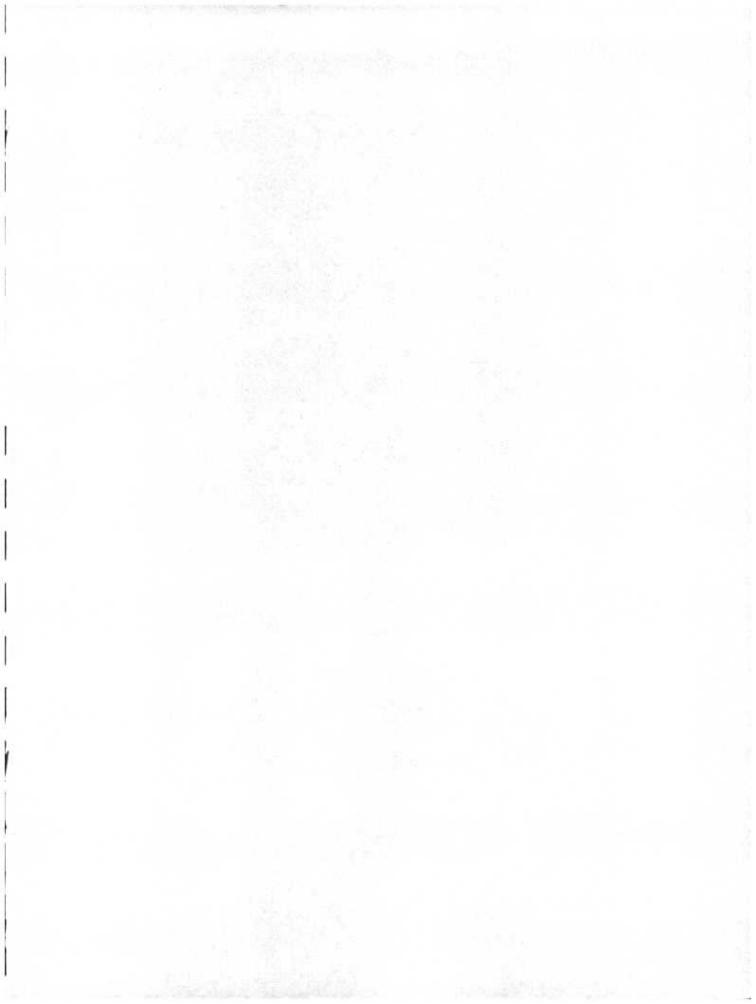
Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant in the capacities and on the dates indicated.

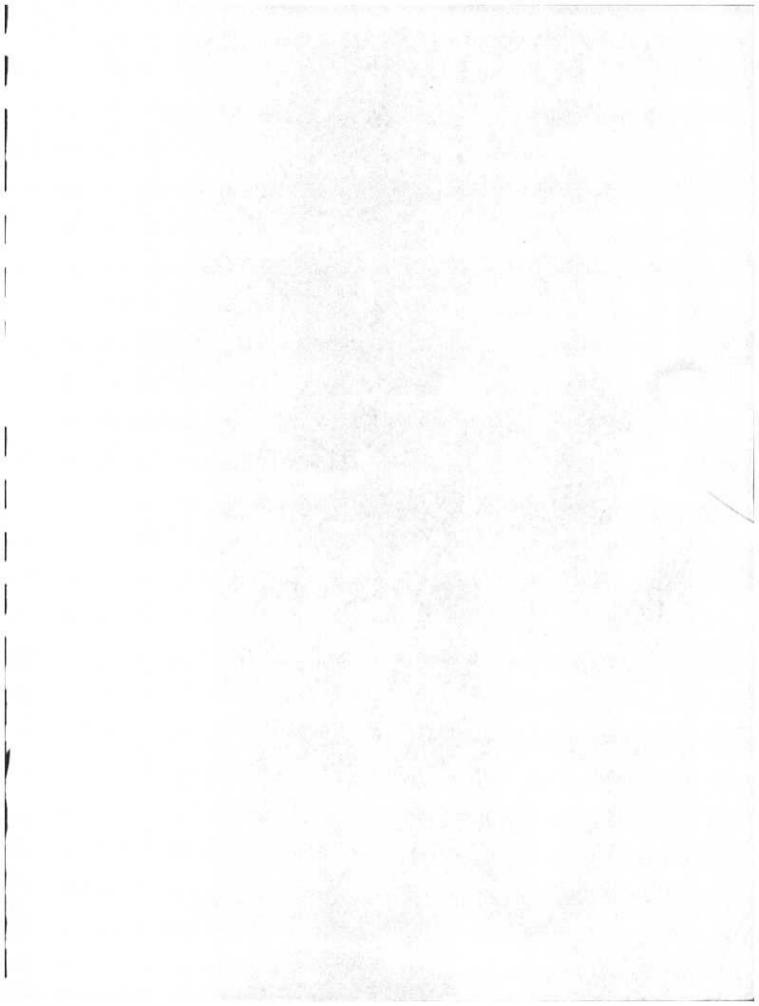
Signature	Title
/s/ KEITH E. BAILEY*	Chairman of the Board, President, Chief
Keith E. Bailey	Executive Officer (Principal Executive Officer) and Director
/s/ JACK D. McCarthy*	Senior Vice President — Finance (Principal
Jack D. McCarthy	Financial Officer)
/s/ GARY R. BELITZ*	Controller (Principal Accounting Officer)
Gary R. Belitz	
/s/ GLENN A. Cox*	Director
Glenn A. Cox	
/s/ THOMAS H. CRUIKSHANK*	Director
Thomas H. Cruikshank	
/s/ PATRICIA L. HIGGINS*	Director
Patricia L. Higgins	
	Director
W. R. Howell	
/s/ ROBERT J. LAFORTUNE*	Director
Robert J. LaFortune	
/s/ JAMES C. LEWIS*	Director
James C. Lewis	
/s/ JACK A. MACALLISTER*	Director
Jack A. MacAllister	
/s/ James A. McClure*	Director
James A. McClure	

Signature	
/s/ PETER C. MEINIG*	Director
Peter C. Meinig	
/s/ KAY A. ORR*	Director
Kay A. Orr	
/s/ GORDON R. PARKER*	Director
Gordon R. Parker	
/s/ JOSEPH H. WILLIAMS*	Director
Joseph H. Williams	
*By /s/ SHAWNA L. BARNARD	
Shawna L. Barnard Attorney-in-fact	The state of the s

Dated: March 26, 1997

Title





Form 10-K

SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 (FEE REQUIRED)

For the fiscal year ended December 31, 1997

OR

□ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 (NO FEE REQUIRED)

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 (Address of principal executive offices)

74172 (Zip Code)

Registrant's telephone number, including area code: (918) 588-2000

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Each Class

Name of Each Exchange on Which Registered

Common Stock, \$1.00 par value Preferred Stock Purchase Rights

New York Stock Exchange and the Pacific Stock Exchange

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT:

None

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 ⋈ No □

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

The aggregate market value of the registrant's voting stock held by nonaffiliates as of the close of business on March 23, 1998, was approximately \$10.3 billion.

The number of shares of the registrant's Common Stock outstanding at March 23, 1998, was 323,219,054, excluding 6,541,475 shares held by the Company.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's Proxy Statement prepared for the solicitation of proxies in connection with the Annual Meeting of Stockholders of the Company for 1998 are incorporated by reference in Part III.

FORM 10-K

PART I

Item 1. Business

(a) General Development of Business

The Williams Companies, Inc. (the "Company" or "Williams") was incorporated under the laws of the State of Nevada in 1949 and was reincorporated under the laws of the State of Delaware in 1987. The principal executive offices of the Company are located at One Williams Center, Tulsa, Okiahoma 74172 (telephone (918) 588-2000). Unless the context otherwise requires, references to the "Company" and "Williams" herein include The Williams Companies, Inc. and its subsidiaries.

On November 24, 1997, the Company announced that it had entered into a definitive merger agreement to acquire MAPCO Inc. ("MAPCO") in a stock-for-stock transaction based upon a fixed exchange ratio of 1.665 shares of the Company's Common Stock and .555 associated preferred stock purchase rights (adjusted to reflect the Company's two-for-one stock split on December 29, 1997) for each share of MAPCO Common Stock and associated preferred stock purchase rights. The Company's and MAPCO's shareholders approved actions necessary to complete the transaction at special stockholder meetings on February 26, 1998. See Note 19 to Notes to Consolidated Financial Statements. The Federal Trade Commission announced on March 27, 1998, that it would allow the parties to consummate the transaction, and the parties closed the transaction on March 28, 1998.

MAPCO is a Tulsa, Oklahoma-based diversified energy company. Subsidiaries of MAPCO engage in the transportation by pipeline of natural gas liquids ("NGLs"), anhydrous ammonia, crude oil, and refined petroleum products; the transportation by truck and rail of NGLs and refined petroleum products; the refining of crude oil; the marketing and trading of NGLs, refined petroleum products, and crude oil; NGL storage; and the marketing of motor fuel and merchandise through convenience store operations. MAPCO's subsidiary, Mid-America Pipeline Company, owns and operates 7,668 miles of pipeline and related pumping, metering, and storage facilities. Subsidiaries of MAPCO also own and operate two petroleum products refineries, one in Alaska, which markets approximately 44,000 barrels of refined products per day in Alaska, Canada, and the Pacific Rim, and one in Tennessee, which markets approximately 110,000 barrels of refined products per day. MAPCO's subsidiary, Thermogas Company, is the fourth largest propane marketer in the United States and sells propane in 18 states to more than 350,000 customers. Its MAPCO Express subsidiaries operate approximately 230 convenience stores and travel centers primarily in Tennessee and Alaska. MAPCO also owns subsidiaries providing fleet operators with motor fuel and data management and providing energy-related information services. MAPCO also holds equity investments in other businesses.

Management believes the acquisition furthers its strategy of seeking growth through strategic acquisitions and alliances and that MAPCO's assets and operations complement the Company's existing lines of business. Following the acquisition, the Company will operate the MAPCO businesses through Williams Energy Group.

On January 5, 1998, the Company's three-year non-compete agreement resulting from the 1995 sale of the network services operations of its telecommunications subsidiary expired, and the Company announced plans to re-enter the long-distance telecommunications market as a provider of wholesale communications services over an 18,000-mile network expected to be in operation by the beginning of 1999.

In April 1997, the Company merged its wholly owned subsidiary, Williams Telecommunications Systems, Inc., with Nortel Communications Systems, Inc., which was a wholly owned subsidiary of Northern Telecom, Inc. The Company holds a 70 percent interest in the newly formed entity, Williams Communications Solutions, LLC. See Note 2 of Notes to Consolidated Financial Statements.

In January 1996, the Company acquired a 49.9 percent interest from its partner in Kern River Gas Transmission Company giving the Company 99.9 percent ownership of this natural gas pipeline system. The purchase price was \$206 million. See Note 2 of Notes to Consolidated Financial Statements. The Company acquired the remaining 0.1 percent interest in the partnership in February 1997, for \$387,600.

(b) Financial Information About Industry Segments

See Part II, Item 8 - Financial Statements and Supplementary Data.

(c) Narrative Description of Business

The Company, through subsidiaries, engages in the transportation and sale of natural gas and related activities; natural gas gathering, processing, and treating activities; the transportation and terminaling of petroleum products; hydrocarbon exploration and production activities; the production and marketing of ethanol; and energy commodity marketing and trading and provides a variety of other products and services, including price risk management services, to the energy industry. The Company also engages in the communications business. In 1997, the Company's energy subsidiaries owned and operated: (i) five interstate natural gas pipeline systems; (ii) natural gas production properties; (iii) natural gas gathering and processing facilities; (iv) a common carrier petroleum products and crude oil pipeline system; (v) petroleum products terminals; and (vi) ethanol production facilities. The Company's communications subsidiaries offer: (i) datavoice- and video-related products and services; (ii) advertising distribution services; (iii) video services and other multimedia services for the broadcast industry; (iv) enhanced facsimile and audio- and videoconferencing services for businesses; (v) customer-premise voice and data equipment, including installation, maintenance, and integration; and (vi) network integration and management services nationwide. The Company also has investments in the equity of certain other companies.

Substantially all operations of Williams are conducted through subsidiaries. Williams performs management, legal, financial, tax, consultative, administrative, and other services for its subsidiaries. Williams' principal sources of cash are from external financings, dividends and advances from its subsidiaries, investments, payments by subsidiaries for services rendered and interest payments from subsidiaries on cash advances. The amount of dividends available to Williams from subsidiaries largely depends upon each subsidiary's earnings and operating capital requirements. The terms of certain subsidiaries' borrowing arrangements limit the transfer of funds to the Company.

To achieve organizational and operating efficiencies, the Company's interstate natural gas pipelines are grouped together under its wholly owned subsidiary, Williams Interstate Natural Gas Systems, Inc. All other operating companies are owned by Williams Holdings of Delaware, Inc., a wholly-owned subsidiary of the Company. The energy operations of Williams Holdings of Delaware, Inc. are grouped into a wholly-owned subsidiary, Williams Energy Group, and its communications operations are grouped into a wholly-owned subsidiary, Williams Communications Group, Inc. Item 1 of this report is formatted to reflect this structure.

WILLIAMS INTERSTATE NATURAL GAS SYSTEMS, INC.

The Company's interstate natural gas pipeline group, comprised of Williams Interstate Natural Gas Systems, Inc. and its subsidiaries, owns and operates a combined total of approximately 27,000 miles of pipelines with a total annual throughput of approximately 3,700 TBtu* of natural gas and peak-day delivery capacity of approximately 15 Bcf of natural gas. The interstate natural gas pipeline group consists of Transcontinental Gas Pipe Line Corporation, Northwest Pipeline Corporation, Kern River Gas Transmission Company, Texas Gas Transmission Corporation and Williams Gas Pipelines Central, Inc. The pipeline group also holds minority interests in joint venture interstate natural gas pipeline systems. The Company acquired Transcontinental Gas Pipe Line Corporation and Texas Gas Transmission Corporation in 1995. For the accounting treatment of the acquisition, see Note 2 of Notes to Consolidated Financial Statements. As noted above, the Company acquired an additional 49.9 percent interest in Kern River Gas Transmission Company in January 1996 and the remaining 0.1 percent interest in February 1997.

The term "Mcf" means thousand cubic feet, "MMcf" means million cubic feet and "Bcf" means billion cubic feet. All volumes of natural gas are stated at a pressure base of 14.73 pounds per square inch absolute at 60 degrees Fahrenheit. The term "Bto" means British Thermal Unit, "MMBtu" means one million British Thermal Units and "TBtu" means one trillion British Thermal Units. The term "Dth" means dekatherm. The term "Mbbl" means one thousand barrels. The term "GWh" means gigawatt hour.

In 1997, the Company's gas pipeline group began the process of combining certain administrative functions, such as human resources, information services, technical services, and finance, of its operating companies in an effort to lower costs and increase effectiveness. In addition, the Company combined the management teams of two of the operating companies, Northwest Pipeline Corporation and Kern River Gas Transmission Company, in 1997. Also in 1997, the senior vice president and general manager of Texas Gas Transmission Corporation assumed additional responsibilities as senior vice president and general manager of Williams Gas Pipelines Central, Inc. The Company made these management changes to increase the organizational efficiency of its natural gas pipeline group; however, each of these operating companies continues to operate as a separate legal entity. The Company's gas pipeline subsidiaries employ approximately 3,600 employees.

The interstate natural gas pipeline group's transmission and storage activities are subject to regulation by the Federal Energy Regulatory Commission ("FERC") under the Natural Gas Act of 1938 ("Natural Gas Act") and under the Natural Gas Policy Act of 1978 ("NGPA"), and, as such, their rates and charges for the transportation of natural gas in interstate commerce, the extension, enlargement or abandonment of jurisdictional facilities, and accounting, among other things, are subject to regulation. Each pipeline holds certificates of public convenience and necessity issued by FERC authorizing ownership and operation of all pipelines, facilities and properties considered jurisdictional for which certificates are required under the Natural Gas Act. Each pipeline is also subject to the Natural Gas Pipeline Safety Act of 1968, as amended by Title I of the Pipeline Safety Act of 1979, which regulates safety requirements in the design, construction, operation and maintenance of interstate gas transmission facilities.

A business description of each company in the interstate natural gas pipeline group follows.

TRANSCONTINENTAL GAS PIPE LINE CORPORATION (Transco)

Transco is an interstate natural gas transmission company that owns a 10,500-mile natural gas pipeline system extending from Texas, Louisiana, Mississippi and the offshore Gulf of Mexico through the states of Alabama, Georgia, South Carolina, North Carolina, Virginia, Maryland, Pennsylvania, and New Jersey to the New York City metropolitan area. The system serves customers in Texas and eleven southeast and Atlantic seaboard states, including major metropolitan areas in Georgia, North Carolina, New York, New Jersey and Pennsylvania. Effective May 1, 1995, Transco transferred the operation of certain production area facilities to Williams Field Services Group, Inc., an affiliated company.

Pipeline System and Customers

At December 31, 1997, Transco's system had a mainline delivery capacity of approximately 3.8 Bcf of gas per day from production areas to its primary markets. Using its Leidy Line and market-area storage capacity, Transco can deliver an additional 2.9 Bcf of gas per day for a system-wide delivery capacity total of approximately 6.7 Bcf of gas per day. Excluding the production area facilities operated by Williams Field Services Group, Inc., Transco's system is composed of approximately 7,300 miles of mainline and branch transmission pipelines, 39 compressor stations and six storage locations. Compression facilities at a sea level-rated capacity total approximately 1.3 million horsepower.

Transco's major gas transportation customers are public utilities and municipalities that provide service to residential, commercial, industrial and electric generation end users. Shippers on Transco's pipeline system include public utilities, municipalities, intrastate pipelines, direct industrial users, electrical generators, marketers and producers. Transco's largest customer in 1997 accounted for approximately 12 percent of Transco's total operating revenues. No other customer accounted for more than 10 percent of total operating revenues in 1997. Transco's firm transportation agreements are generally long-term agreements with various expiration dates and account for the major portion of Transco's business. Additionally, Transco offers interruptible transportation services under shorter term agreements.

Transco has natural gas storage capacity in five underground storage fields located on or near its pipeline system and/or market areas and operates three of these storage fields and a liquefied natural gas (LNG) storage facility. The total top gas storage capacity available to Transco and its customers in such storage fields

and LNG facility is approximately 216 Bcf of gas. Storage capacity permits Transco's customers to inject gas into storage during the summer and off-peak periods for delivery during peak winter demand periods.

Expansion Projects

In February 1997, Pine Needle LNG Company, LLC, which is owned by Transco and several of its major customers, commenced construction of an LNG storage project in Guilford County, North Carolina. The project will have 4 Bcf of storage capacity and 400 MMcf per day of withdrawal capacity, and is expected to be placed into service on or about May 1, 1999. The project is estimated to cost approximately \$107 million. Transco will operate the facility and have a 35 percent ownership interest. Transco expects to make equity investments of approximately \$19 million in this project.

In March 1997, Transco announced its MarketLink Expansion Project. MarketLink will expand Transco's Leidy Line and market-area mainline facilities, providing the final transportation link for several pipeline projects designed to transport Canadian and Rocky Mountain gas supplies to eastern markets. The total cost and capacity of the project, which is targeted to be in service for the 1999-2000 winter heating season, will be determined based on market subscriptions. Transco plans to file for FERC approval of the project during the first quarter of 1998.

In March 1997, Independence Pipeline Company filed with FERC an application, which was amended in December 1997, for approval to construct and operate a pipeline consisting of approximately 400 miles of 36-inch diameter pipe from ANR Pipeline Company's existing compressor station at Defiance, Ohio to Transco's facilities at Leidy, Pennsylvania. Independence will provide approximately 916 MMcf per day of firm gas transportation capacity and is expected to be in service in the 1999-2000 time frame. The estimated cost of the project is \$678 million, and Transco's equity contributions will be approximately \$68 million based on its expected one-third ownership interest in the project.

In April 1997, Transco withdrew its FERC certificate application for the Seaboard Expansion Project and filed an application with the FERC for the Pocono Expansion Project, which was completed and placed into service in November 1997. Pocono added 35 MMcf per day of firm gas transportation capacity on Transco's Leidy Line in Pennsylvania. The cost of the expansion is approximately \$10 million.

In August 1997, FERC issued a certificate authorizing Transco to expand its existing Maiden Lateral to Piedmont Natural Gas Company, Inc. in Lincoln and Catawba Counties, North Carolina. The project facilities include approximately 18 miles of 16-inch pipeline loop and an expansion of Transco's existing Lowesville Meter Station. The project was placed into service in November 1997. The cost for the facilities is approximately \$13 million.

In November 1997, Transco completed and placed into service the SunBelt Expansion Project. This project added approximately 146 MMcf per day of firm gas transportation capacity to markets in Georgia, South Carolina, and North Carolina. The total cost of the expansion was approximately \$85 million, of which \$61 million was expended in 1997.

In November 1997, the North Carolina Utilities Commission issued an order approving the Cardinal Pipeline System Project. Wholly owned subsidiaries of Transco and three of its North Carolina customers will own the pipeline, which will involve the acquisition of the existing 37-mile Cardinal pipeline in North Carolina and construction of an approximately 67-mile extension of the pipeline to new interconnections near Clayton County, North Carolina. This project will provide 140 MMcf per day of additional firm gas transportation capacity to North Carolina markets and is expected to be placed into service by the end of 1999. A wholly owned subsidiary of Transco will operate the pipeline and have a 45 percent ownership interest in the project. Transco expects to make equity investments of approximately \$22 million in this project, of which approximately \$900,000 was invested during 1997.

In December 1997, Transco and AGL Resources Inc. (AGL) formed Cumberland Gas Pipeline Company. Under this project, existing pipeline facilities of Transco and AGL will be expanded northward into Tennessee, establishing a 135-mile pipeline that is expected to provide firm transportation capacity to markets in Georgia and Tennessee by the 2000-2001 winter heating season. The project is expected to be submitted for

FERC approval in the third quarter of 1998. Transco will operate the pipeline facilities and have a 50 percent ownership interest. Transco estimates that the total cost of this project will be up to \$115 million, and expects to make equity investments of up to \$29 million. To complement the Cumberland project, Transco will offer additional pipeline capacity from the terminus of its existing Mobile Bay Lateral in Choctaw County, Alabama, to its interconnect with Cumberland at Transco's Station 125 in Walton County, Georgia, at a cost of up to \$120 million.

In January 1998, the FERC approved the Mobile Bay Lateral Expansion Project, an expansion of Transco's existing 123-mile Mobile Bay Lateral. The project is expected to provide new firm transportation capacity of 350 MMcf of gas per day from the outer continental shelf to Transco's Station 82 and increase capacity on the existing onshore lateral from 520 MMcf of gas per day to 784 MMcf of gas per day. The project is targeted to be placed into service in two phases during 1998 at a cost of approximately \$120 million, of which approximately \$36 million was invested during 1997.

In January 1998, FERC approved the 1998 Cherokee Expansion Project, an incremental expansion of Transco's pipeline system in its southern market area which will provide approximately 84 MMcf of gas per day of new firm gas transportation capacity on Transco's system by a proposed in-service date of November 1, 1998. The estimated cost for this project is \$68 million, of which \$9.3 million was invested during 1997.

In January 1998, Transco and Duke Energy Corporation announced plans to form a joint venture to develop a new natural gas pipeline project into New York City. The project, called the Cross Bay Pipeline, will combine Duke's previously announced Excelsiors project with the existing Long Beach delivery facilities on Transco's system into a new integrated delivery pipeline. The project will provide up to 700 MMcf of gas per day on a phased-in basis, with the in-service date of the initial phase being targeted for 1999.

Operating Statistics. The following table summarizes transportation data for the periods indicated, including the portion of 1995 during which the Company did not own Transco (in TBtus):

	1997	1996	1995
System Deliveries (TBtu)			
Market-area deliveries:			
Long-haul transportation	940.2	948.9	858.4
Market-area transportation	438.9	428.1	467.3
Total market-area deliveries	1,379.1	1,377.0	1.325.7
Production-area transportation	186.8	210.0	165.9
Total system deliveries	1,565.9	1,587.0	1,491.6
Average Daily Transportation Volumes	4.3	4.3	4.1
Average Daily Firm Reserved Capacity	5.5	5.2	5.2

NORTHWEST PIPELINE CORPORATION (Northwest Pipeline)

Northwest Pipeline is an interstate natural gas transmission company that owns and operates a pipeline system for the mainline transmission of natural gas extending from the San Juan Basin in northwestern New Mexico and southwestern Colorado through Colorado, Utah, Wyoming, Idaho, Oregon and Washington to a point on the Canadian border near Sumas, Washington. Northwest Pipeline provides services for markets in California, New Mexico, Colorado, Utah, Nevada, Wyoming, Idaho, Oregon and Washington, directly or indirectly through interconnections with other pipelines.

Pipeline System and Customers

At December 31, 1997, Northwest Pipeline's system, having an aggregate mainline deliverability of approximately 2.5 Bef of gas per day, was composed of approximately 3,900 miles of mainline and branch transmission pipelines and 40 mainline compressor stations with a combined capacity of approximately 307,000 horsepower.

In 1997, Northwest Pipeline transported natural gas for a total of 153 customers. Transportation customers include distribution companies, municipalities, interstate and intrastate pipelines, gas marketers and direct industrial users. The five largest customers of Northwest Pipeline in 1997 accounted for approximately 17 percent, 16.9 percent, 11.8 percent, 10.6 percent and 10.4 percent, respectively, of its total operating revenues. No other customer accounted for more than 10 percent of total operating revenues. Northwest Pipeline's firm transportation agreements are generally long-term agreements with various expiration dates and account for the major portion of Northwest Pipeline's business. Additionally, Northwest Pipeline offers interruptible transportation service under agreements that are generally short term.

As a part of its transportation services, Northwest Pipeline utilizes underground storage facilities in Utah and Washington enabling it to balance daily receipts and deliveries. Northwest Pipeline also owns and operates a liquefied natural gas storage facility in Washington that provides a needle-peaking service for the system. These storage facilities have an aggregate delivery capacity of approximately 973 MMcf of gas per day.

Operating Statistics: The following table summarizes transportation data for the periods indicated (in TBtus):

	1997	1996	1995
Transportation Volumes	714	834	826
Average Daily Transportation Volumes	2.0	2.3	2.3
Average Daily Firm Reserved Capacity	2.5	2.5	2.4

Transportation volumes declined from 1996 to 1997 as a result of Northwest Pipeline's sale in late 1996 of a majority of its South End Facilities.

KERN RIVER GAS TRANSMISSION COMPANY (Kern River)

Kern River is an interstate natural gas transmission company that owns and operates a natural gas pipeline system extending from Wyoming through Utah and Nevada to California. Kern River had been jointly owned and operated by Williams Western Pipeline Company, a subsidiary of the Company, and a subsidiary of an unaffiliated company. As previously indicated, the Company acquired an additional 49.9 percent interest in Kern River in January 1936. See Note 2 of Notes to Consolidated Financial Statements. In February 1997, the Company acquired the remaining 0.1 percent interest in Kern River. The transmission system, which commenced operations in February 1992 following completion of construction, delivers natural gas primarily to the enhanced oil recovery fields in southern California. The system also transports natural gas for utilities, municipalities and industries in California, Nevada and Utah.

Pipeline System and Customers

As of December 31, 1997, Kern River's pipeline system was composed of approximately 705 miles of mainline and branch transmission pipelines and five compressor stations having an aggregate mainline delivery capacity of 700 MMcf of gas per day. The pipeline system interconnects with the pipeline facilities of another pipeline company at Daggett, California. From the point of interconnection, Kern River and the other pipeline company have a common 219-mile pipeline which is owned 63.6 percent by Kern River and 36.4 percent by the other pipeline company, as tenants in common, and is designed to accommodate the combined throughput of both systems. This common facility has a capacity of 1.1 Bcf of gas per day.

Kern River transports gas for others under firm long-term transportation contracts totaling 694 MMcf of gas per day. In 1997, Kern River transported natural gas for customers in California, Nevada, and Utah. Gas was transported for reinjection as a part of enhanced oil recovery in Kern County, California, and for local distribution customers, electric utilities, cogeneration projects, and commercial and other industrial customers. The four largest customers of Kern River in 1997 accounted for approximately 16 percent, 14 percent, 12 percent, and 10 percent, respectively, of its total operating revenues. Three of these customers serve the enhanced oil recovery fields. No other customer accounted for more than 10 percent of total operating revenues in 1997.

Kern River has executed a seasonal firm transportation contract to deliver natural gas into the Las Vegas, Nevada, market area during the winter months. Kern River began deliveries of approximately 10 MMcf of gas per day during 1997 and expects to escalate such deliveries to 40 MMcf of gas per day on a seasonal basis by 1999.

Operating Statistics. The following table summarizes transportation data for the periods indicated, including periods during which the Company owned less than 100 percent of Kern River (in TBtus):

	1997	1996	1995
Transportation Volumes	285	281	286
Average Daily Transportation Volumes		.77	.78
Average Daily Firm Reserved Capacity	.73	.71	.72

TEXAS GAS TRANSMISSION CORPORATION (TXG)

TXG is an interstate natural gas transmission company that owns and operates a natural gas pipeline system originating in the Louisiana Gulf Coast area and in east Texas and running generally north and east through Louisiana, Arkansas, Mississippi, Tennessee, Kentucky, Indiana and into Ohio, with smaller diameter lines extending into Illinois. TXG's direct market area encompasses eight states in the South and Midwest, and includes the Memphis, Tennessee; Louisville, Kentucky; Cincinnati and Dayton, Ohio; and Indianapolis, Indiana, metropolitan areas. TXG also has indirect market access to the Northeast through interconnections with unaffiliated pipelines.

Pipeline System and Customers

At December 31, 1997, TXG's system, having a mainline delivery capacity of approximately 2.8 Bcf of gas per day, was composed of approximately 6,000 miles of mainline and branch transmission pipelines and 32 compressor stations having a sea level-rated capacity totaling approximately 549,000 horsepower.

In 1997, TXG transported gas to customers in Louisiana, Arkansas, Mississippi, Tennessee, Kentucky, Indiana, Illinois, and Ohio and to customers in the Northeast served indirectly by TXG. TXG transported gas for 110 distribution companies and municipalities for resale to residential, commercial and industrial users. TXG provided transportation services to approximately 20 industrial customers located along the system. At December 31, 1997, TXG had transportation contracts with approximately 588 shippers. Transportation shippers include distribution companies, municipalities, intrastate pipelines, direct industrial users, electrical generators, marketers and producers. The largest customer of TXG in 1997 accounted for approximately 12.4 percent of its total operating revenues. No other customer accounted for more than 10 percent of total operating revenues during 1997. TXG's firm transportation and storage agreements are generally long-term agreements with various expiration dates and account for the major portion of TXG's business. Additionally, TXG offers interruptible transportation and storage services under agreements that are generally short-term.

TXG owns and operates natural gas storage reservoirs in 10 underground storage fields located on or near its pipeline system and/or market areas. The storage capacity of TXG's certificated storage fields is approximately 177 Bcf of gas. TXG's storage gas is used in part to meet operational balancing needs on its system, in part to meet the requirements of TXG's firm and interruptible storage customers, and in part to meet the requirements of TXG's "no-notice" transportation service, which allows TXG's customers to temporarily draw from TXG's storage gas to be repaid in-kind during the following summer season. A large portion of the gas delivered by TXG to its market area is used for space heating, resulting in substantially higher daily requirements during winter months.

Operating Statistics. The following table summarizes total system transportation volumes for the periods indicated, including the portion of 1995 during which the Company did not own TXG (in TBtus):

	1997	1996	1995
Transportation Volumes	773.6	794.5	693.3
Average Daily Transportation Volumes	2.1	2.2	1.9
Average Daily Firm Reserved Capacity	2.2	2.1	2.0

WILLIAMS GAS PIPELINES CENTRAL, INC. (Central)

Central, formerly known as Williams Natural Gas Company, is an interstate natural gas transmission company that owns and operates a natural gas pipeline system located in Colorado, Kansas, Missouri, Nebraska, Oklahoma, Texas, and Wyoming. The system serves customers in seven states, including major metropolitan areas of Kansas and Missouri, its chief market areas.

Pipeline System and Customers

At December 31, 1997, Central's system, having a mainline delivery capacity of approximately 2.2 Bcf of gas per day, was composed of approximately 6,000 miles of mainline and branch transmission and storage pipelines and 42 compressor stations having a sea level-rated capacity totaling approximately 218,000 horsepower.

In 1997, Central transported gas to customers in Colorado, Kansas, Missouri, Nebraska, Oklahoma, Texas, and Wyoming. Gas was transported for 70 distribution companies and municipalities for resale to residential, commercial and industrial users in approximately 530 cities and towns. Transportation services were provided to approximately 303 industrial customers, federal and state institutions and agricultural processing plants located principally in Kansas, Missouri and Oklahoma. At December 31, 1997, Central had transportation contracts with approximately 201 shippers. Transportation shippers included distribution companies, municipalities, intrastate pipelines, direct industrial users, electrical generators, marketers and producers.

In 1997, approximately 68 percent (approximately 34 percent each) of total operating revenues were generated from gas transportation services to Central's two largest customers, Kansas Gas Service Company, a division of Oneok, Inc., formerly Western Resources, Inc., and Missouri Gas Energy Company. Kansas Gas Service Company sells or resells gas to residential, commercial and industrial customers principally in certain major metropolitan areas of Kansas. Missouri Gas Energy sells or resells gas to residential, commercial and industrial customers principally in certain major metropolitan areas of Missouri. No other customer accounted for more than 10 percent of operating revenues during 1997.

In 1997, Central reached agreement with its two major customers to renew a major portion of their firm capacity that was to expire under then-existing contracts. The majority of the new contracts have terms ranging from four to five years. Central's remaining firm transportation agreements have various expiration dates ranging from one year to twenty years, with the majority expiring in three to eight years. Additionally, Central offers interruptible transportation services under agreements that are generally short term.

Central operates nine underground storage fields with an aggregate working gas storage capacity of approximately 43 Bcf and an aggregate delivery capacity of approximately 1.2 Bcf of gas per day. Central's customers inject gas in these fields when demand is low and withdraw it to supply their peak requirements. During periods of peak demand, approximately two-thirds of the firm gas delivered to customers is supplied from these storage fields. Storage capacity enables the system to operate more uniformly and efficiently during the year.

During 1997, Central completed four expansion projects which resulted in additional firm transportation contracts totaling over 71,000 Dth per day.

Operating Statistics. The following table summarizes transportation data for the periods indicated (in TBtus):

Transportation Volumes	337	341	334
Average Daily Transportation Volumes	.9	.9	.9
Average Daily Firm Reserved Capacity	2.1	1.9	2.0

Regulatory Matters

In 1992, FERC issued Order 636, which required interstate pipeline companies to restructure their tariffs to eliminate traditional on-system sales services. In addition, the Order required implementation of various

changes in forms of service, including unbundling of gathering, transmission and storage services; terms and conditions of service; rate design; gas supply realignment cost recovery; and other major rate and tariff revisions. Kern River implemented its restructuring on August 1, 1993; Central implemented its restructuring on October 1, 1993; and Transco, Northwest Pipeline and TXG implemented their restructurings on November 1, 1993. Certain aspects of three pipeline companies' Order 636 restructurings are under appeal.

Each interstate natural gas pipeline has various regulatory proceedings pending. Rates are established primarily through FERC's ratemaking process. Key determinants in the ratemaking process are (1) costs of providing service, including depreciation rates, (2) allowed rate of return, including the equity component of the capital structure, and (3) volume throughput assumptions. FERC determines the allowed rate of return in each rate case. Rate design and the allocation of costs between the demand and commodity rates also impact profitability. As a result of such proceedings, the pipeline companies have collected a portion of their revenues subject to refund. See Note 13 of Notes to Consolidated Financial Statements for the amount of revenues reserved for potential refund as of December 31, 1997.

Each of the interstate natural gas pipeline companies that were formerly gas supply merchants has undertaken the reformation of its respective gas supply contracts. None of the pipelines have any significant pending supplier take-or-pay, ratable-take or minimum-take claims. Central has an accrued liability recorded of \$94 million for its estimated remaining contract reformation and gas supply realignment costs under Order 636. These contracts are presently subject to certain FERC proceedings. For information on outstanding issues with respect to contract reformation, gas purchase deficiencies and related regulatory issues, see Note 18 of Notes to Consolidated Financial Statements.

Competition

FERC continues to regulate each of the Company's interstate natural gas pipeline companies pursuant to the Natural Gas Act and the NGPA. However, competition for natural gas transportation has intensified in recent years due to customer access to other pipelines, rate competitiveness among pipelines, customers' desire to have more than one transporter and regulatory developments. FERC's stated purpose for implementing Order 636 was to improve the competitive structure of the natural gas pipeline industry. Future utilization of pipeline capacity will depend on competition from other pipelines, use of alternative fuels, the general level of natural gas demand and weather conditions. Electricity and distillate fuel oil are primary competitive forms of energy for residential and commercial markets. Coal and residual fuel oil compete for industrial and electric generation markets. Nuclear and hydroelectric power and power purchased from grid arrangements among electric utilities also compete with gas-fired power generation in certain markets.

As mentioned, when restructured tariffs became effective under Order 636, all suppliers of natural gas were able to compete for any gas markets capable of being served by the pipelines using nondiscriminatory transportation services provided by the pipelines. As the Order 636 regulated environment has matured, many pipelines have faced reduced levels of subscribed capacity as contractual terms expire and customers opt to reduce firm capacity under contract in favor of alternative sources of transmission and related services. This situation, known in the industry as "capacity turnback," is forcing the pipelines to evaluate the consequences of major demand reductions in traditional long-term contracts. It could also result in significant shifts in system utilization, and possible realignment of cost structure for remaining customers since all interstate natural gas pipeline companies continue to charge rates approved by FERC on a cost of service basis.

The Company is aware that several state jurisdictions have been involved in implementing changes similar to the changes that have occurred at the federal level under Order 636. Such activity, frequently referred to as "LDC unbundling," has been most pronounced in the states of New York, New Jersey, Georgia, and Pennsylvania. New York and New Jersey began establishing LDC unbundling regulations in 1995 and continue to develop regulations regarding LDC unbundling. Georgia enacted an LDC unbundling program in 1997. Pennsylvania is currently considering LDC unbundling and may enact such legislation in 1998. In addition, Maryland and Delaware currently have pilot unbundling programs for industrial, commercial, and

residential end-users. Management expects these regulations to encourage greater competition in the natural gas marketplace.

Ownership of Property

Each of the Company's interstate natural gas pipeline subsidiaries generally owns its facilities in fee. However, a substantial portion of each pipeline's facilities is constructed and maintained pursuant to rights-of-way, easements, permits, licenses or consents on and across properties owned by others. Compressor stations, with appurtenant facilities, are located in whole or in part either on lands owned or on sites held under leases or permits issued or approved by public authorities. The storage facilities are either owned or contracted under long-term leases or easements.

Environmental Matters

Each interstate natural gas pipeline is subject to the National Environmental Policy Act and federal, state and local laws and regulations relating to environmental quality control. Management believes that, with respect to any capital expenditures and operation and maintenance expenses required to meet applicable environmental standards and regulations, FERC would grant the requisite rate relief so that, for the most part, the pipeline subsidiaries could recover such expenditures in their rates. For this reason, management believes that compliance with applicable environmental requirements by the interstate pipelines is not likely to have a material effect upon the Company's earnings or competitive position.

For a discussion of specific environmental issues involving the interstate pipelines, including estimated cleanup costs associated with certain pipeline activities, see "Environmental" under Management's Discussion and Analysis of Financial Condition and Results of Operations and "Environmental Matters" in Note 18 of Notes to Consolidated Financial Statements.

WILLIAMS HOLDINGS OF DELAWARE, INC. (Williams Holdings)

Williams Holdings' energy subsidiaries are engaged in exploration and production; natural gas gathering, processing and treating activities; petroleum products transportation and terminaling; ethanol production and marketing; and energy commodity marketing and trading and price risk management and energy finance services. In addition, these subsidiaries provide a variety of other products and services to the energy industry. Williams Holdings' communications subsidiaries offer data-, voice-, and video-related products and services and customer premise voice and data equipment, including installation, maintenance, and integration, nationwide. Williams Holdings also has certain other equity investments.

WILLIAMS ENERGY GROUP (Williams Energy)

In 1996, Williams Holdings reorganized its energy operations under a newly created, wholly owned subsidiary, Williams Energy Group, and began reporting such operations for financial reporting purposes on this basis in the fourth quarter of 1996.

Williams Energy is comprised of four major business units: Exploration and Production, Field Services, Petroleum Services, and Energy Marketing and Trading. Through its business units, Williams Energy engages in energy production and exploration activities; natural gas gathering, processing, and treating; petroleum liquids transportation and terminal services; ethanol production; and energy commodity marketing and trading.

Williams Energy, through its subsidiaries, owns 600 Bcf of proved natural gas reserves located primarily in the San Juan Basin of Colorado and New Mexico and owns or operates approximately 11,000 miles of gathering pipelines (including certain gathering lines owned by an affiliate but operated by Field Services), 10 gas treating plants, 10 gas processing plants, 53 petroleum products terminals, and approximately 9,100 miles of liquids pipeline. Physical and notional volumes marketed and traded by Williams Energy's Energy Marketing and Trading unit approximated 11,018 TBtu equivalents in 1997. In support of its power marketing activities, Williams Energy acquired a cogeneration plant in Hazleton, Pennsylvania, in 1997 and also owns a cogeneration plant in northwestern New Mexico. These facilities add approximately 113

megawatts of capacity to its portfolio. Williams Energy, through its subsidiaries, employs approximately 2,800 employees.

Revenues and operating profit for Williams Energy by business unit are reported in Note 4 of Notes to Consolidated Financial Statements herein.

A business description of each of Williams Energy's business units follows.

EXPLORATION AND PRODUCTION

Williams Energy, through its wholly owned subsidiary Williams Production Company (Williams Production), owns and operates producing natural gas leasehold properties in the United States. In addition, Williams Production is actively exploring for oil and gas.

Oil and gas properties. Exploration and production properties are located primarily in the Rocky Mountains and Gulf Coast areas. Rocky Mountain properties are located in the San Juan Basin in New Mexico and Colorado, in Wyoming, and in Utah. Gulf Coast properties include North Louisiana, the Houma Embayment and Transition Zone in Southern Louisiana, Pinnacle Reef play in East Texas, Sligo and Wilcox trends in South Texas, and offshore Gulf of Mexico.

Gas Reserves. As of December 31, 1997, 1996, and 1995, Williams Production had proved developed natural gas reserves of 362 Bcf, 323 Bcf, and 292 Bcf, respectively, and proved undeveloped reserves of 238 Bcf, 208 Bcf, and 222 Bcf, respectively. Of Williams Production's total proved reserves, 89 percent are located in the San Juan Basin of Colorado and New Mexico. No major discovery or other favorable or adverse event has caused a significant change in estimated gas reserves since year end.

Customers and Operations. As of December 31, 1997, the gross and net developed leasehold acres owned by Williams Production totaled 268,331 and 115,728 respectively, and the gross and net undeveloped acres owned were 447,458 and 121,351 respectively. As of such date, Williams Production owned interests in 3,113 gross producing wells (558 net) on its leasehold lands. The following tables summarize drilling activity for the periods indicated:

1997 Wells	Gross	Net
Development Drilled	198 198	32.6 32.6
Exploration Drilled	12	4.6 2.8
Completed During	Gross Wells	Net Wells
1997	207 65 61	35 11 22

The majority of Williams Production's gas production is currently being sold in the spot market at market prices. Total net production sold during 1997, 1996, and 1995 was 37.1 Bef, 31.0 Bef, and 30.0 Bef, respectively. The average production costs, including production taxes, per Mcf of gas produced were \$.42, \$.23, and \$.23, in 1997, 1996, and 1995, respectively. The average wellhead sales price per Mcf was \$1.62, \$.98, and \$.88, respectively, for the same periods. Net production sold and average production costs for 1996 and 1995 have been restated to include net profits volumes not previously reported.

In 1993, Williams Production conveyed a net profits interest in certain of its properties to the Williams Coal Seam Gas Royalty Trust. Williams subsequently sold Trust Units to the public in an underwritten public offering. Williams Holdings owns 3,568,791 Trust Units representing 36.8 percent of outstanding Units. Substantially all of the production attributable to the properties conveyed to the Trust was from the Fruitland

coal formation and constituted coal seam gas. Production information reported herein includes Williams Production's interest in such Units.

FIELD SERVICES

Williams Energy, through Williams Field Services Group, Inc. and its subsidiaries (Field Services), owns and operates natural gas gathering, processing, and treating facilities located in northwestern New Mexico, southwestern Colorado, southwestern Wyoming, northwestern Oklahoma, southwestern Kansas, and also in areas offshore and onshore in Texas and Louisiana. Field Services also operates gathering facilities that are owned by Transco, an affiliated company, and that are currently regulated by the FERC. In February 1996, Field Services and Transco filed applications with FERC to spindown all of Transco's gathering facilities to Field Services. FERC subsequently denied the request in September 1996. Field Services and Transco sought rehearing in October 1996. In August 1997, Field Services and Transco filed a second request for expedited treatment of the rehearing request. FERC has yet to rule on this request for rehearing.

Expansion Projects. Field Services continued to expand its operations in the gulf coast region during 1997 primarily through the Mobile Bay Project. During the year, Field Services obtained a life-of-reserves commitment from SOCO Offshore to anchor the construction of the Field Services' facilities required to gather and process near the Outer Continental Shelf. These committed reserves along with existing production from the Mobile Bay area will more than adequately supply this plant, scheduled to begin operations in early 1999. In addition, Field Services has acquired the remaining 50 percent interest in the 500 MMcfd Cameron Meadows processing plant in south Texas, has reached an agreement to partner in a 200 MMcfd processing plant in Louisiana, and finalized construction plans for a deep water gathering line to Green Canyon Federal Block 205 off Transco's Southeast Louisiana gathering system where planned capacity is expected to reach 90 MMcfd in the fourth quarter of 1998.

Customers and Operations. Facilities owned and/or operated by Field Services consist of approximately 11,000 miles of gathering pipelines (including certain gathering lines owned by an affiliate but operated by Field Services), 10 gas treating plants and 10 gas processing plants (one of which is partially owned). The aggregate daily inlet capacity is approximately 7.9 Bcf for the gathering systems and 6.7 Bcf of gas for the gas processing, treating, and dehydration facilities. Gathering and processing customers have direct access to interstate pipelines, including affiliated pipelines, which provide access to multiple markets.

During 1997, Field Services gathered natural gas for 296 customers. The largest gathering customer accounted for approximately 17 percent of total gathered volumes. During 1997, Field Services processed natural gas for a total of 130 customers. The largest customer accounted for approximately 24 percent of total processed volumes. No other customer accounted for more than 10 percent of gathered or processed volumes. Field Services' gathering and processing agreements with large customers are generally long-term agreements with various expiration dates. These long-term agreements account for the majority of the gas gathered and processed by Field Services.

Operating Statistics. The following table summarizes gathering, processing, and natural gas liquid sales volumes for the periods indicated. The information includes operations attributed to facilities owned by affiliated entities but operated by Field Services, including the portion of 1995 during which the Company did not own such facilities:

	1997	1996	1995
Gas volumes (TBtu, except liquids sales):			
Gathering	2,153	2,155	1,806
Processing	520	484	406
Natural gas liquid sales (millions of gallons)	551	403	284

PETROLEUM SERVICES

Williams Energy, through wholly owned subsidiaries in its Petroleum Services unit, owns and operates a petroleum products and crude oil pipeline system, two ethanol production plants (one of which is partially owned), and petroleum products terminals and provides services and markets products related thereto.

Transportation. A subsidiary in the Petroleum Services unit, Williams Pipe Line Company (Williams Pipe Line), owns and operates a petroleum products and crude oil pipeline system which covers an 11-state area extending from Oklahoma in the south to North Dakota and Minnesota in the north and Illinois in the east. The system is operated as a common carrier offering transportation and terminaling services on a nondiscriminatory basis under published tariffs. The system transports refined products, LP-gases, lube extracted fuel oil, and crude oil.

At December 31, 1997, the system traversed approximately 7,100 miles of right-of-way and included approximately 9,100 miles of pipeline in various sizes up to 16 inches in diameter. The system includes 77 pumping stations, 23 million barrels of storage capacity, and 40 delivery terminals. The terminals are equipped to deliver refined products into tank trucks and tank cars. The maximum number of barrels which the system can transport per day depends upon the operating balance achieved at a given time between various segments of the system. Because the balance is dependent upon the mix of products to be shipped and the demand levels at the various delivery points, the exact capacity of the system cannot be stated.

An affiliate of Williams Pipe Line, Longhorn Enterprises of Texas, Inc. ("LETI"), owns a 31.5 percent interest in Longhorn Partners Pipeline, LP, a joint venture formed to construct and operate a refined products pipeline from Houston to El Paso, Texas. The pipeline is expected to commence operations in 1998. Williams Pipe Line will design, construct, and operate the pipeline, and LETI has irrevocably committed to contribute \$87.4 million to the joint venture in 1998.

Operating Statistics. The operating statistics set forth below relate to the system's operations for the periods indicated:

	1997	1996	1995
Shipments (thousands of barrels):			
Refined products:			
Gasolines	132,428	134,296	125,060
Distillates	71,694	68,628	61,238
Aviation fuels	10,557	11,189	12,535
LP-Gases	13,322	15,618	12,839
Lube extracted fuel oil	7,471	8,555	4,462
Crude oil	31	891	860
Total Shipments	235,503	239,177	216,994
Daily average (thousands of barrels)	645	655	595
Average haul (miles)	259	259	269
Barrel miles (millions)	61,086	61,969	58,326

Environmental regulations and changing crude supply patterns continue to affect the refining industry. The industry's response to environmental regulations and changing supply patterns will directly affect volumes and products shipped on the Williams Pipe Line system. Environmental Protection Agency ("EPA") regulations, driven by the Clean Air Act, require refiners to change the composition of fuel manufactured. A pipeline's ability to respond to the effects of regulation and changing supply patterns will determine its ability to maintain and capture new market shares. Williams Pipe Line has successfully responded to changes in diesel fuel composition and product supply and has adapted to new gasoline additive requirements. Reformulated gasoline regulations have not yet significantly affected Williams Pipe Line. Williams Pipe Line will continue to attempt to position itself to respond to changing regulations and supply patterns but cannot predict how future changes in the marketplace will affect its market areas.

Ethanol. Williams Energy, through its wholly owned subsidiary Williams Energy Ventures, Inc. (WEV), is engaged in the production and marketing of ethanol. WEV owns and operates two ethanol plants of which com is the principal feedstock. The Pekin, Illinois, plant, which WEV purchased in 1995, has an annual production capacity of 100 million gallons of fuel-grade and industrial ethanol and also produces various coproducts. The Aurora, Nebraska, plant (in which WEV owns a 74.68 percent interest) began operations in November 1995 and has an annual production capacity of 30 million gallons. WEV also markets ethanol produced by third parties.

The sales volumes set forth below include ethanol produced by third parties as well as by WEV for the periods indicated:

	1997	1996	1995
Ethanol sold (thousands of gallons)	145,612	119,800	53,500
Coproducts sold (thousands of tons)		398	159

Terminals and Services. Williams Energy, through its subsidiary WEV, operates petroleum products terminals in the western and southeastern United States and provides services including performance additives and ethanol blending. In September 1996, WEV acquired a 45.5 percent interest in eight petroleum products terminals located in the southeast United States. In 1997, these terminals loaded approximately 17.3 million barrels of refined products. In December 1997, WEV acquired a terminal in Dallas, Texas. The preceding volume data do not reflect activity at this terminal.

ENERGY MARKETING AND TRADING

Williams Energy, through subsidiaries, primarily Williams Energy Services Company and its subsidiaries ("WESCO"), is a national energy services provider that buys, sells, and transports a full suite of energy commodities, including natural gas, electricity, refined products, natural gas liquids, crude oil, and liquefied natural gas, on a wholesale and retail level, serving over 3,500 companies. In addition, WESCO offers a comprehensive array of price-risk management products and services and capital services to the diverse energy industry.

WESCO markets natural gas throughout North America and grew its total volumes (physical and notional) to an average of 22.3 Bcf per éay in 1997. The core of WESCO's business has traditionally been the Gulf Coast and eastern regions, using the pipeline systems owned by the Company, but also includes marketing on approximately 50 non-Williams' pipelines. During 1997, approximately one-third of WESCO's volumes were from the Mid-Continent region, up from 10 percent in 1996. WESCO's natural gas customers include producers, industrials, local distribution companies, utilities, and other marketers.

During 1997, WESCO also marketed refined products, natural gas liquids, crude, and liquefied natural gas with total volumes (physical and notional) averaging 1,208.2 Mbbl per day. WESCO's acquisition in 1997 of the wholesale propane business of Level Energy significantly enhanced its natural gas liquids marketing effort.

WESCO entered the power marketing and trading business in 1996. During 1997, WESCO marketed 8.3 GWh per hour (physical and notional) of electricity.

WESCO provides price-risk management services through a variety of financial instruments including forwards, futures, and option and swap agreements related to various energy commodities. Through its energy capital services, WESCO provides participants in both the upstream and downstream portions of the energy industry with capital for energy-related projects including acquisitions of proved reserves and related drilling projects.

During 1997, WESCO has continued to develop its retail energy services group through acquisitions and alliances. As part of that strategy, WESCO acquired Utility Management Corporation, an energy management services and marketing company in the southeastern United States, serving small- to mid-sized

commercial, industrial, and municipal customers. WESCO also has signed a letter of intent with GPU Advanced Resources to form an alliance which will serve markets in six mid-Atlantic states.

Operating Statistics. The following table summarizes operating profit and marketing volumes for the periods indicated:

 Complete the Complete State of the Complete State of	1997	1996	1995
Average marketing volumes (physical and notional):	or and a		146
Natural gas (Bcfd)	22.3	15.9	10.2
Refined products, natural gas liquids, crude (MBpd)	1,202	384	19
Electricity (GWh/hr)	8.3	0.5	-

Regulatory Matters

Field Services. In May 1994, after reviewing its legal authority in a Public Comment Proceeding, FERC determined that while it retains some regulatory jurisdiction over gathering and processing performed by interstate pipelines, pipeline-affiliated gathering and processing companies are outside its authority under the Natural Gas Act. An appellate court has affirmed FERC's determination and the U.S. Supreme Court has denied requests for certiorari. As a result of these FERC decisions, some of the individual states in which Field Services conducts its operations have considered whether to impose regulatory requirements on gathering companies. Kansas, Oklahoma, and Texas currently regulate gathering activities using complaint mechanisms under which the state commission may resolve disputes involving an individual gathering arrangement. Other states may also consider whether to impose regulatory requirements on gathering companies.

Petroleum Services. Williams Pipe Line, as an interstate common carrier pipeline, is subject to the provisions and regulations of the Interstate Commerce Act. Under this Act, Williams Pipe Line is required, among other things, to establish just, reasonable and nondiscriminatory rates, to file its tariffs with FERC, to keep its records and accounts pursuant to the Uniform System of Accounts for Oil Pipeline Companies, to make annual reports to FERC and to submit to examination of its records by the audit staff of FERC. Authority to regulate rates, shipping rules, and other practices and to prescribe depreciation rates for common carrier pipelines is exercised by FERC. The Department of Transportation, as authorized by the 1995 Pipeline Safety Reauthorization Act, is the oversight authority for interstate liquids pipelines. Williams Pipe Line is also subject to the provisions of various state laws applicable to intrastate pipelines.

On December 31, 1989, a rate cap, which resulted from a settlement with several shippers, effectively freezing Williams Pipe Line's rates for the previous five years, expired. Williams Pipe Line filed a revised tariff on January 16, 1990, with FERC and the state commissions. The tariff set an average increase in rates of 11 percent and established volume incentives and proportional rate discounts. Certain shippers on the Williams Pipe Line system and a competing pipeline carrier filed protests with FERC alleging that the revised rates are not just and reasonable and are unlawfully discriminatory. Williams Pipe Line elected to bifurcate this proceeding in accordance with the then-current FERC policy. Phase I of FERC's bifurcated proceeding provides a carrier the opportunity to justify its rates and rate structure by demonstrating that its markets are workably competitive. Any issues unresolved in Phase I require cost justification in Phase II.

FERC's Presiding Judge issued the Initial Decision in Phase II on May 29, 1996. The Judge ruled that Williams Pipe Line failed to demonstrate that the rates at issue for the 12 less competitive markets were just and reasonable and that Williams Pipe Line must roll back those rates to pre-1990 levels and pay refunds with interest to its shippers. The Initial Decision held that Williams Pipe Line's individual rates must be judged on the basis of cost allocations, although Williams Pipe Line was given no notice of this particular basis of judgment and the Commission expressly declined to adopt such standards in its Opinion No. 391. Moreover, the Commission clarified its final order in Phase I (Opinion No. 391-A) by stating that Williams Pipe Line was not required to defend its rates with cost allocations. Primarily on this basis, Williams Pipe Line sought a review of the Initial Decision by the full Commission by filing a brief on exceptions on June 28, 1996. The review of the Phase II Initial Decision is pending before the Commission, and a shipper's appeal of the Phase I

order in the United States Court of Appeals for the District of Columbia Circuit has been stayed pending the completion of Phase II. Williams Pipe Line is not required to comply with the Initial Decision in Phase II prior to the Commission's issuance of a final order. Williams Pipe Line continues to believe that its revised tariffs will ultimately be found lawful. See Note 18 of Notes to Consolidated Financial Statements.

Energy Marketing and Trading. Management believes that WESCO's activities are conducted in substantial compliance with the marketing affiliate rules of FERC Order 497. Order 497 imposes certain nondiscrimination, disclosure, and separation requirements upon interstate natural gas pipelines with respect to their natural gas trading affiliates. WESCO has taken steps to ensure it does not share employees with affiliated interstate natural gas pipelines and does not receive information from such affiliates that is not also available to unaffiliated natural gas trading companies.

Competition

Exploration and Production. Williams Energy's exploration and production unit competes with a wide variety of independent producers as well as integrated oil and gas companies for markets for its production.

Field Services. Williams Energy competes for gathering and processing business with interstate and intrastate pipelines, producers, and independent gatherers and processors. Numerous factors impact any given customer's choice of a gathering or processing services provider, including rate, term, timeliness of well connections, pressure obligations, and the willingness of the provider to process for either a fee or for liquids taken in-kind.

Petroleum Services. Williams Energy's petroleum services operations are subject to competition because Williams Pipe Line operates without the protection of a federal certificate of public convenience and necessity that might preclude other entrants from providing like service in its area of operations. Further, Williams Pipe Line must plan, operate and compete without the operating stability inherent in a broad base of contractually obligated or owner-controlled usage. Because Williams Pipe Line is a common carrier, its shippers need only meet the requirements set forth in its published tariffs in order to avail themselves of the transportation services offered by Williams Pipe Line.

Competition exists from other pipelines, r. fineries, barge traffic, railroads, and tank trucks. Competition is affected by trades of products or crude oil between refineries that have access to the system and by trades among brokers, traders and others who control products. Such trades can result in the diversion from the Williams Pipe Line system of volume that might otherwise be transported on the system. Shorter, lower revenue hauls may also result from such trades. Williams Pipe Line also is exposed to interfuel competition whereby an energy form shipped by a liquids pipeline, such as heating fuel, is replaced by a form not transported by a liquids pipeline, such as electricity or natural gas. While Williams Pipe Line faces competition from a variety of sources throughout its marketing areas, the principal competition is other pipelines. A number of pipeline systems, competing on a broad range of price and service levels, provide transportation service to various areas served by the system. The possible construction of additional competing products or crude oil pipelines, conversions of crude oil or natural gas pipelines to products transportation, changes in refining capacity, refinery closings, changes in the availability of crude oil to refineries located in its marketing area, or conservation and conversion efforts by fuel consumers may adversely affect the volumes available for transportation by Williams Pipe Line.

Williams Energy's ethanol operations compete in local, regional, and national fuel additive markets with one large ethanol producer, numerous smaller ethanol producers, and other fuel additive producers, such as refineries.

Energy Marketing and Trading. Williams Energy's energy marketing and trading operations directly compete with large independent energy marketers, marketing affiliates of regulated pipelines and utilities, electric wholesalers and retailers, and natural gas producers. The financial trading business competes with other energy-based companies offering similar services as well as certain brokerage houses. This level of competition contributes to a business environment of constant pricing and margin pressure.

Ownership of Property

The majority of Williams Energy's ownership interests in exploration and production properties are held as working interests in oil and gas leaseholds.

Williams Energy's gathering and processing facilities are owned in fee. Gathering systems are constructed and maintained pursuant to rights-of-way, easements, permits, licenses, and consents on and across properties owned by others. The compressor stations and gas processing and treating facilities are located in whole or in part on lands owned by subsidiaries of Williams Energy or on sites held under leases or permits issued or approved by public authorities.

Williams Energy's petroleum pipeline system is owned in fee. However, a substantial portion of the system is operated, constructed and maintained pursuant to rights-of-way, easements, permits, licenses, or consents on and across properties owned by others. The terminals, pump stations, and all other facilities of the system are located on lands owned in fee or on lands held under long-term leases, permits, or contracts. Management believes that the system is in such a condition and maintained in such a manner that it is adequate and sufficient for the conduct of business.

The primary assets of Williams Energy's energy marketing and trading unit are its term contracts, employees, and related systems and technological support.

Environmental Matters

Williams Energy is subject to various federal, state, and local laws and regulations relating to environmental quality control. Management believes that Williams Energy's operations are in substantial compliance with existing environmental legal requirements. Management expects that compliance with such existing environmental legal requirements will not have a material adverse effect on the capital expenditures, earnings, and competitive position of Williams Energy.

The EPA has named Williams Pipe Line as a potentially responsible party as defined in Section 107(a) of the Comprehensive Environmental Response, Compensation, and Liability Act, for a site in Sioux Falls, South Dakota. The EPA placed this site on the National Priorities List in July 1990. In April 1991, Williams Pipe Line and the EPA executed an administrative consent order under which Williams Pipe Line agreed to conduct a remedial investigation and feasibility study for this site. The EPA issued its "No Action" Record of Decision in 1994, concluding that there were no significant hazards associated with the site subject to two additional years of monitoring for arsenic in certain ex sting monitoring wells. Williams Pipe Line completed monitoring in the second quarter of 1997 and has submitted a report of results to the EPA. Management believes no significant additional expenditures will be required for investigation and follow-up at this site.

WILLIAMS COMMUNICATIONS GROUP, INC. (Williams Communications)

As of December 31, 1997, Williams Communications has organized its operating companies into three business units: Solutions, which provides customer-premise voice and data equipment, including installation, integration, and maintenance; Network, which operates the Company's fiber optic network; and Applications, which provides video services and other multimedia services for the broadcast industry; advertising distribution; business television applications; and audio- and videoconferencing services and enhanced facsimile services for businesses. Management believes that the new structure will better position it to provide total enterprise network solutions and superior customer service. In addition, management believes this structure will facilitate growth and diversification while recognizing the convergence of customers, markets and product offerings of its communications entities. In Canada, Solutions operates through its subsidiary, WilTel Communications (Canada), Inc. In late 1997, Williams Communications announced plans to sell its product and content training services business, Williams Learning Network, Inc. See Note 6 of Notes to Consolidated Financial Statements.

Williams Communications and its subsidiaries own an approximately 11,000-mile communications network (with an additional 21,000-route miles planned or under construction), maintain 155 offices primarily across North America but also in London, Singapore, and Australia, service approximately 133,000 customer

sites with approximately 11 million customer ports. In addition, Williams Communications owns or manages five teleports in the United States and has rights to capacity on domestic and international satellite transponders. Williams Communications employed approximately 8,000 employees as of December 31, 1997.

Consolidated revenues by business unit and operating profit/loss for Williams Communications were as follows for 1997 (dollars in millions):

Revenues:	
Solutions	\$1,206.5
Network	43.0
Application	222.4
Eliminations	(26.6)
Total	\$1,445.3
Operating loss	\$ (55.7)

The revenues for the Solutions business unit include only eight months of revenues resulting from the merger, which is discussed below, with Nortel Communications Systems, Inc., effective April 30, 1997. The operating loss includes \$49.8 million in fourth quarter charges related to the previously noted decision to sell the learning content business and the write-down of assets and the development costs associated with certain advanced applications.

A business description of each of Williams Communications' business units follows.

SOLUTIONS

The Solutions unit of Williams Communications provides data, voice and video communications products and services to customers in the United States and Canada. In April 1997, Williams Communications merged its wholly owned subsidiary, Williams Telecommunications Systems, Inc. with Nortel Communications Systems Inc., which was a wholly owned subsidiary of Northern Telecom, Inc. (Northern Telecom). Williams Communications holds a 70 percent interest in the newly formed entity, Williams Communications Solutions, LLC (WCS). Northern Telecom owns the remaining 30 percent. This merger effectively doubled the size of Williams Communications Solutions Customer ρremise and network solutions operations.

Williams Communications, through subsidiaries including WCS, serves its customers through more than 120 sales and service locations throughout the United States, over 6,000 employees and over 2,200 stocked service vehicles. WCS employs more than 2,500 technicians and more than 700 sales representatives and sales support personnel to serve an estimated 133,000 commercial, governmental and institutional customer sites. WCS's customer base ranges from large, publicly-held corporations and the federal government to small privately-owned entities.

WCS offers its customers a full array of data, multimedia, voice and video network interconnect products including digital key systems (generally designed for voice applications with fewer than 100 lines), private branch exchange (PBX) systems (generally designed for voice applications with greater than 100 lines), voice processing systems, interactive voice response systems, automatic call distribution applications, call accounting systems, network monitoring and management systems, desktop video, routers, channel banks, intelligent hubs and cabling. WCS's services also include the design, configuration and installation of voice and data networks and call centers and the management of customers' telecommunications operations and facilities. WCS's National Technical Resource Center provides customers with on-line order entry and trouble reporting services, advanced technical assistance and training. Other service capabilities include Local Area Network and PBX remote monitoring and toll fraud detection.

Operating Statistics. The following table summarizes the results of operations for Williams Communications Solutions for the periods indicated (dollars and ports in millions):

A Secretary and Advisory and Advisory and Advisory	_	1997	1996	15	995
Revenues	SI	,206.5	\$568.1	\$49	94.9
Percentage of revenues by type of service:					
New system sales		52%	40%		34%
System modifications		28	34		36
Maintenance		19	24		25
Other		1	2		2
Backlog	S	202.5	\$112.2	5 5	85.0
Total ports		11.0	5.1		4.7

A port is defined as an electronic address resident in a customer's PBX or key system that supports a station, trunk, or data port.

In 1997, WCS derived approximately 47.8 percent of its revenues from its existing customer base and approximately 52.2 percent from the sale of new telecommunications systems. WCS's three largest suppliers accounted for approximately 86 percent of equipment sold in 1997. A single manufacturer, Northern Telecom, supplied 73 percent of all equipment sold. In this case, WCS is the largest independent distributor in the United States of certain of this company's products. About 63 percent of WCS's active customer base consists of this manufacturer's products. The distribution agreement with this supplier is scheduled to expire at the end of 2000. Management believes there is minimal risk as to the availability of products from suppliers.

NETWORK

The Network unit of Williams Communications owns and operates an approximately 11,000-route mile communications network, which is restricted to multi-media applications, and is currently constructing an unrestricted network along a 1,600 mile route from Houston to Washington, D.C. in proximity to pipeline right-of-way owned by an affiliated company. Williams Communications Inc., a subsidiary of Williams Communications, has entered into an exchange agreement with IXC Communications under which it will provide IXC Communications rights to use dark fiber along the Houston-to-Washington, D.C. route and obtain rights to use dark fiber along a 4,500-mile route from Los Angeles to New York, which IXC Communications is constructing. In addition, Williams Communications, Inc. also owns an interest in a joint venture constructing a 1,600-mile fiber optic network on a route connecting Portland, Salt Lake City, and Las Vegas, with a dark fiber agreement extending the network to Los Angeles. With these construction projects and dark fiber agreements and other projects, Williams Communications, Inc. anticipates having an 18,000route mile fiber optic network in operation by the end of 1998. Williams Communications, Inc. has also signed an agreement to acquire a 350-mile fiber network in Florida and plans to construct additional fiber to connect the Florida network to its existing network in the southeastern United States, and to construct a new fiber route in the Midwestern United States from Chicago westward. The Network unit has ultimate plans for a 32,000-route mile network.

Upon the expiration of the non-compete agreement related to the Company's 1995 sale of its network services operations on January 5, 1998, Williams Communications announced that it was re-entering the long-distance communications market as a wholesale provider of telecommunications services and had entered into a five-year, multimillion dollar agreement with U S WEST Communications Group to provide wholesale services using its fiber optic network. Williams Communications has also entered into an agreement with Concentric Network Corporation to provide wholesale communications services.

During 1997, Williams Communications acquired Critical Technologies, Inc., a professional services company deriving revenue from integrating, designing, building, implementing, and maintaining large-scale business communications systems. In addition, Williams Communications acquired a 12.5 percent interest in Concentric Network Corporation, a provider of Internet protocol-based networking services for business and consumer markets.

APPLICATIONS

Vvvx

Vyvx, an unincorporated business unit of Williams Communications, Inc., offers broadcast-quality television and multimedia transmission services nationwide by means of Network's 11,000-mile multimedia network, five satellite uplink/downlink facilities and satellite capacity on 30 transponders. Vyvx owns 53 television switching centers, 20 sales and service locations in the United States, and sales and service offices in London, Singapore, and Australia. Vyvx primarily provides backhaul or point-to-point transmission of sports, news and other programming between two or more customer locations. With satellite facilities, Vyvx provides point-to-multipoint transmission service. Vyvx's customers include all of the major broadcast and cable networks. Vyvx is also engaged in the business of advertising distribution and is exploring other multimedia communication opportunities.

Vyvx owns four teleports (including satellite earth station facilities) located near Atlanta, Denver, Los Angeles, and New York, and operates a fifth teleport in Kansas City. Vyvx also owns assets for the distribution of television advertising, which provide connectivity and presence in more than 550 television broadcast stations around the country.

Global Access

Global Access, offers multi-point videoconferencing, audioconferencing and enhanced facsimile services as well as single point to multi-point business television services. Global Access enables Williams Communications to provide customers with integrated media conferences, bringing together voice, video and facsimile by utilizing Williams Communications's existing fiber-optic and satellite services.

In March 1997, Global Access acquired Satellite Management, Inc., a U.S.-based satellite integrator for business television applications, interactive long distance learning, and corporate communications.

In December 1996, Williams Communications announced the formation of The Business Channel, a joint venture with the Public Broadcast Service (PBS), to utilize Internet, video-on-demand, fiber-optic and satellite technologies to bring professional development and training services to the business community.

Regulatory Matters

The equipment WCS sells must meet the requirements of Part 68 of the Federal Communications Commission (FCC) rules governing the equipment registration, labeling and connection of equipment to telephone networks. WCS relies on the equipment manufacturers' compliance with these requirements for its own compliance regarding the equipment it distributes. These regulations have a minimal impact on WCS's operations.

Williams Communications, Inc. is subject to FCC regulations as common carriers with regard to certain of their transmission services and are subject to the laws of certain states governing public utilities. An FCC rulemaking to eliminate domestic, common carrier tariffs has been stayed pending judicial review. In the interim, the FCC is requiring such carriers to operate under traditional tariff rules. Operations of intrastate microwave communications, satellite earth stations and certain other related transmission facilities are also subject to FCC licensing and other regulations. These regulations do not significantly impact Williams Communications, Inc.'s operations. In 1997, the FCC began implementation of the Universal Service Fund contemplated in the Telecommunications Act of 1996. Williams Communications, Inc. is required to contribute to this fund based upon certain revenues. Although Williams Communications, Inc. intends to pass on such charges to its customers, FCC rulings raise questions about the right of companies like Williams Communications, Inc. to do so.

Competition

WCS has many competitors ranging from Lucent Technologies and the Regiona! Bell Operating Companies to small individually-owned companies that sell and service customer premise equipment.

Competitors include companies that sell equipment comparable or identical to that sold by WCS. There are virtually no barriers to entry into this market.

Vyvx's video and multimedia transmission operations compete primarily with companies offering video or multimedia transmission services by means of satellite facilities and to a lesser degree with companies offering transmission services via microwave facilities or fiber-optic cable.

Network faces existing competition from a number of large, well-established interexchange carriers, some with extensive fiber optic networks. Several other carriers are constructing or have plans to construct new fiber optic networks or are establishing networks based on dark fiber rights obtained from facilities-based carriers.

Federal telecommunications reform legislation enacted in February 1996 is designed to increase competition both in the long distance market and local exchange market by significantly liberalizing current restrictions on market entry. In particular, the legislation establishes procedures permitting Regional Bell Operating Companies to provide long distance services including, but not limited to, video transmission services, subject to certain restrictions and conditions precedent. Moreover, electric and gas utilities may provide telecommunications services, including long distance services, through separate subsidiaries. The legislation also calls for elimination of federal tariff filing requirements and relaxation of regulation over common carriers. At this time, management cannot predict the impact such legislation may have on the operations of Williams Communications, Inc.

In late 1997, a Federal District Court decision, which has been stayed pending appeal, invalidated provisions of the 1996 federal legislation. While legislation or rulings by appellate courts may overturn this lower court ruling, the Regional Bell Operating companies continue to seek regulatory approval to provide national long distance services. As courts or regulators remove restrictions on the Regional Bell Operating Companies, they will be both important potential customers and important potential competitors of Network.

Ownership of Property

Williams Communications owns part of its fiber-optic transmission facilities and leases the remainder. Approximately 11,000-route miles of its owned facilities are comprised of a single fiber, which is on a portion of the fiber optic network of WorldCom, Inc. ("WorldCom") and is restricted to multimedia content usage. Williams Communications retained this fiber when a predecessor of WorldCom purchased the Company's network services operations in 1995. Williams Communications and WorldCom are currently in litigation to clarify, among other things, whether the usage restriction would permit internet services and Williams Communications' right to purchase additional WorldCom fiber. Williams Communications carries signals by means of its own fiber-optics facilities, as well as carrying signals over fiber-optic facilities leased from third-party interexchange carriers and the various local exchange carriers. Williams Communications holds its satellite transponder capacity under various agreements. Williams Communications owns part of its teleport facilities and holds the remainder under either a management agreement or long-term facilities leases.

Williams Network intends to obtain capacity primarily by means of the fiber optic networks Williams Communications is constructing or plans to construct or acquire, as well as acquiring dark fiber rights on fiber optic facilities of other carriers. Network obtains dark fiber rights in the form of the purchase or lease of "indefeasible rights of use" or "IRUs" in specific fiber strands. Purchased IRUs have many of the characteristics of ownership, including many of the associated risks, but the owner of the fiber optic cable retains legal title to the fibers.

Environmental Matters

Williams Communications is subject to federal, state, and local laws and regulations relating to the environmental aspects of its business. Management believes that Williams Communications' operations are in substantial compliance with existing environmental legal requirements. Management expects that compliance with such existing environmental legal requirements will not have a material adverse effect on the capital expenditures, earnings and competitive position of Williams Communications.

OTHER INFORMATION

Williams believes that it has adequate sources and availability of raw materials to assure the continued supply of its services and products for existing and anticipated business needs. Williams' pipeline systems are all regulated in various ways resulting in the financial return on the investments made in the systems being limited to standards permitted by the regulatory bodies. Each of the pipeline systems has ongoing capital requirements for efficiency and mandatory improvements, with expansion opportunities also necessitating periodic capital outlays.

A plant site in Pensacola, Florida, that was previously operated by a former subsidiary of Williams, has been placed on the National Priorities List. This former subsidiary has also been identified as a potentially responsible party at a National Priorities List cleanup site in Michigan. A third site, located in Lakeland, Florida, which was formerly owned and operated by this subsidiary, is under investigation by the Florida Department of Environmental Protection and cleanup is anticipated. Williams does not believe that the ultimate resolution of the foregoing matters, taken as a whole and after consideration of insurance coverage, contribution or other indemnification arrangements, will have a material adverse financial effect on the Company. See Note 18 of Notes to Consolidated Financial Statements.

At December 31, 1997, the Company had approximately 15,000 full-time employees, of whom approximately 2,300 were represented by unions and covered by collective bargaining agreements. The Company considers its relations with its employees to be generally good.

Forward-Looking Information

Certain matters discussed in this report, excluding historical information, include forward-looking statements. Although the Company believes such forward-looking statements are based on reasonable assumptions, no assurance can be given that every objective will be reached. Such statements are made in reliance on the safe harbor protections provided under the Private Securities Litigation Reform Act of 1995.

As required by such Act, the Company hereby identifies the following important factors that could cause actual results to differ materially from any results projected, forecasted, estimated or budgeted by the Company in forward-looking statements: (i) risks and uncertainties impacting the Company as a whole relate to changes in general economic conditions in the United States; the availability and cost of capital; changes in laws and regulations to which the Company is subject, including tax, environmental and employment laws and regulations; the cost and effects of legal and administrative claims and proceedings against the Company or its subsidiaries or which may be brought against the Company or its subsidiaries; conditions of the capital markets utilized by the Company to access capital to finance operations; and, to the extent the Company increases its investments and activities abroad, such investments and activities will be subject to foreign economies, laws, and regulations; (ii) for the Company's regulated businesses, risks and uncertainties primarily relate to the impact of future federal and state regulations of business activities, including allowed rates of return and the resolution of other matters discussed herein; and (iii) risks and uncertainties associated with the Company's unregulated businesses primarily relate to energy prices and the ability of such entities to develop expanded markets and product offerings as well as their ability to maintain existing markets. It is also possible that certain aspects of the Company's businesses that are currently unregulated may be subject to both federal and state regulation in the future. In addition, future utilization of pipeline capacity will depend on energy prices, competition from other pipelines and alternate fuels, the general level of natural gas and petroleum product demand and weather conditions, among other things. Further, gas prices, which directly impact transportation and gathering and processing throughput and operating profit, may fluctuate in unpredictable ways as may corn prices, which directly affect the Company's ethanol business. Factors impacting future results of the Company's communications business include successful completion of its network build, technological developments, high levels of competition, lack of customer diversification, and general uncertainties of governmental regulation.

(d) Financial Information about Foreign and Domestic Operations and Export Sales

Williams has no significant foreign operations.

Item 2. Properties

See Item 1(c) for description of properties.

Item 3. Legal Proceedings

For information regarding certain proceedings pending before federal regulatory agencies, see Note 18 of Notes to Consolidated Financial Statements. Williams is also subject to other ordinary routine litigation incidental to its businesses.

Contract reformations and gas purchase deficiencies

As a result of FERC Order 636, which requires interstate gas pipelines to change the way they do business, each of the natural gas pipeline subsidiaries has undertaken the reformation or termination of its respective gas supply contracts. None of the pipelines has any significant pending supplier take-or-pay, ratable take or minimum take claims.

Current FERC policy associated with Orders 436 and 500 requires interstate gas pipelines to absorb some of the cost of reforming gas supply contracts before allowing any recovery through direct bill or surcharges to transportation as well as sales commodity rates. Under Orders 636, 636-A, 636-B and 636-C, costs incurred to comply with these rules are permitted to be recovered in full, although a percentage of such costs must be allocated to interruptible transportation service.

Pursuant to a stipulation and agreement approved by the FERC, Williams Gas Pipelines Central (Central) has made 11 filings to direct bill take-or-pay and gas supply realignment costs. The total amount approved for direct billing, net of certain amounts collected subject to refunds, is \$67 million. An intervenor has filed protests seeking to have the FERC review the prudence and eligibility of approximately \$40 million of costs covered by these filings. On July 31, 1990, the administrative law judge issued an initial decision rejecting the intervenor's prudency challenge. On September 30, 1997, the FERC, by a two-to-one vote, reversed the administrative law judge and determined that three life-of-lease producer contracts were imprudently entered into in 1982. Central has filed for rehearing, and management plans to vigorously defend the prudency of these contracts. An intervenor has also filed a protest seeking to have the FERC decide whether non-settlement costs are eligible for recovery under Order No, 636. In January 1997, the FERC held that none of the non-settlement costs could be recovered by Central if these costs were not eligible for recovery under Order No. 636. This order was affirmed on rehearing in April 1997. An initial decision from the administrative law judge is expected in the first quarter of 1998. If the FERC's final ruling on eligibility is unfavorable, Central will appeal these orders to the courts. Central will make additional filings under the applicable FERC orders to recover such additional costs as may be incurred in the future.

Because of the uncertainties pertaining to the outcome of these issues currently pending at the FERC and the status of settlement negotiation and various other factors. Central cannot reasonably estimate the costs that may be incurred nor the related amounts that could be recovered from customers. Central is actively pursuing negotiations with the producers to resolve all outstanding obligations under the contracts. Based on the terms of what Central believes would be a reasonable settlement, \$94 million has been accrued as a liability at December 31, 1997, including a \$5 million fourth-quarter 1997 charge to expense for additional absorption of future costs. Central also has an \$88 million regulatory asset at December 31, 1997, for estimated recovery of future costs from customers. Central cannot predict the final outcome of the FERC's rulings on contract prudency and cost recovery under Order No. 636 and is unable to determine the ultimate liability and loss, if any, at this time. If Central does not prevail in these FERC proceedings or any subsequent appeals, and if Central is able to reach a settlement with the producers consistent with the \$94 million accrued liability, the loss could be the total of the regulatory asset and the \$40 million of protested assets. Central continues to believe that it entered into the gas purchase contracts in a prudent manner under FERC rules in place at the time. Central also believes that the future recovery of these costs would be in accordance with the terms of Order No. 636.

The foregoing accruals are in accordance with Williams' accounting policies regarding the establishment of such accruals which take into consideration estimated total exposure, as discounted and risk-weighted, as well as costs and other risks associated with the difference between the time costs are incurred and the time such costs are recovered from customers. The estimated portion of such costs recoverable from customers is deferred or recorded as a regulatory asset based on an estimate of expected recovery of the amounts allowed by FERC policy. While Williams believes that these accruals are adequate and the associated regulatory assets are appropriate, costs actually incurred and amounts actually recovered from customers will depend upon the outcome of various court and FERC proceedings, the success of settlement negotiations and various other factors, not all of which are presently foreseeable.

Environmental matters

Since 1989, Texas Gas and Transcontinental Gas Pipe Line have had studies under way to test certain of their facilities for the presence of toxic and hazardous substances to determine to what extent, if any, remediation may be necessary. Transcontinental Gas Pipe Line has responded to data requests regarding such potential contamination of certain of its sites. The costs of any such remediation will depend upon the scope of the remediation. At December 31, 1997, these subsidiaries had reserves totaling approximately \$28 million for these costs.

Certain Williams subsidiaries, including Texas Gas and Transcontinental Gas Pipe Line, have been identified as potentially responsible parties (PRP) at various Superfund and state waste disposal sites. In addition, these subsidiaries have incurred, or are alleged to have incurred, various other hazardous materials removal or remediation obligations under environmental laws. Although no assurances can be given, Williams does not believe that the PRP status of these subsidiaries will have a material adverse effect on its financial position, results of operations or net cash flows.

Transcontinental Gas Pipe Line, Texas Gas and Central have identified polychlorinated biphenyl (PCB) contamination in air compressor systems, soils and related properties at certain compressor station sites. Transcontinental Gas Pipe Line, Texas Gas and Central have also been involved in negotiations with the U.S. Environmental Protection Agency (EPA) and state agencies to develop screening, sampling and cleanup programs. In addition, negotiations with certain environmental authorities and other programs concerning investigative and remedial actions relative to potential mercury contamination at certain gas metering sites have been commenced by Central, Texas Gas and Transcontinental Gas Pipe Line. As of December 31, 1997. Central had recorded a liability for approximately \$17 million, representing the current estimate of future environmental cleanup costs to be incurred over the next six to ten years. The Field Services unit of Energy Services had recorded an aggregate liability of approximately \$12 million, representing the current estimate of its future environmental and remediation costs, including approximately \$5 million relating to former Central facilities. Texas Gas and Transcontinental Gas Pipe Line likewise had recorded liabilities for these costs which are included in the \$28 million reserve mentioned above. Actual costs incurred will depend on the actual number of contaminated sites identified, the actual amount and extent of contamination discovered, the final cleanup standards mandated by the EPA and other governmental authorities and other factors. Texas Gas, Transcontinental Gas Pipe Line and Central have deferred these costs pending recovery as incurred through future rates and other means.

In connection with the 1987 sale of the assets of Agrico Chemical Company, Williams agreed to indemnify the purchaser for environmental cleanup costs resulting from certain conditions at specified locations, to the extent such costs exceed a specified amount. Such costs have exceeded this amount. At December 31, 1997, Williams had approximately \$11 million accrued for such excess costs. The actual costs incurred will depend on the actual amount and extent of contamination discovered, the final cleanup standards mandated by the EPA or other governmental authorities, and other factors.

A lawsuit was filed in May 1993 in a state court in Colorado in which certain claims have been made against various defendants, including Northwest Pipeline, contending that gas exploration and development activities in portions of the San Juan Basin have caused air, water and other contamination. The plaintiffs in the case sought certification of a plaintiff class. In June 1994, the lawsuit was dismissed for failure to join an

indispensable party over which the state court had no jurisdiction. The Colorado court of appeals has affirmed the dismissal and remanded the case to Colorado district court for action consistent with the appeals court's decision. Since June 1994, eight individual lawsuits have been filed against Northwest Pipeline and others in U.S. district court in Colorado, making essentially the same claims. The district court has stayed all of the cases involving Northwest Pipeline until the plaintiffs exhaust their remedies before the Southern Ute Indian Tribal Court. Some plaintiffs filed cases in the Tribal court, but none named Northwest Pipeline as a defendant.

Other legal matters

Williams Communications owns one fiber, which is restricted to media content usage, on a portion of the fiber optic network of WorldCom, Inc. ("WorldCom"). Williams Communications retained this fiber, along with an option to purchase additional fiber from WorldCom in connection with WorldCom's subsequent fiber builds, acquisitions, and expansions, when a predecessor of WorldCom purchased the Company's network services operations in 1995. On March 20, 1998, Williams Communications filed suit in Oklahoma District Court in Tulsa County against WorldCom claiming that WorldCom had failed to fulfill its obligations associated with the single fiber as well as a number of other obligations arising from the agreements entered into in 1995 in conjunction with the network services operations sale.

In 1991, the Southern Ute Indian Tribe (the Tribe) filed a lawsuit against Williams Production Company (Williams Production), a wholly-owned subsidiary of Williams, and other gas producers in the San Juan Basin area, alleging that certain coal strata were reserved by the United States for the benefit of the Tribe and that the extraction of coal-seam gas from the coal strata was wrongful. The Tribe seeks compensation for the value of the coal-seam gas. The Tribe also seeks an order transferring to the Tribe ownership of all of the defendants' equipment and facilities utilized in the extraction of the coal-seam gas. In September 1994, the court granted summary judgment in favor of the defendants and the Tribe lodged an interlocutory appeal with the U.S. Court of Appeals for the Tenth Circuit. Williams Production agreed to indemnify the Williams Coal Seam Gas Royalty Trust (Trust) against any losses that may arise in respect of certain properties subject to the lawsuit. In addition, if the Tribe is successful in showing that Williams Production has no rights in the coalseam gas, Williams Production has agreed to pay to the Trust for distribution to then-current unitholders, an amount representing a return of a portion of the original purchase price paid for the units. On July 16, 1997, the U.S. Court of Appeals for the Tenth Circuit reversed the decision of the district court, held that the Tribe owns the coal-seam gas produced from certain coal strata on fee lands within the exterior boundaries of the Tribe's reservation, and remanded the case to the district court for further proceedings. On September 16. 1997. Amoco Production Company, the class representative for the defendant class (of which Williams Production is a part), filed its motion for rehearing en banc before the Court of Appeals. On December 4. 1997, the Tenth Circuit Court of Appeals agreed to rehear the appeal.

In connection with agreements to resolve take-or-pay and other contract claims and to amend gas purchase contracts. Transcontinental Gas Pipe Line and Texas Gas each entered into certain settlements with producers which may require the indemnification of certain claims for additional royalties which the producers may be required to pay as a result of such settlements. In one of the two remaining cases, a jury verdict found that Transcontinental Gas Pipe Line was required to pay to a producer damages of \$23.3 million including \$3.8 million in attorneys' fees. Transcontinental Gas Pipe Line is considering an appeal. In the other remaining case, a producer has asserted damages, including interest calculated through December 31, 1996, of approximately \$6 million.

Summary

While no assurances may be given, Williams does not believe that the ultimate resolution of the foregoing matters, taken as a whole and after consideration of amounts accrued, insurance coverage, recovery from customers or other indemnification arrangements, will have a materially adverse effect upon Williams' future financial position, results of operations or cash flow requirements.

Item 4. Submission of Matters to a Vote of Security Holders

Not applicable.

Executive Officers of Williams

The names, ages, positions and earliest election dates of the executive officers of Williams are:

Name	Age	Positions and Offices Held	Held Office Since
Keith E. Bailey	55	Chairman of the Board, President, Chief Executive Officer and Director (Principal Executive Officer)	05-19-94
John C. Bumgarner, Jr	55	Senior Vice President — Corporate Development and Planning; President — Williams International Company	01-01-79
James R. Herbster	56	Senior Vice President — Administration	01-01-92
Jack D. McCarthy	55	Senior Vice President — Finance (Principal Financial Officer)	01-01-92
William G. von Glahn	54	Senior Vice President and General Counsel	08-01-96
Gary R. Belitz	48	Controller (Principal Accounting Officer)	01-01-92
Stephen L. Cropper	48	President - Williams Energy Group	10-01-96
Howard E. Janzen	44	President and Chief Operating Officer — Williams Communications, Inc.	02-11-97
Brian E. O'Neill	62	President — Williams Interstate Natural Gas Systems, Inc.	01-01-88

All of the above officers have been employed by Williams or its subsidiaries as officers or otherwise for more than five years and have had no other employment during such period.

PART II

Item 5. Market for the Registrant's Common Equity and Related Stockholder Matters

WMB." At the close of business on December 31, 1997, Williams had approximately 12,250 holders of record of its Common Stock. The daily closing price ranges (composite transactions) and dividends declared by quarter for each of the past two years (adjusted to reflect the December 29, 1997, two-for-one common stock split and distribution) are as follows:

		1997			1996	
Quarter	High	Low.	Dividend	High	I.ow	Diridend
1st	\$23.38	\$18.19	\$.13	\$17.00	\$14.25	\$.114
2nd	\$23.50	\$20.00	\$.13	\$17.71	\$15.58	\$.113
3rd	\$24.59	\$21.56	\$.13	\$17.29	\$15.25	\$.113
4th	\$28.50	\$23.09	\$.15	\$19.16	\$16.25	\$.13

On December 29, 1997, the Company distributed one additional share of Common Stock of the Company, \$1 par value, for every share of Common Stock outstanding on December 5, 1997, pursuant to a two-for-one stock split.

Item 6. Selected Financial Data

The following financial data are an integral part of, and should be read in conjunction with, the consolidated financial statements and notes thereto. Information concerning significant trends in the financial condition and results of operations is contained in Management's Discussion and Analysis of Financial Condition and Results of Operations on pages F-1 through F-13 of this report.

CONTRACTOR OF THE STATE OF THE	1997	1996	1995	1994	1993
	-	(Millions, e	acept per-share	amounts)	
Revenues	\$ 4,409.6	\$ 3,531.2	\$ 2,855.7	\$1,751.1	\$1,793.4
Income from continuing operations(1)	350.5	362.3	299.4	164.9	185.4
Income from discontinued operations(2)	_	_	1,018.8	94.0	46.4
Extraordinary loss(3)	(79.1)	_	-	(12.2)	-
Diluted earnings per share:(4)					
Income from continuing operations	1.04	1.07	.92	.51	.57
Income from discontinued operations	Or -	-	3.25	.30	.15
Extraordinary loss(3)	(.24)	-4.		(.04)	
Cash dividends per common share(4)	.54	.47	.36	.28	.26
Total assets at December 31	13,879.0	12,418.8	10,561.2	5,226.1	5,020.4
Long-term obligations at December 31		4,376.9	2,874,0	1,307.8	1,604.8
Stockholders' equity at December 31	3,571.7	3,421.0	3,187.1	1,505.5	1,724.0

- (1) See Notes 2 and 6 of Notes to Consolidated Financial Statements for discussion of the gain on sale of interest in subsidiary, significant asset sales and write-offs in 1997, 1996 and 1995. Income from continuing operations in 1994 includes a \$22.7 million pre-tax gain from the sale of a portion of Williams' interest in Northern Border Partners, L.P. Income from continuing operations in 1993 includes a pre-tax gain of \$51.6 million as a result of the sale of 6.1 million units in the Williams Coal Seam Gas Royalty Trust.
- (2) See Note 3 of Notes to Consolidated Financial Statements for discussion of the gain from the 1995 sale of discontinued operations. Amounts prior to 1995 reflect operating results of the network services' operations.
- (3) See Note 8 of Notes to Consolidateu Financial Statements for discussion of the 1997 extraordinary loss.
- (4) Per-share amounts reflect the adoption of Statement of Financial Accounting Standards No. 128, "Earnings per Share," and the effect of the December 29, 1997, common stock split and distribution as discussed in Notes 1 and 15, respectively, of Notes to Consolidated Financial Statements.

Item 7. Management's Discussion & Analysis of Financial Conditions, and Results of Operations Results of Operations

1997 vs. 1996

Central's revenues increased \$6 million, or 3 percent, due primarily to the net effect of adjustments to certain accruals in 1997. Total throughput decreased 4.2 TBtu, or 1 percent, due primarily to lower interruptible volumes.

Other (income) expense — net includes a \$1 million gain from the sale-in-place of natural gas from a decommissioned storage field.

Operating profit increased \$12.2 million, or 27 percent, due primarily to the gain from the sale-in-place of natural gas, lower operating and maintenance expenses, an increase in firm reserved capacity and lower general and administrative expenses.

Kern River Gas Transmission's (Kern River) revenues increased \$6.5 million, or 4 percent, due primarily to a full year of Williams' ownership in 1997 as compared to 1996 and increased transportation revenues. Results for 1996 reflect operations from January 16, 1996, when Williams acquired the remaining interest in

Kern River. Total throughput increased 15.5 TBtu, or 6 percent, due primarily to the full year of Williams' ownership in 1997 and increased firm transportation volumes during the last half of 1997.

Operating profit increased \$7.3 million, or 6 percent, due primarily to the full year of Williams' ownership in 1997, higher transportation revenues and lower operations and maintenance expenses, partially offset by the impact of Kern River's levelized rate design.

Northwest Pipeline's revenues increased \$3.4 million, or 1 percent, due primarily to a new rate design, effective March 1, 1997, that enabled greater short-term firm and interruptible transportation volumes and a \$3.5 million gain on the sale of system balancing gas. Largely offsetting these increases were \$7 million of adjustments to rate refund accruals in 1997 and the effect of \$9 million of revenue in 1996 associated with reserve reversals and favorable regulatory decisions. Total throughput decreased 120.3 TBtu, or 14 percent, as a result of the 1996 sale of the south-end facilities.

Operating profit decreased \$900,000, or 1 percent, due primarily to the combined impact of the increase to rate reserve accruals in 1997 and recognition in 1996 of favorable regulatory actions, significantly offset by the new transportation rates effective in 1997, lower operating and maintenance expenses and the \$3.5 million gain on the sale of system balancing gas.

Texas Gas Transmission's revenues decreased \$13.1 million, or 4 percent, and costs and operating expenses decreased \$13 million, or 8 percent, due primarily to lower reimbursable costs passed through to customers as provided in Texas Gas' rates including \$6 million related to the suspension of gas supply realignment cost recovery from firm transportation customers. Total throughput decreased 20.9 TBtu, or 3 percent.

Operating profit increased \$2.5 million, or 3 percent, due primarily to cost reductions and efficiency efforts and the favorable resolutions in 1997 of certain contractual and regulatory issues, partially offset by lower gas processing revenue and favorable 1996 adjustments to rate refund accruals.

Transcontinental Gas Pipe Line's (Transco) revenues increased \$5.9 million, or 1 percent, due primarily to the effects of a mainline expansion placed into service in late 1996, new services begun in late 1997, new rates effective May 1, 1997, to recover costs associated with increased capital expenditures, and the effects of a 1996 downward adjustment (offset in costs) of \$14 million to reflect a rate case settlement, partially offset by \$23 million of lower reimbursable costs passed through to customers as provided in Transco's rates. Total throughput decreased 21.1 TBtu, or 1 percent, due primarily to milder weather during 1997 as compared to 1996, which lowered firm long-haul and production area interruptible transportation volumes.

Costs and operating expenses decreased \$17.3 million, or 4 percent, due primarily to the lower reimbursable costs charged to Transco and passed through to customers, lower operation and maintenance expenses and a \$5.4 million settlement related to a prior rate proceeding, partially offset by the effect of a 1996 downward adjustment (offset in revenues) of \$14 million to depreciation expense to reflect a rate case settlement and higher depreciation expense in 1997 associated with recent capital expenditures.

Operating profit increased \$30.7 million, or 16 percent, due primarily to lower operation and maintenance expenses, the \$5.4 million settlement and the effects of the mainline expansion, new services and the new rates effective May 1, 1997, slightly offset by higher depreciation expense.

Energy Marketing & Trading's revenues decreased \$125.3 million, or 48 percent, and costs and operating expenses decreased \$141 million, or 93 percent, due primarily to the 1997 reporting on a net margin basis of certain natural gas and gas liquids marketing operations previously not considered to be included in trading operations. Excluding this decrease, revenues increased \$16 million due primarily to the initial income recognition from long-term electric power contracts, increased physical and notional natural gas volumes of 22 percent and 44 percent, respectively, and higher petroleum trading volumes, partially offset by lower natural gas trading margins as a result of decreased price volatility. Revenues also increased from project financing services for energy producers and the sale of excess transportation capacity.

Operating profit increased \$4.2 million, or 6 percent, due primarily to the \$16 million increase in net revenues and a \$6.3 million recovery of an account previously written off, largely offset by the expenses associated with expansion of business growth platforms.

Exploration & Production's revenues increased \$47.7 million, or 58 percent, due primarily to higher average natural gas sales prices for company-owned production and from the marketing of Williams Coal Seam Gas Royalty Trust (Royalty Trust) natural gas, and a 21 percent increase in company-owned production volumes.

Costs and operating expenses increased \$23 million, or 32 percent, due primarily to higher Royalty Trust natural gas purchase prices, increased production activities and higher dry hole costs.

Operating profit increased \$27.5 million, from \$2.8 million in 1996, due primarily to the increase in average natural gas prices and company-owned production volumes, partially offset by higher expenses associated with increased activity levels.

Field Services' revenues increased \$74 million, or 12 percent, due primarily to higher natural gas liquids sales of \$44 million, receipt of \$8 million of business interruption insurance proceeds related to a 1996 claim, and higher gathering, processing and condensate revenues of \$7 million, \$5 million and \$11 million, respectively. Natural gas liquids sales increased due to a 37 percent increase in volumes, slightly offset by lower average sales prices.

Costs and operating expenses increased \$79 million, or 20 percent, due primarily to \$56 million higher fuel and replacement gas purchases, a \$9 million increase in operating and maintenance expenses, and \$8 million higher depreciation.

Other (income) expense — net for 1996 includes a \$20 million gain from the property insurance coverage associated with construction of replacement gathering facilities and \$6 million of gains from the sale of two small gathering systems, partially offset by \$5 million of environmental remediation accruals.

Operating profit decreased \$24.4 million, or 13 percent, due primarily to lower per-unit liquids margins, the \$12 million net effect of lower insurance recoveries between 1997 and 1996, higher operating and maintenance expenses, increased depreciation, and higher gathering fuel and replacement gas purchase costs, partially offset by increased liquids and processing volumes.

Petroleum Services' revenues increased \$55.4 million, or 11 percent, due primarily to a \$24 million increase in product sales from transportation activities and a \$27 million increase in ethanol sales. Ethanol sales increased as a result of 22 percent higher sales volumes, partially offset by lower average ethanol sales prices. Ethanol production was reduced during the second half of 1996 due to unfavorable market conditions. Pipeline shipments and average rates were comparable to 1996.

Costs and operating expenses increased \$33 million, or 9 percent, due primarily to the increase in refined product sales and ethanol production, partially offset by lower corn costs.

Operating profit increased \$21.3 million, or 28 percent, due primarily to increased ethanol sales volumes and per-unit margins.

Communications' revenues increased \$734 million, or 103 percent, due primarily to acquisitions which contributed revenues of approximately \$650 million, including \$536 million from the acquisition of the customer premise equipment sales and services operations of Northern Telecom. Additionally, increased business activity resulted in a \$119 million revenue increase in new system sales, partially offset by a \$46 million decrease in system modification revenue. The number of ports in service at December 31, 1997, more than doubled as compared to December 31, 1996, due primarily to the Nortel acquisition. Fiber billable minutes from occasional service increased 47 percent. Dedicated service voice-grade equivalent miles at December 31, 1997, increased 26 percent as compared with December 31, 1996.

Costs and operating expenses increased \$550 million, or 102 percent, due primarily to acquired operations, the overall increase in business activity, higher expenses for developing advanced network applications and increased depreciation associated with added capacity. Selling, general and administrative

expenses increased \$198 million, or 121 percent, due primarily to acquired operations, the overall increase in business activity, higher expenses for developing advanced network applications and expanding the infrastructure of this business for future growth.

Other (income) expense — net includes \$49.8 million of charges in 1997 related to the decision to sell the learning content business, and the write-down of assets and the development expenses associated with certain advanced applications.

Operating profit decreased \$62.3 million from a \$6.6 million operating profit in 1996 to a \$55.7 million operating loss in 1997, due primarily to the other expense charges of \$49.8 million and the expense of developing infrastructure while integrating the most recent acquisitions, partially offset by improved operating profit from Communications Solutions including the impact of the Nortel acquisition.

General corporate expenses increased \$9.5 million, or 23 percent, due primarily to costs related to the pending MAPCO acquisition and higher consulting fees. Interest accrued increased \$44.6 million, or 12 percent, due primarily to higher borrowing levels including increased borrowing under the \$1 billion bank-credit facility and Williams Holdings' commercial paper program, partially offset by a lower average interest rate. The lower average interest rate reflects lower rates on new 1997 borrowings as compared to previously outstanding borrowings. Interest capitalized increased \$9 million, or 132 percent, due primarily to capital expenditures for Communications' fiber-optic network. For information concerning the 1997 gain on sale of interest in subsidiary, see Note 2. The 1996 gain on sales of assets results from the sale of certain communication rights. The minority interest in income of consolidated subsidiaries in 1997 is related primarily to the 30 percent interest held by Williams Communications Solutions, LLC's minority shareholders (see Note 2). The \$12 million unfavorable change in other income (expense) — net in 1997 is due primarily to the costs associated with expansion of the sale of receivables program in 1997 and the effect of \$10 million of reserve reversals in 1996, partially offset by lower environmental accruals in 1997.

The provision for income taxes on continuing operations decreased \$5.1 million, or 3 percent. The effective income tax rate in 1997 is less than the federal statutory rate due primarily to the effect of the non-taxable gain recognized in 1997 (see Note 2) and income tax credits from coal-seam gas production, partially offset by the effects of state income taxes. The effective tax rate in 1996 is less than the federal statutory rate due primarily to income tax credits from research activities and coal-seam gas production, partially offset by the effects of state income taxes. In addition, 1996 includes recognition of favorable adjustments totaling \$13 million related to previously provided deferred income taxes on certain regulated capital projects and state income tax adjustments.

The 1997 extraordinary loss results from the early extinguishment of debt (see Note 8).

1996 vs. 1995

Central's revenues increased \$4.1 million, or 2 percent, due primarily to increased transportation revenue resulting from new tariff rates that became effective August 1, 1995. Total throughput increased 6.9 TBiu, or 2 percent.

Operating profit was substantially the same as the prior year as the effect of a \$4 million 1995 reversal of a regulatory accrual was offset by new tariff rates that became effective August 1, 1995.

Kern River's remaining interest was acquired by Williams on January 16, 1996. Revenues and operating profit amounts for 1996 include the operating results of Kern River since the acquisition date. Kern River's revenues were \$160.6 million for 1996, while costs and operating expenses were \$35 million, selling, general and administrative expenses were \$13 million and operating profit was \$113 million. Prior to the acquisition. Williams accounted for its 50 percent ownership in Kern River using the equity method of accounting, with its share of equity earnings recorded in investing income. Throughput was 269.9 TBtu during 1996 (for the period subsequent to the acquisition date). Throughput for 1996 is comparable to 1995.

Northwest Pipeline's revenues increased \$14.5 million, or 6 percent, due primarily to increased transportation rates, effective February 1, 1996, associated with the expansion of mainline capacity placed into

service on December 1, 1995. In addition, \$9 million of revenue in 1996 associated with reserve reversals and favorable regulatory decisions was more than offset by the effect of the 1995 reversal of approximately \$16 million of accrued liabilities for estimated rate refund accruals. Total throughput increased 8 TBtu, or 1 percent.

Operating profit increased \$9.2 million, or 8 percent, due primarily to increased transportation rates associated with the expansion of mainline capacity, and the reserve reversals and favorable regulatory decisions. Partially offsetting were higher depreciation expense associated with the mainline expansion and the approximate \$11 million net favorable effect of two 1995 reserve accrual adjustments. The 1995 reserve accrual adjustments included a \$16 million favorable adjustment of rate refund accruals based on a favorable rate case order, partially offset by a loss accrual (included in other (income) expense — net) in connection with a lawsuit involving a former transportation customer.

Texas Gas Transmission's revenues and operating profit increased \$29.8 million, or 11 percent, and \$21.1 million, or 33 percent, respectively, due primarily to new rates that became effective April 1, 1995, and an adjustment to regulatory accruals based upon a recent rate case settlement. Also, 1995 reflected operations from January 18, when Williams acquired a majority interest in Transco Energy. Revenues associated with the period January 1 through January 17, 1995, were \$16 million. Total throughput increased 141.1 TBtu, or 22 percent, due primarily to a full year of Williams' ownership in 1996 compared to a partial year in 1995 and the impact of a colder winter in 1996.

Transco's revenues increased \$35.1 million, or 5 percent, due primarily to higher natural gas transportation revenues and liquids and liquefiable transportation revenues of \$20 million and \$9 million, respectively. Additionally, revenue for 1996 reflects a full year of Williams' ownership as compared with 1995, which reflected operations from January 18, 1995, when Williams acquired a majority interest in Transco Energy. Revenues associated with the period January 1 through January 17, 1995, were approximately \$36 million. Offsetting these increases were lower revenues resulting from lower transportation costs charged to Transco by others and passed through to customers as provided in Transco's rates. Transportation revenues increased due primarily to increased long-haul throughput, which benefitted from a two-phase system expansion placed in service in late 1996 and late 1995, and new rates effective September 1, 1995, which allowed the passthrough of increased costs. Total throughput increased 176.1 TBtu, or 12 percent, due primarily to a full year of Williams' ownership in 1996 compared to a partial year in 1995.

Operating profit increased \$29.6 million, or 18 percent, due primarily to increased transportation revenues, lower general and administrative expenses and a full year of Williams' ownership in 1996, partially offset by higher operation and maintenance expenses and higher taxes other than income taxes.

Energy Marketing & Trading's revenues increased \$107.6 million, or 70 percent, due primarily to higher natural gas and gas liquids marketing, price-risk management activities and petroleum product marketing of \$77 million, \$24 million and \$18 million, respectively, partially offset by lower contract origination revenues of \$10 million. Natural gas and gas liquids marketing revenues increased due to higher marketing volumes and prices. In addition, net physical trading revenues increased \$3 million, due to a 19 percent increase in natural gas physical trading volumes from 754 TBtu to 896 TBtu, largely offset by lower physical trading margins.

Costs and operating expenses increased \$73 million, or 94 percent, due primarily to higher natural gas purchase volumes and prices.

Operating profit increased \$33.2 million, or 100 percent, due primarily to higher price-risk management revenues, a reduction of development costs associated with its information products business and increased natural gas marketing volumes. Partially offsetting were higher selling, general and administrative expenses and lower contract origination revenues resulting from the impact of profits realized from certain long-term natural gas supply obligations in 1995.

Exploration & Production's revenues increased \$19.5 million, or 31 percent, due primarily to higher revenues from the marketing of production from the Royalty Trust and increased production revenues of \$9 million and \$8 million, respectively. The increase in marketing revenues reflects both increased volumes and higher average gas prices. The increase in production revenues reflects higher average gas prices.

Costs and operating expenses increased \$18 million due primarily to higher Royalty Trust natural gas purchase costs. Other (income) expense — net in 1995 includes an \$8 million loss accrual for a future minimum price natural gas commitment.

Operating profit increased \$8.7 million to \$2.8 million in 1996 due primarily to the effect of the \$8 million 1995 loss accrual.

Field Services' revenues increased \$83.4 million, or 16 percent, due primarily to higher natural gas liquids sales revenues of \$64 million combined with higher gathering and processing revenues of \$6 million and \$13 million, respectively. Natural gas liquids sales revenues increased due to a 36 percent increase in volumes combined with higher average prices. Gathering and processing volumes each increased 19 percent while average gathering rates decreased.

Costs and operating expenses increased \$52 million, or 15 percent, due primarily to higher fuel and replacement gas purchases, expanded facilities and increased operations. Other (income) expense — net for 1996 includes a \$20 million gain from the property insurance coverage associated with construction of replacement gathering facilities and \$6 million of gains from the sale of two small gathering systems, partially offset by \$5 million of environmental remediation accruals. Other (income) expense — net for 1995 includes \$20 million in operating profit from a favorable resolution of contingency issues involving previously regulated gathering and processing assets.

Operating profit increased \$26.4 million, or 16 percent, due primarily to higher natural gas liquids margins and higher gathering and processing revenues, partially offset by higher costs and operating expenses. Operating profit was favorably impacted in both 1996 and 1995 by approximately \$20 million of other income.

Petroleum Services' revenues increased \$165.2 million, or 50 percent, due primarily to an increase in transportation activities and ethanol sales of \$31 million and \$133 million, respectively. Revenues from transportation activities increased due primarily to a 10 percent increase in shipments and a \$14 million increase in product sales. Shipments increased as a result of new business and the 1995 impacts of unfavorable weather conditions and a fire at a truck-loading rack. Average length of haul and transportation rate per barrel were slightly below 1995 due primarily to shorter haul movements. Ethanol revenues increased following the August 1995 acquisition of Pekin Energy and the fourth-quarter 1995 completion of the Aurora plant.

Costs and operating expenses increased \$155 million, or 68 percent, due primarily to a full year of ethanol production activities.

Operating profit increased \$6.5 million, or 9 percent, due primarily to increased shipments, partially offset by lower ethanol margins and production levels as a result of record high corn prices.

Communications' revenues increased \$172.4 million, or 32 percent, due primarily to the 1996 acquisitions which contributed revenues of \$95 million. Additionally, increased business activity resulted in a \$36 million revenue increase in new systems sales and a \$16 million increase in digital fiber television services. The number of ports in service at December 31, 1996, increased 8 percent and billable minutes from occasional service increased 16 percent. Dedicated service voice-grade equivalent miles at December 31, 1996, decreased 6 percent as compared with December 31, 1995, which in part reflects a shift to occasional service.

Costs and operating expenses increased \$126 million, or 31 percent, and selling, general and administrative expenses increased \$63 million, or 62 percent, due primarily to the overall increase in business activity and higher expenses for developing additional products and services, including the cost of integrating the most recent acquisitions.

Operating profit decreased \$18.4 million, or 74 percent, due primarily to the expenses of developing additional products and services along with integrating the most recent acquisitions.

General corporate expenses increased \$3.7 million, or 10 percent, due primarily to higher employee compensation expense and consulting fees, partially offset by the effect of a \$5 million contribution in 1995 to The Williams Companies Foundation. Interest accrued increased \$82 million, or 30 percent, due primarily to higher borrowing levels including debt associated with the January 1996 acquisition of the remaining interest in Kern River (see Note 2), slightly offset by lower average interest rates. Interest capitalized decreased

\$7.6 million, or 53 percent, due primarily to lower capital expenditures for gathering and processing facilities and the 1995 completion of Northwest Pipeline's mainline expansion. Investing income decreased \$75.1 million, or 80 percent, due primarily to the effect of interest earned in 1995 on the invested portion of the cash proceeds from the sale of Williams' network services operations, a \$15 million dividend in 1995 from Texasgulf Inc. (sold in 1995), and \$31 million lower equity earnings from Williams' 50 percent ownership in Kern River. Kern River's 1996 operating results are included in operating profit since the acquisition date (see Note 2). The 1996 gain on sales of assets results from the sale of certain communication rights. The 1995 loss on sales of assets results from the sale of the 15 percent interest in Texasgulf Inc. The 1995 write-off of project costs results from the cancellation of an underground coal gasification project in Wyoming (see Note 6). Minority interest in income of consolidated subsidiaries in 1995 is associated with the Transco merger. The \$2 million favorable change in other income (expense) — net in 1996 is due primarily to approximately \$10 million of reserve reversals in 1996, partially offset by higher environmental accruals of \$4 million and additional expense of international activities.

The \$81.1 million, or 79 percent, increase in the provision for income taxes on continuing operations is primarily a result of higher pre-tax income and a higher effective income tax rate. The increase in the effective income tax rate is the result of the 1995 recognition of \$29.8 million of previously unrecognized tax benefits realized as a result of the sale of Texasguif Inc. (see Note 6). The effective income tax rate in 1996 is less than the federal statutory rate due primarily to income tax credits from research activities and coal-seam gas production, partially offset by the effects of state income taxes. In addition, 1996 includes recognition of favorable adjustments totaling \$13 million related to previously provided deferred income taxes on certain regulated capital projects and state income tax adjustments related to 1995. The effective income tax rate in 1995 is less than the federal statutory rate due primarily to income tax credits from coal-seam gas production, partially offset by the effects of state income taxes and minority interest. In addition, 1995 includes the previously unrecognized tax benefits related to the sale of Texasgulf Inc. (see Note 6) and recognition of an \$8 million income tax benefit resulting from settlements with taxing authorities (see Note 7).

On January 5, 1995, Williams sold its network services operations to LDDS Communications, Inc. for \$2.5 billion in cash. The sale yielded an after-tax gain of approximately \$1 billion, which is reported as income from discontinued operations (see Note 3).

Preferred stock dividends decreased \$4.9 million, or 32 percent, due primarily to the 1995 effect of a difference in the fair value of subordinated debentures issued and the carrying value of the exchanged \$2.21 cumulative preferred stock (see Note 15).

Financial Condition and Liquidity

Debt Restructuring

In September 1997, Williams initiated a restructuring of a portion of its debt portfolio (see Note 14). As of December 31, 1997, Williams has paid approximately \$1.4 billion to redeem approximately \$1.3 billion of debt with stated interest rates in excess of 8.8 percent, resulting in an extraordinary loss of \$79.1 million (see Note 8). The restructuring is expected to reduce interest expense by approximately \$25 million annually. The restructuring was temporarily financed with a combination of borrowings under the \$1 billion bank-credit facility, commercial paper and new short-term bank agreements with commitments totaling \$1.2 billion. Registration statements were filed with the Securities and Exchange Commission in September 1997 by Williams, Williams Holdings of Delaware, Northwest Pipeline and Transcontinental Gas Pipe Line (each a wholly-owned subsidiary of Williams). These additional filings brought the total shelf financing availability to \$900 million, \$820 million, \$400 million and \$500 million, respectively, prior to the restructuring. During the fourth quarter of 1997 and January 1998, \$1.1 billion of debentures and notes with interest rates ranging from 5.91 percent to 6.625 percent were issued under these registration statements in connection with the restructuring. The restructuring is expected to be completed during the first quarter of 1998 with the issuance of additional long-term debt securities.

Liquidity

Williams considers its liquidity to come from two sources: internal liquidity, consisting of available cash investments, and external liquidity, consisting of borrowing capacity from available bank-credit facilities and Williams Holdings' commercial paper program, which can be utilized without limitation under existing loan covenants. At December 31, 1997, Williams had access to \$155 million of liquidity including \$132 million available under its \$1 billion bank-credit facility. This compares with liquidity of \$550 million at December 31, 1996, and \$656 million at December 31, 1995. The decrease in 1997 is due primarily to additional borrowings under the bank-credit facility to finance increased capital expenditures and to provide interim financing related to the debt restructuring program.

During 1997, Williams Holdings entered into a commercial paper program backed by \$650 million of new short-term bank-credit facilities. At December 31, 1997, \$645 million of commercial paper was outstanding under the program. After completion of the debt restructuring, Williams expects approximately \$1 billion of shelf availability to remain under outstanding registration statements. These registration statements may be used to issue a variety of debt or equity securities. In addition, short-term uncommitted bank lines are utilized in managing liquidity. Williams believes any additional financing arrangements can be obtained on reasonable terms if required.

Williams had a net working-capital deficit of \$772 million at December 31, 1997, compared with \$309 million at December 31, 1996. Williams manages its borrowings to keep cash and cash equivalents at a minimum and has relied on bank-credit facilities to provide flexibility for its cash needs. As a result, it historically has reported negative working capital. The increase in the working-capital deficit at December 31, 1997, as compared to prior year-end is primarily a result of short-term borrowings under the commercial paper program.

Terms of certain borrowing agreements limit transfer of funds to Williams from its subsidiaries. The restrictions have not impeded, nor are they expected to impede. Williams' ability to meet its cash requirements in the future.

During 1998, Williams expects to finance capital expenditures, investments and working-capital requirements through cash generated from operations and the use of the available portion of its \$1 billion bank-credit facility, commercial paper, short-term uncommitted bank lines and debt or equity public offerings.

Operating Activities

Cash provided by operating activities was: 1997 — \$920 million; 1996 — \$710 million; and 1995 — \$829 million. Receivables, inventories and accounts payable increased due primarily to the combination of customer equipment sales and services operations with Nortel (see Note 2) and increased trading activities by Energy Marketing & Trading.

Financing Activities

Net cash provided (used) by financing activities was: 1997 — \$317 million; 1996 — \$734 million; and 1995 — (\$1.4) billion. Long-term debt principal payments, net of debt proceeds, were \$161 million during 1997, and notes payable proceeds, net of notes payable payments, were \$615 million during 1997. The increase in notes payable at December 31, 1997, reflects borrowings under the new commercial paper program to fund capital expenditures, investments and acquisition of businesses. Long-term debt proceeds, net of principal payments, were \$609 million during 1996. The increase in net new borrowings during 1996 was primarily to fund capital expenditures, investments and acquisitions of businesses. Long-term debt principal payments, net of debt proceeds, were \$610 million during 1995. The net payments in 1995 were primarily a result of payments Williams made to retire and/or terminate approximately \$700 million of Transco Energy's borrowings, preferred stock, interest-rate swaps and sale of receivable facilities in connection with the acquisition of Transco Energy.

The proceeds from issuance of common stock in 1997, 1996 and 1995 include Williams' benefit plan stock purchases and exercise of stock options under Williams' stock plan. The 1995 proceeds from issuance of common stock also includes \$46.2 million from the sale of 3.6 million shares of Williams common stock.

The 1996 purchases of Williams' treasury stock include 1.9 million shares of common stock on the open market for \$31 million. The Williams' board of directors authorized up to \$800 million of such purchases. No additional shares were purchased during 1997, and Williams' board of directors terminated the repurchase program during the fourth quarter of 1997.

Long-term debt at December 31, 1997, was \$4.6 billion, compared with \$4.4 billion at December 31, 1996, and \$2.9 billion at December 31, 1995. At December 31, 1997 and 1996, \$560 million and \$200 million, respectively, in current debt obligations have been classified as non-current obligations based on Williams' intent and ability to refinance on a long-term basis. The 1996 increase in long-term debt is due primarily to the \$643 million outstanding debt assumed with the acquisition of Kern River (see Note 2), \$300 million in additional borrowings under the \$1 billion bank-credit facility and \$250 million of debt issued by Williams Holdings. The long-term debt to debt-plus-equity ratio was 56.1 percent for 1997 and 1996 compared to 47.4 percent at December 31, 1995. If short-term notes payable and long-term debt due within one year are included in the calculations, these ratios would be 59.7 percent, 57.9 percent and 50.1 percent, respectively.

Investing Activities

Net cash provided (used) by investing activities was: 1997 — (\$1.3) billion; 1996 — (\$1.4) billion; and 1995 — \$585 million. Capital expenditures of gas pipeline subsidiaries, primarily to expand and modernize systems, were \$419 million in 1997, \$441 million in 1996, and \$445 million in 1995. Expenditures in 1997 and 1996 include Transcontinental Gas Pipe Line and Northwest Pipeline's expansions. Capital expenditures of Energy Services, primarily to expand and modernize gathering and processing facilities, were \$305 million in 1997, \$292 million in 1996, and \$336 million in 1995. Capital expenditures of Communications were \$276 million in 1997, \$67 million in 1996, and \$332 million 1995. The 1997 expenditures include the fiber-optic network. Budgeted capital expenditures and investments for 1998 are estimated to be approximately \$2.5 billion, primarily to expand and modernize pipeline systems, gathering and processing facilities and the fiber-optic network. If the pending MAPCO acquisition is completed, budgeted capital expenditures will increase an estimated \$400 million.

On April 30, 1997, Williams and Northern Telecom (Nortel) combined their customer-premise equipment sales and services operations into a limited liability company, Williams Communications Solutions, LLC (LLC). In addition, Williams paid \$68 million to Nortel. Williams has accounted for its 70 percent interest in the operations that Nortel contributed to the LLC as a purchase business combination. Williams recorded the 30 percent reduction in its operations contributed to the LLC as a sale to the minority shareholders of the LLC (see Note 2). During 1997, Williams also purchased a 20 percent interest in a foreign telecommunications business for \$65 million in cash. During 1996, Williams acquired the remaining interest in Kern River for \$206 million cash (see Note 2). In addition, during 1996 Williams acquired various communications technology businesses totaling \$165 million in cash. In 1995, Williams acquired all of Transco Energy's outstanding common stock for cash of \$430.5 million and 31.2 million shares of Williams common stock valued at \$334 million (see Note 2). During 1995, Williams also acquired the Gas Company of New Mexico's natural gas gathering and processing assets in the San Juan and Permian basins for \$154 million and Pekin Energy Co., the nation's second largest ethanol producer, for \$167 million in cash.

During 1995, Williams received proceeds of \$2.5 billion in cash from the sale of its network services operations (see Note 3) and proceeds of \$124 million from the sale of its 15 percent interest in Texasgulf Inc. (see Note 6).

New Accounting Standards

See Note 1 for the effects of Statement of Financial Accounting Standards (SFAS) No. 130, "Reporting Comprehensive Income," and SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information."

MAPCO Acquisition

On November 24, 1997, Williams and MAPCO Inc. announced that they had entered into a definitive merger agreement whereby Williams would acquire MAPCO by exchanging 1.665 share of Williams common stock for each outstanding share of MAPCO common stock. In addition, outstanding MAPCO employee stock options would be converted into Williams common stock. Based on the closing market price of Williams common stock on December 31, 1997, approximately 96.8 million shares of Williams common stock valued at approximately \$2.8 billion would be issued in the transaction (see Note 19). The transaction closed on March 28, 1998.

Effects of inflation

Williams has experienced increased costs in recent years due to the effects of inflation. However, approximately 66 percent of Williams' property, plant and equipment has been acquired or constructed since 1995, a period of relatively low inflation. A substantial portion of Williams' property, plant and equipment is subject to regulation, which limits recovery to historical cost. While Williams believes it will be allowed the opportunity to earn a return based on the actual cost incurred to replace existing assets, competition or other market factors may limit the ability to recover such increased costs.

Environmental

Williams is a participant in certain environmental activities in various stages involving assessment studies, cleanup operations and/or remedial processes. The sites, some of which are not currently owned by Williams (see Note 18), are being monitored by Williams, other potentially responsible parties, the U.S. Environmental Protection Agency (EPA), or other governmental authorities in a coordinated effort. In addition, Williams maintains an active monitoring program for its continued remediation and cleanup of certain sites connected with its refined products pipeline activities. Williams has both joint and several liability in some of these activities and sole responsibility in others. Current estimates of the most likely costs of such cleanup activities, after payments by other parties, are approximately \$73 million, all of which is accrued at December 31, 1997. Williams expects to seek recovery of approximately \$41 million of the accrued costs through future natural gas transmission rates. Williams will fund these costs from operations and/or available bank-credit facilities. The actual costs incurred will depend on the final amount, type and extent of contamination discovered at these sites, the final cleanup standards mandated by the EPA or other governmental authorities, and other factors.

Year 2000 Compliance

Williams has initiated an enterprise-wide project to address the year 2000 compliance issue for all technology hardware and software, external interfaces with customers and suppliers, operations process control, automation and instrumentation systems, and facility items. The assessment phase of this project as it relates to traditional information technology areas should be substantially complete by the end of the first quarter of 1998. Completion of the assessment phase for non-traditional information technology areas is expected in mid-1998. Necessary conversion and replacement activities will begin in 1998 and continue through mid-1999. Testing of systems has begun and will continue throughout the process. Williams has initiated a formal communications process with other companies with which Williams' systems interface or rely on to determine the extent to which those companies are addressing their year 2000 compliance, and where necessary, Williams will be working with those companies to mitigate any material adverse effect on Williams.

Williams expects to utilize both internal and external resources to complete this process. Existing resources will be redeployed and previously planned system replacements will be accelerated during this time. For example, implementation of previously planned financial and human resources systems is currently in process. These systems will address the year 2000 compliance issues in certain areas. Costs incurred for new software and hardware purchases will be capitalized and other costs will be expensed as incurred. For the regulated pipelines, Williams considers costs associated with the year 2000 compliance to be prudent costs

incurred in the ordinary course of business, and, therefore, recoverable through rates. While the total cost of this project is still being evaluated, Williams estimates that external costs, excluding previously planned system replacements, necessary to complete the project within the schedule described will total at least \$15 million. Williams will update this estimate as additional information becomes available. The costs of the project and the completion dates are based on management's best estimates, which were derived utilizing numerous assumptions of future events, including the continued availability of certain resources, third party year 2000 compliance modification plans and other factors. There can be no guarantee that these estimates will be achieved and actual results could differ materially from these estimates.

Market Risk Disclosures

Interest Rate Risk

Williams' interest rate risk exposure results from short-term rates, primarily LIBOR based borrowings from commercial banks and the issuance of commercial paper, and long-term U.S. Treasury rates. To mitigate the impact of fluctuations in interest rates, Williams targets to maintain a significant portion of its debt portfolio in fixed rate debt. At December 31, 1997, the amount of Williams' fixed and variable rate debt was approximately the same as a result of a debt restructuring program begun in 1997 where Williams extinguished higher cost long-term debt. During early 1998, the percent of fixed rate debt will increase to targeted levels as Williams completes issuing long-term debt under the restructuring program and repays its interim financings. The maturity of Williams' long-term debt portfolio is influenced by the life of its operating assets. Williams also utilizes interest rate swaps to change the ratio of its fixed and variable rate debt portfolio based on management's assessment of future interest rates, volatility of the yield curve and Williams' ability to access the capital markets in a timely manner. Williams has entered into interest rate forward contracts to establish an effective borrowing rate for anticipated long-term debt issuances.

The following table provides information about Williams' notes payable, long-term debt, interest rate swaps and interest rate forward contracts that are subject to interest rate risk. For notes payable and long-term debt, the table presents principal cash flows and weighted average interest rates by expected maturity dates. For interest rate swaps and interest rate forward contracts, the table presents notional amounts and weighted average interest rates by contractual maturity dates. Notional amounts are used to calculate the contractual cash flows to be exchanged under the interest rate swaps and the settlement amounts under the interest rate forward contracts.

	1	998	1999	2000	2001 (D	-	002 rs in m	-	reafter	Total	Fair Value December 31, 1997
Notes payable	5	693	s —	s -	5 -	5	_	5	_	\$ 693	\$ 693
Interest rate		6.6%									
Long-term debt, including current portion:											
Fixed rate	5	40	\$219	\$251	\$776	5	441	5	,373	\$3,100	\$3,188
Interest rate		7.4%	7.4%	7.4%	7.4%		7.4%		7.4%		
Variable rate	5		\$130	5 -	\$276	51	.071	5	28	\$1,505	\$1,505
Interest rate(1)											
Interest rate swaps:											
Pay variable/receive fixed	5	36	\$ 42	\$ 47	\$461	5	-	5	450	\$1,036	5 9
Pay rate(2)									O-FRIENDS	30.0400.000	
Receive rate		6.3%	6.3%	6.4%	6.4%		6.8%		6.5%		
Pay fixed/receive variable(3)	5	36	\$172	\$ 47	\$ 53	5	59	\$	349	\$ 716	\$ (56)
Pay rate	N.	7.8%	7.8%	7.8%	8.0%	-	8.0%		8.0%		
Receive rate(4)				11.00.00	12.7						
Interest rate forward contracts purchased related to anticipated long-term debt											
issuances	\$1	,150	5 -	5 -	5 -	5	_	5	_	\$1,150	\$ (8)

Average locked in rate of 5.9 percent referenced to underlying Treasury securities having a weighted-average maturity of 6 years.

- (1) LIBOR plus .33 percent.
- (2) LIBOR, except \$250 million notional amount maturing after 2002 is at LIBOR less 1.04 percent.
- (3) Counterparties have an option to cancel all outstanding swaps in 2001.
- (4) LIBOR.

Commodity Price Risk

Energy Marketing & Trading has trading operations that provide price risk management services to thirdparty customers. The trading operations have commodity price risk exposure associated with the crude oil,
natural gas, refined products, natural gas liquids and electricity energy markets in the United States and the
natural gas markets in Canada. The trading operations enter into energy-related financial instruments
(forward contracts, futures contracts, option contracts and swap agreements) and have commodity inventories
and purchase and sale commitments which involve the physical delivery of an energy commodity. These
financial instruments and physical positions and commitments are valued at market value and unrealized gains
and losses from changes in market value are recognized in income. The trading operations are subject to risk
from changes in energy commodity market prices, the portfolio position of its financial instruments and
physical commitments, the liquidity of the market in which the contract is transacted, changes in interest rates
and credit risk. Energy Marketing & Trading manages risk by maintaining its portfolio within established
trading policy guidelines. A Risk Control Group, independent of the trading operations, monitors compliance
with established trading policy guidelines and measures the risk associated with the trading portfolio.

Energy Marketing & Trading uses a value at risk methodology to estimate the potential one day loss from adverse changes in the market value of its trading operations. At December 31, 1997, the value at risk for the trading operations is \$4 million. This reflects a 97.5 percent probability that as a result of changes in

commodity prices, the one day loss in the market value of the trading portfolio will not exceed the value at risk. The value at risk includes all the financial instruments and physical positions and commitments that expose the trading operations to market risk. The value-at-risk model estimates assume normal market conditions based upon historical market prices. Value at risk does not purport to represent actual losses in market value that could be incurred from the trading portfolio, nor does it consider that changing our trading portfolio in response to market conditions could affect market prices and could take longer to execute than the one-day holding period assumed in our value at risk model.

Foreign Currency Risk

Williams has investments in companies whose operations are located in foreign countries, of which \$87 million are accounted for using the cost method. Fair value for the cost method investments is deemed to approximate their carrying amount, because estimating cash flows by year is not practicable given that the time frame for selling these investments is uncertain. Williams' financial results could be affected if the investments incur a permanent decline in value as a result of changes in foreign currency exchange rates and the economic conditions in foreign countries. Williams attempts to mitigate these risks by investing in different countries and business segments. Approximately 80 percent of the cost method investments are in Asian countries and 20 percent in South American countries. Of the Asian investments, approximately 50 percent are in countries whose currencies have recently suffered significant devaluations and volatility. The ultimate duration and severity of the conditions in Asia remains uncertain as does the long-term impact on Williams' investments.

Item 8. Financial Statements and Supplementary Data

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REPORT OF INDEPENDENT AUDITORS

To the Stockholders of The Williams Companies, Inc.

We have audited the accompanying consolidated balance sheet of The Williams Companies. Inc. as of December 31, 1997 and 1996, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 1997. Our audits also included the financial statement schedule listed in the Index at Item 14(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Williams Companies, Inc. at December 31, 1997 and 1996, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 1997, in conformity with generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

ERNST & YOUNG LLP

Tulsa, Oklahoma February 13, 1998

THE WILLIAMS COMPANIES, INC.

CONSOLIDATED STATEMENT OF INCOME

	Years	Ended Decemb	er 31,
	1997	1996	1995
Revenues:	(Millions,	except per-shar	e amounts)
Gas Pipelines (Note 4)	\$1,683.9	\$1,675.2	\$1,431.1
Energy Services (Note 4)	1,504.9	1,453.1	1,077.4
Communications (Note 2)	1,445.3	711.3	538.9
Other	38.4	48.0	17.4
Intercompany eliminations (Note 17)	(262.9)	(356.4)	(209.1
Total revenues	4,409.6	3,531.2	2,855.7
Profit-center costs and expenses:			
Costs and operating expenses	2,664.5	2.064.1	1,700.7
Selling, general and administrative expenses	780.1	585.5	488.8
Other (income) expense—net (Note 6)	38.6	(19.8)	(4.5
Total profit-center costs and expenses	3,483.2	2,629.8	2,185.0
Operating profit:		-	
Gas Pipelines (Note 4)	614.2	562.4	389.7
Energy Services (Note 4)	360.9	332.3	257.5
Communications (Notes 2 and 6)	(55.7)	6.6	25.0
Other	7.0	.1	(1.5
Total operating profit	926.4	901.4	670.7
General corporate expenses	(50.9)	(41.4)	(37.7)
Interest accrued	(404.5)	(359.9)	(277.9)
Interest capitalized	15.9	6.9	14.5
Investing income (Note 5)	19.2	18.8	93.9
Gain on sale of interest in subsidiary (Note 2)	44.5		-
Gain (loss) on sales of assets (Note 6)		15.7	(12.6)
Write-off of project costs (Note 6)	-	-	(41.4
Minority interest in income of consolidated subsidiaries (Note 2)	(14.0)		(10.0)
Other income (expense)—net	(8.1)	3.9	1.9
Income from continuing operations before income taxes	528.5	545.4	401.4
Provision for income taxes (Note 7)	178.0	183.1	102.0
Income from continuing operations	350.5	362.3	299.4
Income from discontinued operations (Note 3)	_		1,018.8
Income before extraordinary loss	350.5	362.3	1,318.2
Extraordinary loss (Note 8)	(79.1)	_	
Net income	271.4	362.3	1,318.2
Preferred stock dividends (Note 15)	9.8	10.4	15.3
Income applicable to common stock	\$ 261.6	\$ 351.9	\$1,302.9
Basic earnings per common share (Notes 1 and 9):	Security Change	STREET COMMON	STATE OF STATE
Income from continuing operations	\$ 1.06	\$ 1.10	\$.94
Income from discontinued operations (Note 3)		- 1.10	3.36
그는 사람이 가장이 하는데 하는데 하는데 하는데 하는데 나를 하는데	1.06	1.10	-
Income before extraordinary loss Extraordinary loss (Note 8)	(.25)	1.10	4.30
Net income	\$.81	\$ 1.10	\$ 4.30
Diluted earnings per common share (Notes 1 and 9):	2 .571	4 1.10	4.50
Income from continuing operations	\$ 1.04	\$ 1.07	\$.92
Income from discontinued operations (Note 3)	3 1.04	3 1.07	3.25
Income before extraordinary loss	1.04	1.07	the second second second
Extraordinary loss (Note 8)	(.24)	1.07	4.17
Net income	\$.80	\$ 1.07	6 417
iver medine	3 .80	5 1.07	\$ 4.17

THE WILLIAMS COMPANIES, INC. CONSOLIDATED BALANCE SHEET

ASSETS

	Decem	ber 31,
	1997	1996
	(Dollars in m	
Current assets:	1900007000	
Cash and cash equivalents	\$ 81.3	\$ 115.3
Receivables less allowance of \$19.3 (\$9.7 in 1996)	1,200.5	952.9
Transportation and exchange gas receivable	130.4	117.7
Inventories (Note 11)	300.5	204.6
Commodity trading assets	180.3	147.2
Deferred income taxes (Note 7)	224.6	199.5
Other	138.3	152.9
Total current assets	2,255.9	1,890.1
Investments (Note 5)	291.4	190.6
Property, plant and equipment—net (Note 12)	10,055.6	9,386.3
Goodwill and other intangible assets—net (Notes 1 and 2)	435.2	198.1
Other assets and deferred charges	840.9	753.7
Total assets	\$13,879.0	\$12,418.8
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable (Note 14)	\$ 693.0	\$ 269.5
Accounts payable (Note 13)	886.3	683.3
Transportation and exchange gas payable	67.7	73.7
Transportation and exchange gas payable	1.157.3	975.3
Accrued liabilities (Note 13)	182.0	137.9
Long-term debt due within one year (Note 14)	41.1	59.6
Total current liabilities	3,027.4	2.199.3
Total current habilities	3,027.4	2,177.3
Long-term debt (Note 14)	4,565.3	4,376.9
Deferred income taxes (Note 7)	1,718.9	1,626.6
Other liabilities	878.6	787.5
Minority interest in consolidated subsidiaries (Note 2)	117.1	7.5
Stockholders' equity (Note 15): Preferred stock, \$1 par value, 30,000,000 shares authorized, 2,497,472 shares		
issued in 1997 and 3,241,552 shares issued in 1996	142.2	161.0
Common stock, \$1 par value, 480,000,000 shares authorized, 325,065,668 shares issued in 1997 and 320,428,326 shares issued in 1996	325.1	320.4
Capital in excess of par value	957.6	887.5
Retained earnings	2,209.4	2,119.5
Other	(4.5)	(2.2
	3,629.8	3,486.2
Less treasury stock (at cost), 4,879,127 shares of common stock in 1997 and		Pog 860000
5,474,674 shares of common stock in 1996	(58.1)	(65.2
Total stockholders' equity	3,571.7	3,421.0
Total liabilities and stockholders' equity	\$13,879.0	\$12,418.8

THE WILLIAMS COMPANIES, INC. CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

	Preferred Stock	Common Stock	Capital in Excess Par Value	Retained Earnings	Other	Treasury Stock	Total		
		(Dollar	s in millions	except per-	except per-share amounts)				
Balance, December 31, 1994	\$100.0	\$313.2	\$782.2	\$ 716.5	\$(1.3)	\$(405.1)	\$1,505.5		
Net income — 1995	_	-	-	1.318.2	-	-	1.318.2		
Cash dividends				10775837771			Mark The Control of t		
Common stock (\$.36 per share)				(107.2)	-	-0.00	(107.2)		
Preferred stock (Note 15)	-	-	1000	(11.9)	-	-	(11.9)		
Issuance of shares —									
38,639,762 common	-	2.8	56.9	-	(1.7)	352.7	410.7		
2,500,000 preferred	142.5	-	_		-	_	142.5		
Exchange of shares for debentures —									
2,760,548 preferred (Note 15)	(69.0)	_	(3.5)	per	_	-	(72.5)		
Purchase of treasury stock —									
142,800 preferred	-		-	, and	-	(3.7)	(3.7)		
Tax benefit of stock-based awards	-	-	4.8	-	-	-	4.8		
Amortization of deferred compensation	-	_		-	7				
Balance, December 31, 1995	173.5	316.0	840.4	1,915.6	(2.3)	(56.1)	3,187.1		
Net income — 1996	-	_	30000	362.3	-	And Therefore	362.3		
Cash dividends —				20212			502.5		
Common stock (\$.47 per share)			_	(148.0)			(148.0)		
Preferred stock (Note 15)	-	100-		(10.4)	-	-	(10.4)		
Issuance of shares - 5,574,916 common	-	4.4	31.4	100000	(.6)	12.0	47.2		
Purchase of treasury stock —							200		
1,915,500 common	2000	940	-	-	-	(31.3)	(31.3)		
96,300 preferred		-	- market	Total Control		(2.6)	(2.6)		
Retirement of treasury stock -									
497,900 preferred	(12.5)	200	(.3)	100	-	12.8			
Tax benefit of stock-based awards	_	-	16.0	-	-	-	16.0		
Amortization of deferred compensation	-		-		.7	_	.7		
Balance, December 31, 1996	\$161.0	\$320.4	\$887.5	\$2,119.5	\$(2.2)	\$ (65.2)	\$3,421.0		
Net income — 1997		T area		271.4			271.4		
Cash dividends —				-					
Common stock (\$.54 per share)	-	944	1004	(171.7)			(171.7)		
Preferred stock (Note 15)	1000			(9.8)	_	-	(9.8)		
Issuance of shares - 5,221,039 common	-	4.7	48.7	630764	(.7)	7.1	59.8		
Conversion of preferred stock - 2,528 shares	(.3)	-	.3	-	-				
Redemption of preferred stock - 741,552 shares	7,000								
(Note 15)	(18.5)	-	-	-	-	-	(18.5)		
Tax benefit of stock-based awards	-		21.1	-	-	-	21.1		
Amortization of deferred compensation	-		-	-	.8		.8		
Unrealized loss on marketable equity									
							4.7		
securities		-	-	-	(2.4)	-	(2.4)		

Note: Certain amounts have been restated to reflect the December 29, 1997, two-for-one stock split and distribution.

THE WILLIAMS COMPANIES, INC. CONSOLIDATED STATEMENT OF CASH FLOWS

Operating Activities: Net income	1997 \$ 271.4	(Millions)	1995
	\$ 271.4	(Millions)	
	\$ 271.4		
Net income	3 2/1.4	\$ 362.3	\$ 1,318.2
Adjustments to reconcile to cash provided from operations:			47.5355
Discontinued operations	-	-	(8.810,1)
Extraordinary loss	79.1	-	_
Premium on early extinguishment of debt	(171.2)		
Depreciation, depletion and amortization	499.5	421.0	375.5
Provision for deferred income taxes	81.8	72.4	125.4
Provision for loss on property and other assets	49.8	_	41.4
(Gain) loss on dispositions of property and interest in subsidiary	(56.8)	(46.4)	10.5
Minority interest in income of consolidated subsidiaries	14.0	_	10.0
Changes in receivables sold	188.6	(13.1)	55.9
Changes in receivables	(180.6)	(214.2)	33.2
Changes in inventories	(73.7)	(16.1)	11.9
Changes in other current assets	25.5	3.8	1.1
Changes in accounts payable	195.8	204.0	(6.5)
Changes in accrued liabilities	(7.9)	(24.9)	(33.4)
Changes in current commodity trading assets and liabilities	11.0	(29.7)	28.1
Changes in non-current commodity trading assets and liabilities	(47.7)	(37.7)	(82.1)
Other, including changes in non-current assets and liabilities	41.0	29.0	(41.7)
	The second second second second	and the second second	- Appendix
Net cash provided by operating activities	919.6	710.4	828.7
Financing Activities: Proceeds from notes payable		266.0	1160
Proceeds from notes payable	1,860.4	356.8	116.8
Payments of notes payable	(1,245.9)	(87.3)	100000000000000000000000000000000000000
Proceeds from long-term debt	2,007.7	1,996.7	399.0
Payments of long-term debt	(2,169.0)	(1,387.7)	(1,009.4)
Proceeds from issuance of common stock	62.9	54.3	78.1
Purchases of treasury stock		(33.9)	(3.7)
Dividends paid	(181.5)	(158.4)	(119.1)
Subsidiary preferred stock redemptions	-	_	(193.7)
Other — net	(17.7)	(6.3)	(3.5)
Net cash provided (used) by financing activities	316.9	734.2	(1.359.3)
Investing Activities:			
Property, plant and equipment:	*****	(010.0)	(022.6)
Capital expenditures	(1,162.1)	(818.9)	(827.5)
Proceeds from dispositions	100.3	60.2	28.2
Acquisition of businesses, net of cash acquired	(87.0)	(366.2)	
Proceeds from sales of businesses	_	7.77	2,588.3
Income tax and other payments related to discontinued operations	(9.7)	(261.7)	・ ・ ・ ・ ・ ・ ・ ・ ・ ・ ・ ・ ・ ・ ・ ・ ・ ・ ・
Proceeds from sales of assets	5.2	23.0	125.1
Purchase of investments/advances to affiliates	(134.2)	(76.9)	(49.7)
Purchase of note receivable		-	(75.1)
Other — net	17.0	20.8	4.9
Net cash provided (used) by investing activities	(1,270.5)	(1,419.7)	584.9
Increase (decrease) in cash and cash equivalents	(34.0)	24.9	54.3
Cash and cash equivalents at beginning of year	115.3	90.4	36.1
Cash and cash equivalents at end of year	\$ 81.3	\$ 115.3	\$ 90.4

THE WILLIAMS COMPANIES, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Summary of significant accounting policies

Nature of Operations

Operations of The Williams Companies, Inc. (Williams) are located principally in the United States and are organized into three operating groups as follows: (1) Gas Pipelines, which is comprised of five interstate natural gas pipelines located in the eastern, midsouth, Gulf Coast, midwest and northwest regions; (2) Energy Services, which is comprised of natural gas gathering and processing facilities in the Rocky Mountain, midwest and Gulf Coast regions, energy trading and price-risk management activities throughout the United States, a petroleum products pipeline and ethanol production/marketing operations in the midwest region, and hydrocarbon exploration and production activities in the Rocky Mountain and Gulf Coast regions; and (3) Communications, which includes network integration and management services; video and other multimedia transmission services for the broadcast industry; business audio and video conferencing services; and installation and maintenance of customer-premise voice and data equipment. Additional information about these businesses is contained throughout the following notes.

Basis of Presentation

Revenues and operating profit amounts previously reported as Williams Natural Gas and Merchant Services are now reported as Central and Energy Marketing & Trading, respectively.

On April 30, 1997, Williams and Northern Telecom (Nortel) combined their customer-premise equipment sales and service operations into a limited liability company, Williams Communications Solutions, LLC (LLC), formerly WilTel Communications, LLC (see Note 2). Communications' revenues and operating profit amounts for 1997 include the operating results of the LLC beginning May 1, 1997.

Revenues and operating profit amounts include the operating results of Kern River Gas Transmission Company (Kern River) since the January 16, 1996, acquisition by Williams of the remaining interest (see Note 2). Prior to this acquisition, Williams accounted for its 50 percent ownership in Kern River using the equity method of accounting, with its share of equity earnings recorded in investing income.

Revenues and operating profit amounts include the operating results of Transco Energy Company (Transco Energy) since its January 18, 1995, acquisition by Williams (see Note 2). The transportation operations from Transco Energy's two interstate natural gas pipelines are reported separately within the Gas Pipelines group. Transco Energy's gas gathering operations are included in Field Services, and its gas marketing operations are included in Energy Marketing & Trading.

Principles of Consolidation

The consolidated financial statements include the accounts of Williams and its majority-owned subsidiaries. Companies in which Williams and its subsidiaries own 20 percent to 50 percent of the voting common stock, or otherwise exercise sufficient influence over operating and financial policies of the company, are accounted for under the equity method.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles 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.

Cash and Cash Equivalents

Cash and cash equivalents include demand and time deposits, certificates of deposit and other marketable securities with maturities of three months or less when acquired.

THE WILLIAMS COMPANIES, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Transportation and Exchange Gas Imbalances

In the course of providing transportation services to customers, the natural gas pipelines may receive different quantities of gas from shippers than the quantities delivered on behalf of those shippers. Additionally, the pipelines and other Williams subsidiaries transport gas on various pipeline systems which may deliver different quantities of gas on their behalf than the quantities of gas received. These transactions result in gas transportation and exchange imbalance receivables and payables which are recovered or repaid in cash or through the receipt or delivery of gas in the future. Settlement of imbalances requires agreement between the pipelines and shippers as to allocations of volumes to specific transportation contracts and timing of delivery of gas based on operational conditions.

Inventory Valuation

Inventories are stated at cost, which is not in excess of market, except for those held by Energy Marketing & Trading, which are primarily stated at market. The cost of inventories is primarily determined using the average-cost method, except for certain inventories held by Transcontinental Gas Pipe Line, which are determined using the last-in, first-out (LIFO) method.

Property. Plant and Equipment

Property, plant and equipment is recorded at cost. Depreciation is provided primarily on the straight-line method over estimated useful lives. Gains or losses from the ordinary sale or retirement of property, plant and equipment for regulated pipeline subsidiaries are credited or charged to accumulated depreciation; other gains or losses are recorded in net income.

Goodwill and Other Intangible Assets

Goodwill, which represents the excess of cost over fair value of assets of businesses acquired, is amortized on a straight-line basis over periods not exceeding 25 years. Other intangible assets are amortized on a straight-line basis over periods not exceeding 11 years. Accumulated amortization at December 31, 1997 and 1996 was \$56 million and \$31.8 million, respectively. Amortization of intangible assets was \$24.2 million, \$9.6 million and \$6.2 million in 1997, 1996 and 1995, respectively.

Treasury Stock

Treasury stock purchases are accounted for under the cost method whereby the entire cost of the acquired stock is recorded as treasury stock. Gains and losses on the subsequent reissuance of shares are credited or charged to capital in excess of par value using the average-cost method.

Revenue Recognition

Revenues generally are recorded when services have been performed or products have been delivered. Petroleum Services bills customers when products are shipped and defers the estimated revenues for shipments in transit. The Gas Pipelines recognize revenues based upon contractual terms and the related transportation volumes through month-end. These pipelines are subject to Federal Energy Regulatory Commission (FERC) regulations and, accordingly, certain revenues are subject to possible refunds pending final FERC orders. Williams records rate refund accruals based on management's estimate of the expected outcome of these proceedings. Communications' customer-premise equipment sales and service business primarily uses the percentage of completion method of recognizing revenues for services provided.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Commodity Price-Risk Management Activities

Energy Marketing & Trading has trading operations that enter into energy-related derivative financial instruments and derivative commodity instruments (forward contracts, futures contracts, option contracts and swap agreements) to provide price-risk management services to its third-party customers. This trading operation also has commodity inventories and enters into short- and long-term energy-related purchase and sale commitments which involve physical delivery of an energy commodity. These financial instruments, physical inventories and commitments are valued at market and are recorded in commodity trading assets, other assets and deferred charges, commodity trading liabilities and other liabilities in the Consolidated Balance Sheet. The change in unrealized market gains and losses is recognized in income currently and is recorded as revenues in the Consolidated Statement of Income. Such market values are subject to change in the near term and reflect management's best estimate of market prices considering various factors including closing exchange and over-the-counter quotations, liquidity of the market in which the contract is transacted, the terms of the contract, credit considerations, time value and volatility factors underlying the positions. Energy Marketing & Trading reports its trading operations' physical sales transactions net of the related purchase costs, consistent with market value accounting for such trading activities.

Certain Energy Marketing & Trading's revenues were not considered to be trading operations in 1996 and 1995 and, therefore, were not reported net of related costs to purchase such items.

Williams' operations also enter into energy-related derivative financial instruments and derivative commodity instruments (primarily futures contracts, option contracts and swap agreements) to hedge against market price fluctuations of certain commodity inventories and sales and purchase commitments. Unrealized and realized gains and losses on these hedge contracts are deferred and recognized in income when the related hedged item is recognized and recorded with the related hedged item. These contracts are initially and regularly evaluated to determine that there is a high correlation between changes in the market value of the hedge contract and market value of the hedged item.

Interest-Rate Derivatives

Williams enters into interest-rate swap agreements to modify the interest characteristics of its long-term debt. These agreements are designated with all or a portion of the principal balance and term of specific debt obligations. These agreements involve the exchange of amounts based on a fixed-interest rate for amounts based on variable interest rates without an exchange of the notional amount upon which the payments are based. The difference to be paid or received is accrued and recognized as an adjustment of interest expense. Gains and losses from terminations of interest-rate swap agreements are deferred and amortized as an adjustment to interest expense over the original term of the terminated swap agreement.

Kern River specifically has interest-rate swap agreements that are not designated with long-term debt that are recorded in other liabilities at market value. Changes in market value are recorded as adjustments to a regulatory asset which is expected to be recovered in transportation rates.

Williams enters into interest-rate forward contracts to lock-in underlying treasury rates on anticipated long-term debt issuances. The settlement amounts upon termination of the contracts are deferred and amortized as an adjustment to interest expense of the issued long-term debt over the term of the settled forward contract.

Capitalization of Interest

Williams capitalizes interest on major projects during construction. Interest is capitalized on borrowed funds and, where regulation by the FERC exists, on internally generated funds. The rates used by regulated companies are calculated in accordance with FERC rules. Rates used by unregulated companies approximate

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

the average interest rate on related debt. Interest capitalized on internally generated funds is included in non-operating other income (expense) — net.

Employee Stock-Based Awards

Employee stock-based awards are accounted for under Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations. Williams' fixed plan common stock options do not result in compensation expense, because the exercise price of the stock options equals the market price of the underlying stock on the date of grant.

Income Taxes

Williams includes the operations of its subsidiaries in its consolidated federal income tax return. Deferred income taxes are computed using the liability method and are provided on all temporary differences between the financial basis and the tax basis of Williams' assets and liabilities.

Earnings Per Share

Basic earnings per share are based on the sum of the average number of common shares outstanding and issuable restricted and deferred shares. Diluted earnings per share assumes issuance of common stock from dilutive stock options and conversion of the \$3.50 cumulative convertible preferred stock into common stock effective May 1, 1995. The earnings per share amounts and number of shares for 1996 and 1995 have been restated to reflect the effect of the two-for-one stock split and distribution (see Note 15) and the adoption of Statement of Financial Accounting Standards (SFAS) No. 128, "Earnings Per Share" (see Note 9).

New Accounting Standards

In June 1997, the Financial Accounting Standards Board issued two new accounting standards, SFAS No. 130, "Reporting Comprehensive Income," and SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information." Both standards, effective for fiscal years beginning after December 15, 1997, are disclosure-oriented standards. Therefore, neither standard will affect Williams' reported consolidated net income or cash flows.

Note 2. Acquisitions

Nortel

On April 30, 1997, Williams and Nortel combined their customer-premise equipment sales and service operations into a limited liability company, Williams Communications Solutions, LLC. In addition, Williams paid \$68 million to Nortel. Williams has accounted for its 70 percent interest in the operations that Nortel contributed to the LLC as a purchase business combination, and beginning May 1, 1997, has included the results of operations of the acquired company in Williams' Consolidated Statement of Income. Accordingly, the acquired assets and liabilities, including \$168 million in accounts receivable, \$68 million in accounts payable and accrued liabilities and \$150 million in debt obligations, have been recorded based on an allocation of the purchase price, with substantially all of the cost in excess of historical carrying values allocated to goodwill.

Williams recorded the 30 percent reduction in its operations contributed to the LLC as a sale to the minority shareholders of the LLC. Williams recognized a gain of \$44.5 million based on the excess of the fair value over the net book value (approximately \$71 million) of its operations conveyed to the LLC minority interest. Income taxes were not provided on the gain, because the transaction did not affect the difference between the financial and tax bases of identifiable assets and liabilities.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

If the transaction had occurred on January 1, 1996, Williams' unaudited pro forma revenues for the years ended 1997 and 1996 would have been \$4,658 million and \$4,268 million, respectively. The pro forma effect of the transaction on Williams' net income is not significant. Pro forma financial information is not necessarily indicative of results of operations that would have occurred if the transaction had occurred on January 1, 1996, or of future results of operations of the combined companies.

Kern River

On January 16, 1996, Williams acquired the remaining interest in Kern River for \$206 million in cash. The acquisition was accounted for as a purchase, and the acquired assets and liabilities have been recorded based on an allocation of the purchase price, with substantially all of the cost in excess of Kern River's historical carrying value allocated to property, plant and equipment.

Transco

On January 18, 1995, Williams acquired 60 percent of Transco Energy's outstanding common stock in a cash tender offer for \$430.5 million. Williams acquired the remaining 40 percent of Transco Energy's outstanding common stock on May 1, 1995, through a merger by exchanging the remaining Transco Energy common stock for approximately 31.2 million shares of Williams common stock valued at \$334 million. The acquisition was accounted for as a purchase with 60 percent of Transco Energy's results of operations included in Williams' Consolidated Statement of Income for the period January 18, 1995, through April 30, 1995, and 100 percent included beginning May 1, 1995. The purchase price, including transaction fees and other related costs, was approximately \$800 million, excluding \$2.3 billion in preferred stock and debt obligations of Transco Energy.

Note 3. Discontinued operations

On January 5, 1995, Williams sold its network services operations to LDDS Communications, Inc. for \$2.5 billion in cash. The sale yielded a gain of \$1 billion (net of income taxes of approximately \$732 million) which is reported as income from discontinued operations.

Note 4. Revenues and operating profit

Revenues and operating profit of Gas Pipelines and Energy Services for the years ended December 31, 1997, 1996 and 1995, are as follows:

		1997		1996		1995
		and the same	()	lillions)	-	
Revenues:						
Gas Pipelines:						
Central	5	184.4	5	178.4	5	174.3
Kern River Gas Transmission		167.1		160.6		-
Northwest Pipeline		273.1		269.7		255.2
Texas Gas Transmission		293.0		306.1		276.3
Transcontinental Gas Pipe Line		766.3		760.4		725.3
	51	,683.9	\$1	,675.2	\$1	,431.1

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Energy Services: Energy Marketing & Trading \$ 135.8 \$ 261.1 \$ 135.8
Energy Marketing & Trading \$ 135.8 \$ 261.1 \$ 15 Exploration & Production 130.1 82.4 6 Field Services 690.3 616.3 5 Petroleum Services 548.7 493.3 35 \$1,504.9 \$1,453.1 \$1.05 Operating Profit:
Exploration & Production 130.1 82.4 6 Field Services 690.3 616.3 5 Petroleum Services 548.7 493.3 3 \$1,504.9 \$1,453.1 \$1,00
Field Services 690.3 616.3 5. Petroleum Services 548.7 493.3 3. \$1,504.9 \$1,453.1 \$1,00 Operating Profit:
\$1,504.9 \$1,453.1 \$1,0 ⁻¹ Operating Profit:
Operating Profit:
Gas Pipelines:
Central \$ 57.0 \$ 44.8 \$
Kern River Gas Transmission
Northwest Pipeline
Texas Gas Transmission
Transcontinental Gas Pipe Line
\$ 614.2 \$ 562.4 \$ 38
Energy Services:
Energy Marketing & Trading \$ 70.6 \$ 66.4 \$
Exploration & Production
Field Services
Petroleum Services
\$ 360.9 \$ 332.3 \$ 2

Note 5. Investing activities

Investing income for the years ended December 31, 1997, 1996 and 1995, is as follows:

		1997	-	1996	_	1995
			(M	lillions)		
Interest	5	9.9	5	11.1	5	37.2
Dividends		1.4		1.6		16.1
Equity earnings		7.9		6.1		40.6
	S	19.2	5	18.8	5	93.9

Dividends and distributions received from companies carried on an equity basis were \$7 million in 1997 and 1996, and \$44 million in 1995.

At December 31, 1997, certain equity investments, with a carrying value of \$46 million, have a market value of \$175 million.

Note 6. Asset sales and write-offs

In the fourth quarter of 1997, Communications incurred charges totaling \$49.8 million related to the decision to sell the learning content business, and the write-down of assets and the development costs associated with certain advanced applications.

In 1996, Williams recognized a pre-tax gain of \$15.7 million from the sale of certain communication rights for approximately \$38 million.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

In 1995, the development of a commercial coal gasification venture in south-central Wyoming was canceled, resulting in a \$41.4 million pre-tax charge.

In 1995, Williams sold its 15 percent interest in Texasgulf Inc. for approximately \$124 million in cash, which resulted in an after-tax gain of approximately \$16 million because of previously unrecognized tax benefits included in the provision for income taxes.

Note 7. Provision for income taxes

The provision (credit) for income taxes from continuing operations includes:

	1997	1996	1995
		(Millions)	
Current:			
Federal	\$ 75.9	\$ 96.3	\$(26.5)
State	18.4	14.4	3.1
Foreign	1.9		
	96.2	110.7	(23.4)
Deferred:			
Federal	70.4	61.9	114.2
State	11.4	10.5	11.2
	81.8	72.4	125.4
Total provision	\$178.0	\$183.1	\$102.0

Reconciliations from the provision for income taxes from continuing operations at the statutory rate to the provision for income taxes are as follows:

	1997	1996	1995
and Armen Parks		(Millions)	
Provision at statutory rate	\$185.0	\$190.9	\$140.5
Increases (reductions) in taxes resu'ting from:			
State income taxes	19.3	16.1	13.5
Income tax credits	(16.5)	(19.0)	(18.7)
Non-taxable gain from sale of interest in subsidiary (Note 2)	(15.6)		-
Decrease in valuation allowance for deferred tax assets	-	_	(29.8)
Reversal of prior tax accruals		_	(8.0)
Other — net	5.8	(4.9)	4.5
Provision for income taxes	\$178.0	\$183.1	\$102.0

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Significant components of deferred tax liabilities and assets as of December 31 are as follows:

	1997	1996*
	(Mil	lions)
Deferred tax liabilities:		
Property, plant and equipment	\$1,839.4	\$1,755.8
Investments	120.9	93.3
Other	116.8	120.3
Total deferred tax liabilities	2,077.1	1,969.4
Deferred tax assets:		
Deferred revenues	84.9	31.5
Rate refunds	119.9	111.4
Accrued liabilities	144.5	171.7
Minimum tax credits	131.3	86.8
Other	102.2	140.9
Total deferred tax assets	582.8	542.3
Net deferred tax liabilities	\$1,494.3	\$1,427.1

[·] Reclassified to conform to current classifications.

Cash payments for income taxes (net of refunds) were \$48 million, \$395 million and \$339 million in 1997, 1996 and 1995, respectively.

Note 8. Extraordinary loss

In September 1997, Williams initiated a restructuring of its debt portfolio (see Note 14). During 1997, Williams paid approximately \$1.4 billion to redeem approximately \$1.3 billion of debt with stated interest rates in excess of 8.8 percent, resulting in an extraordinary loss of \$79.1 million (net of a \$46.6 million benefit for income taxes). In addition, approximately \$30 million of costs to redeem have been deferred as a regulatory asset for rate recovery.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 9. Earnings per share

Basic and diluted earnings per common share are computed for the years ended December 31, 1997, 1996 and 1995, as follows:

	(Dellery in		
		millions, excep s; shares in tho	
Income from continuing operations		\$362.3	\$299.4 (15.3
Income from continuing operations available to common stockholders for basic earnings per share	. 340.7	351.9	284.1
Convertible preferred stock dividends	8.7	8.8	5.8
Income from continuing operations available to common stockholders for diluted earnings per share	\$349.4	\$360.7	\$289.9
Basic weighted-average shares	321,184	319,048	302,807
Convertible preferred stock	. 11,717	11,718	7,866
Stock options	4,638	5,232	3,370
	16,355	16,950	11,236
Diluted weighted-average shares	. 337,539	335,998	314,043
Earnings per share from continuing operations:		Management.	-
Basic	\$1.06	\$1.10	\$.94
Diluted	\$1.04	\$1.07	\$.92

Options to purchase approximately 3.1 million shares of common stock at a weighted-average exercise price of \$27.93 were outstanding at December 31, 1997, but were not included in the computation of diluted earnings per common share. Inclusion of these shares would be antidilutive, as the exercise prices of the options exceed the average market price of the common shares.

Note 10. Employee benefit plans

Pensions

Williams maintains non-contributory defined-benefit pension plans covering substantially all of its employees. Benefits are based on years of service and average final compensation. Pension costs are funded to satisfy minimum requirements prescribed by the Employee Retirement Income Security Act of 1974.

Net pension expense consists of the following:

	1997	1996	1995
		(Millions)	
Service cost for benefits earned during the year	\$ 30.9	\$ 30.3	\$ 19.5
Interest cost on projected benefit obligation	49.8	43.9	40.1
Actual return on plan assets		(100.6)	(120.3)
Amortization and deferrals		61.3	82.0
Net pension expense	\$ 30.7	\$ 34.9	\$ 21.3

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Net pension expense increased in 1996 from 1995 as a result of a decrease in the discount rate from 8½ percent to 7¼ percent and an increase in the number of plan participants.

The following table presents the funded status of the plans:

	19	97	1996
	-	(Mill	ions)
Actuarial present value of benefit obligations:			
Vested benefits	\$5	07	\$407
Non-vested benefits	_	42	37
Accumulated benefit obligations	5	49	444
Effect of projected salary increases	2	08	167
Projected benefit obligations		57	611
Assets at market value	7	36	637
Assets less than (in excess of) projected benefit obligations		21	(26)
Unrecognized net (loss) gain		12)	37
Unrecognized prior-service cost		(6)	(8)
Unrecognized transition asset	_	3	3
Pension liability	5	6	\$ 6

The discount rate used to measure the present value of benefit obligations is 7½ percent (7½ percent in 1996); the assumed rate of increase in future compensation levels is 5 percent; and the expected long-term rate of return on assets is 10 percent. Plan assets consist primarily of commingled funds and assets held in a master trust. The master trust is comprised primarily of domestic and foreign common and preferred stocks, corporate bonds, United States government securities and commercial paper.

Subsequent to December 31, 1997, Williams offered an early retirement incentive program to a certain group of employees. This program will not have a material impact on the funded status of the plans or Williams' financial position.

Postretirement Benefits Other Than Pensions

Williams sponsors health care plans that provide postretirement medical benefits to retired Williams employees who were employed full time, hired prior to January 1, 1992 (January 1, 1996, for Transco Energy employees) and have met certain other requirements.

The plans provide for retiree contributions and contain other cost-sharing features such as deductibles and coinsurance. The accounting for the plans anticipates future cost-sharing changes to the written plans that are consistent with Williams' expressed intent to increase the retiree contribution rate annually, generally in line with health care cost increases, except for certain retirees whose premiums are fixed. A portion of the cost has been funded in trusts by Williams' FERC-regulated natural gas pipeline subsidiaries to the extent recovery from customers can be achieved. Plan assets consist of assets held in two master trusts and money market funds. One of the master trusts was previously described, and the other consists primarily of domestic and foreign common stocks, government bonds and commercial paper.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Net postretirement benefit expense consists of the following:

	_1	997		996 illions)		1995
Service cost for benefits earned during the year	\$	7.1	5	6.4	S	7.4
Interest cost on accumulated postretirement benefit obligation		24.4		22.7		23.9
Actual return on plan assets	(19.4)	(16.4)	((17.9)
Amortization of unrecognized transition obligation		4.1		5.0		5.0
Amortization and deferrals		21.0		19.7		23.1
Net postretirement benefit expense	s	37.2	\$	37.4	s	41.5

The following table presents the funded status of the plans:

	1997	1996
	(Mill	ions)
Actuarial present value of postretirement benefit obligation:		
Retirces	\$223	\$200
Fully eligible active plan participants	34	26
Other active plan participants	126	89
Accumulated postretirement benefit obligation	383	315
Assets at market value	185	155
Assets less than accumulated postretirement benefit obligation	198	160
Unrecognized net gain	18	60
Unrecognized prior-service credit	4	1
Unrecognized transition obligation	(61)	(65)
Postretirement benefit liability	\$159	\$156

The amount of postretirement benefit costs deferred as a regulatory asset at December 31, 1997 and 1996, is \$107 million and \$118 million, respectively, and is expected to be recovered through rates over approximately 15 years.

The discount rate used to measure the present value of benefit obligations is 74 percent (7½ percent in 1996). The expected long-term rate of return on plan assets is 10 percent (6 percent after taxes). The annual assumed rate of increase in the health care cost trend rate for 1998 is 8½ to 9½ percent, systematically decreasing to 5 percent by 2006. The health care cost trend rate assumption has a significant effect on the amounts reported. Increasing the assumed health care cost trend rate by 1 percent in each year would increase the aggregate of the service and interest cost components of postretirement benefit expense for the year ended December 31, 1997, by \$5 million and the accumulated postretirement benefit obligation as of December 31, 1997, by \$46 million.

Other

Williams maintains various defined-contribution plans covering substantially all employees. Company contributions are based on employees' compensation and, in part, match employee contributions. Company contributions are invested primarily in Williams common stock. Williams' contributions to these plans were \$29 million in 1997, \$23 million in 1996 and \$19 million in 1995.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Note 11. Inventories

	1997	1996
	(Mil	lions)
Natural gas in underground storage:		
Transcontinental Gas Pipe Line (LIFO)	\$ 38.3	\$ 38.8
Energy Marketing & Trading	3.0	1.5
Other	16.5	_
Petroleum products:		
Energy Marketing & Trading	68.6	12.7
Other	30.1	33.7
Materials and supplies	140.3	112.0
Other	3.7	5.9
	\$300.5	\$204.6

If inventories valued on the LIFO method at D cember 31, 1997, were valued at current average cost, the amount would increase by approximately \$13 million. Inventories valued on the LIFO method at December 31, 1996, approximate current average cost.

Note 12. Property, plant and equipment

1997	1996
(Mill	ions)
 \$ 844.2	\$ 787.4
1,003.9	990.5
1,478.6	1,447.9
 1,022.7	958.9
 3,334.8	3.095.7
100 800 00000	N KNOTH CO
 43.0	5.4
 318.5	255.1
2.352.4	2.188.3
1,055.2	1.073.1
535.0	257.3
296.1	152.7
12,284.4	11,212.3
 (2,228.8)	(1,826.0)
\$10,055.6	\$ 9,386.3
	(Milli \$ 844.2 1,003.9 1,478.6 1,022.7 3,334.8 43.0 318.5 2,352.4 1,055.2 535.0 296.1 12,284.4 (2,228.8)

Commitments for construction and acquisition of property, plant and equipment are approximately \$530 million at December 31, 1997.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Note 13. Accounts payable and accrued liabilities

Under Williams' cash-management system, certain subsidiaries' cash accounts reflect credit balances to the extent checks written have not been presented for payment. The amounts of these credit balances included in accounts payable are \$92 million at December 31, 1997, and \$95 million at December 31, 1996.

	1996	1997
	(Mills	ions)
Accrued liabilities:		
Rate refunds	\$ 337.5	\$305.1
Employee costs	191.5	178.1
Interest	79.4	95.2
Income taxes payable	76.0	77.6
Taxes other than income taxes	72.4	66.2
Other	400.5	253.1
	\$1,157.3	\$975.3

Note 14. Debt, leases and banking arrangements

Notes Payable

During 1997, Williams Holdings of Delaware, Inc. (Williams Holdings) entered into a commercial paper program backed by new short-term bank-credit facilities totaling \$650 million. At December 31, 1997, \$645 million of commercial paper was outstanding under the program. In addition, Williams has entered into various other short-term credit agreements with amounts outstanding totaling \$48 million and \$269.5 million at December 31, 1997 and 1996, respectively. The weighted-average interest rate on the outstanding short-term borrowings at December 31, 1997 and 1996, was 6.56 percent and 7.85 percent, respectively.

THE WILLIAMS COMPANIES, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Debt

	Weighted-average	Manager and Property of the Parket of the Pa	ber 31,
	interest rate*	1997	1996
The Williams Companies, Inc.		(Millions)	
Revolving credit loans	7.1%	\$ 383.0	s -,
2025	8.6	137.0	587.5
Notes, 6.365% — 9.625%, payable through 2004	7.0	994.7	817.5
Williams Gas Pipelines Central	100	The state of	
Variable rate notes, payable 1999 Kern River Gas Transmission	8.2	130.0	130.0
Notes, 6.42% and 6.72%, payable through 2001	6.6	586.4	617.7
Northwest Pipeline			
Debentures, 7.125% — 10.65%, payable through 2025	8.3	151.6	360.0
Notes, 6.625%, payable 2007	6.6	250.0	-
Adjustable rate notes, payable through 2002	9.0	8.3	10.0
Texas Gas Transmission			
Debentures, 7.25%, payable 2027	7.3	99.0	-
Notes, 9.625% and 8.625%, payable 1997 and 2004	8.6	152.4	253.6
Transcontinental Gas Pipe Line		-	9.7
Revolving credit loans	6.3	160.0	_
Debentures, 7.25% and 9.125%, payable through 2026	7.3	199.7	352.4
redemption in 2001)		200.0	200.0
Notes, 8.125% and 8.875%, payable 1997 and 2002	8.9	128.2	227.7
Adjustable rate note, payable 2002	5.8	150.0	_
Williams Holdings of Delaware			
Revolving credit loans	6.3	200.0	500.0
Debentures, 6.25%, payable 2006		248.9	248.8
Notes, 6.365% — 6.91%, payable through 2002	6.7	258.6	_
Williams Pipe Line	4.2		11
Notes, 8.95% and 9.78%, payable through 2001	9.0	40.0	0.001
Williams Energy Ventures			200
Adjustable rate notes	-	_	25.6
Williams Communications Solutions, LLC	98.2	0.0000	
Revolving credit loans	6.2	125.0	
Other, payable through 2000	7.8	3.6	5.7
		4,606.4	4,436.5
Current portion of long-term debt		(41.1)	(59.6
		\$4,565.3	\$4,376.9

^{*} At December 31, 1997, including the effects of interest-rate swaps.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

In September 1997, Williams initiated a restructuring of its debt portfolio. As of December 31, 1997, Williams has redeemed approximately \$1.3 billion of debt with stated interest rates in excess of 8.8 percent. In January 1998, Williams redeemed \$40 million of additional debt obligations. The restructuring was temporarily financed with the combination of short-term bank agreements, commercial paper and Williams' existing bank-credit agreement, until new long-term debt securities were issued. During the fourth quarter of 1997, Williams issued \$550 million of new long-term debt obligations. In January 1998, Williams issued approximately \$700 million in additional debt obligations.

In July 1997, Williams entered into a new \$1 billion bank-credit agreement, replacing the previous agreement. Under the new credit agreement, Northwest Pipeline, Transcontinental Gas Pipe Line, Texas Gas Transmission, and Williams Communications Solutions, LLC have access to various amounts of the facility, while Williams (parent) and Williams Holdings have access to all unborrowed amounts. Interest rates vary with current market conditions.

For financial statement reporting purposes at December 31, 1997, \$560 million in notes payable and current debt obligations, primarily related to the restructuring noted above, have been classified as non-current obligations based on Williams' intent and ability to refinance on a long-term basis. Williams' subsequent issuance of \$700 million of long-term debt obligations in January 1998 is sufficient to complete these refinancings.

Interest-rate swaps with a notional value of \$450 million are currently being utilized to convert certain fixed rate debt obligations resulting in an effective weighted-average floating rate of 5.24 percent at December 31, 1997. Interest-rate swaps with a notional value of \$130 million are currently being utilized to convert certain variable rate debt obligations resulting in an effective weighted-average fixed rate of 7.78 percent at December 31, 1997.

Certain interest-rate swap agreements relating to Kern River which preceded the January 1996 purchase of Kern River by Williams and the subsequent Kern River debt refinancing, remain outstanding. In 1996, Kern River entered into additional interest-rate swap agreements to manage the exposure from the original interest-rate swap agreements. As described in Note 1, these interest-rate swap agreements are not designated with the Kern River debt, but when combined with interest on the debt obligations, Kern River's effective interest rate is 8.5 percent.

Aggregate minimum maturities and sinking-fund requirements, excluding lease payments and considering the reclassification of current obligations as previously described, for each of the next five years are as follows:

	(Millions)
1998	\$ 40
1999	349
2000	251
2001	1,052
2002	1,512

Cash payments for interest (net of amounts capitalized) are as follows: 1997 — \$396 million; 1996 — \$347 million; and 1995 — \$266 million.

Leases

Future minimum annual rentals under non-cancelable operating leases are \$113 million in 1998, \$99 million in 1999, \$84 million in 2000, \$59 million in 2001, \$55 million in 2002 and \$176 million thereafter.

Total rent expense was \$126 million in 1997 and \$78 million in 1996 and 1995.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 15. Stockholders' equity

On November 20, 1997, the board of directors of Williams declared a two-for-one common stock split and distribution; 160.1 million shares were issued on December 29, 1997. All references in the financial statements and notes to the number of common shares outstanding and per-share amounts reflect the effect of the split.

In the third quarter of 1996, the board of directors authorized the open-market purchase of up to \$800 million of Williams common stock. During 1996, 1.9 million shares were purchased at a total cost of approximately \$31 million. No shares were purchased during 1997. In the fourth quarter of 1997, Williams' board of directors terminated the repurchase program.

In connection with the 1995 merger with Transco Energy, Williams exchanged all of Transco Energy's outstanding \$3.50 cumulative convertible preferred stock for 2.5 million shares of Williams' \$3.50 cumulative convertible preferred stock. These shares are redeemable by Williams beginning in November 1999, at an initial price of \$51.40 per share. Each share of \$3.50 preferred stock is convertible at the option of the holder into 4.6875 shares of Williams common stock. Dividends per share of \$3.50 were recorded in 1997 and 1996, and \$2.33 in 1995.

During 1995, Williams exchanged 2.8 million shares of its \$2.21 cumulative preferred stock with a carrying value of \$69 million for 9.6 percent debentures with a fair value of \$72.5 million. The difference in the fair value of the new securities and the carrying value of the preferred stock exchanged was recorded as a decrease in capital in excess of par value. This amount did not impact net income, but is included in preferred stock dividends on the Consolidated Statement of Income and in the computation of earnings per share. The remaining shares of \$2.21 cumulative preferred stock were redeemed by Williams at par (\$25) in September 1997 for a total of \$18.5 million. Dividends per share of \$1.47 were recorded in 1997, and \$2.21 in 1996 and 1995.

In 1996, the board of directors adopted a Stockholder Rights Plan (the Rights Plan). Under the Rights Plan, each outstanding share of common stock has one-third of a preferred stock purchase right attached. Under certain conditions, each right may be exercised to purchase, at an exercise price of \$140 (subject to adjustment), one two-hundredth of a share of junior participating preferred stock. The rights may be exercised only if an Acquiring Person acquires (or obtains the right to acquire) 15 percent or more of Williams common stock; or commences an offer for 15 percent or more of Williams common stock; or the board of directors determines an Adverse Person has become the owner of 10 percent or more of Williams common stock. The rights, which do not have voting rights, expire in 2006 and may be redeemed at a price of \$.01 per right prior to their expiration, or within a specified period of time after the occurrence of certain events. In the event a person becomes the owner of more than 15 percent of Williams common stock or the board of directors determines that a person is an Adverse Person, each holder of a right (except an Acquiring Person or an Adverse Person) shall have the right to receive, upon exercise, common stock having a value equal to two times the exercise price of the right. In the event Williams is engaged in a merger, business combination or 50 percent or more of Williams' assets, cash flow or earnings power is sold or transferred, each holder of a right (except an Acquiring Person or an Adverse Person) shall have the right to receive, upon exercise, common stock of the acquiring company having a value equal to two times the exercise price of the right.

Williams has several plans providing for common-stock-based awards to employees and to non-employee directors. The plans permit the granting of various types of awards including, but not limited to, stock options, stock-appreciation rights, restricted stock and deferred stock. Awards may be granted for no consideration other than prior and future services. The purchase price per share for stock options and the grant price for stock-appreciation rights may not be less than the market price of the underlying stock on the date of grant. Stock options generally become exercisable after five years, subject to accelerated vesting if certain future stock prices are achieved. Stock options expire 10 years after grant. At December 31, 1997, 46.7 million shares

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

of common stock were reserved for issuance pursuant to existing and future stock awards, of which 21.4 million shares were available for future grants (15.6 million at December 31, 1996).

The following summary reflects stock option activity and related information for 1997 and 1996:

	1997		1996		
	Options	Weighted- Average Exercise Price	Options	Weighted- Average Exercise Price	
		(Options)	n millions)		
Outstanding — beginning of year	19.7	\$12.85	15.7	\$10.02	
	6.7	24.83	8.2	16.71	
Exercised		11.13	(4.0)	9.14	
Canceled	(.3)	19.82	(.2)	21.01	
Outstanding — end of year	22.3	\$16.66	19.7	\$12.85	
Exercisable at end of year	15.7	\$13.21	10.9	\$10.29	
Weighted-average grant date fair value of options					
granted during the year		\$ 5.98		\$ 3.92	
Granted Exercised Canceled Outstanding — end of year Exercisable at end of year Weighted-average grant date fair value of options	6.7 (3.8) (.3) 22.3	24.83 11.13 19.82 \$16.66 \$13.21	8.2 (4.0) (.2) 19.7	16.7 9.1- 21.0 \$12.8 \$10.2	

The following summary provides information about stock options outstanding and exercisable at December 31, 1997:

	Stock Options Outstanding			Stock Options			
Range of Exercise Prices	Options	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Life	Options	Weighted- Average Exercise Price		
	(millions)			(millions)			
\$4.62 to \$17.32	15.4	\$12.91	7.5 years	15.4	\$12.91		
\$18.00 to \$49.34	6.9	24.98	9.6 years	3	28.14		
Total	22.3	\$16.66	8.1 years	15.7	\$13.21		

The fair value of the stock options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted-average assumptions: expected life of the stock options of five years; volatility of the expected market price of Williams common stock of 23 percent (24 percent in 1996 and 1995); risk-free interest rate of 6.1 percent (6.2 percent in 1996 and 1995); and a dividend yield of 2.4 percent (3 percent in 1996 and 1995).

Pro forma net income and earnings per share, assuming Williams had applied the fair-value method of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" in measuring compensation cost beginning with 1995 employee stock-based awards, are as follows:

	1997		1996			1995						
The State of the last		Pro	Rej	ported		Pro orma	Re	ported		Pro orma	R	ported
Net income (millions)	\$2	52.8	\$2	71.4	\$	359.9	\$	362.3	\$1	,306.1	\$1	,318.2
Basic	5	.76	5	.81	\$	1.10	5	1.10	5	4.26	5	4.30
Diluted	5	.74	5	.80	\$	1.07	\$	1,07	\$	4.13	5	4.17

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Pro forma amounts for 1997 include the remaining total compensation expense from the awards made in 1996, as these awards fully vested in 1997 as a result of the accelerated vesting provisions. Pro forma amounts for 1995 include total compensation expense from the awards made in 1995, as these awards fully vested in 1995 as a result of the accelerated vesting provisions. Since compensation expense from stock options is recognized over the future years' vesting period, and additional awards generally are made each year, pro forma amounts may not be representative of future years' amounts.

Note 16. Financial instruments

Fair-Value Methods

The following methods and assumptions were used by Williams in estimating its fair-value disclosures for financial instruments:

Cash and cash equivalents and notes payable: The carrying amounts reported in the balance sheet approximate fair value due to the short-term maturity of these instruments.

Notes and other non-current receivables: For those notes with interest rates approximating market or maturities of less than three years, fair value is estimated to approximate historically recorded amounts.

Investments — cost: Fair value is estimated to approximate historically recorded amounts as the operations underlying these investments are in their initial phases.

Long-term debt: The fair value of Williams' long-term debt is valued using indicative year-end traded bond market prices for publicly traded issues, while private debt is valued based on the prices of similar securities with similar terms and credit ratings. At December 31, 1997 and 1996, 57 percent and 69 percent, respectively, of Williams' long-term debt was publicly traded. Williams used the expertise of an outside investment banking firm to estimate the fair value of long-term debt.

Interest-rate swaps: Fair value is determined by discounting estimated future cash flows using forward interest rates derived from the year-end yield curve. Fair value was calculated by the financial institutions that are the counterparties to the swaps.

Interest-rate locks: Fair value is determined using year-end traded market prices for the referenced U.S. Treasury securities underlying the contracts. Fair value was calculated by the financial institutions that are parties to the locks.

Energy-related trading and hedging: Includes forwards, options, swaps and purchase and sales commitments. Fair value reflects management's best estimate of market prices considering various factors including closing exchange and over-the-counter quotations, liquidity of the market in which the contract is transacted, the terms of the contract, credit considerations, time value and volatility factors underlying the position:

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Carrying amounts and fair values of Williams' financial instruments

		1997		199	6	77
Asset (liability)		rrylog	Fair Value	Carrying Amount	Fair Value	1
THE REST PROPERTY.		National Services	(Millio	as)	0.00	Ö
Cash and cash equivalents	\$	81,3 \$	81.3	\$ 115.3	\$ 115.3	
Notes and other non-current	receivables	32.5	32.5	27.4	27.4	
Investments - cost		102.8	102.8	71.2	71.2	30
Notes payable	(693.0)	(693.0)	(269.5)	(269.5)
Long-term debt, including cu		(605.4)	(4,693.0)	(4,435.1)	(4,594.4	6
Interest-rate swaps		(51.1)	(46.8)	(54.8)	(63.7	700
Interest-rate locks			(8.3)		6 -	ĵ)
Energy-related trading:						
Assets	PORTS IN VITE	324.9	324.9	253.6	253.6	
Liabilities	manusina popular	383.7)	(383.7)	(339.1)	(339.1	
	to market a too a se	- 1/3 PULL	1000			-
Assets		. 9	11.0	.9	11.2	-
Liabilities		-	(3.6)	(1.3)	(12.2	5.11
The second secon	CALL PARTY OF THE		Control of the Contro	THE RESERVE TO SERVE THE PARTY OF THE PARTY		

The preceding asset and liability amounts for energy-related hedging represent unrealized gains or losses and do not include the related deferred amounts.

The 1997 average fair value of the energy-related trading assets and liabilities is \$258 million and \$345 million, respectively. The 1996 average fair value of the energy-related trading assets and liabilities is \$196 million and \$322 million, respectively.

Williams has recorded liabilities of \$21 million and \$18 million at December 31, 1997 and 1996, respectively, for certain guarantees that represent the estimated fair value of these financial instruments.

Off-Balance-Sheet Credit and Market Risk

Williams is a participant in the following transactions and arrangements that involve financial instruments that have off-balance-sheet risk of accounting loss. It is not practicable to estimate the fair value of these off-balance-sheet financial instruments because of their unusual nature and unique characteristics.

In 1997, Williams entered into agreements to sell, on an ongoing basis, certain of their accounts receivables. Williams also sold certain receivables in 1996 under another revolving receivable sales program. At December 31, 1997 and 1996, \$343 million and \$152 million have been sold, respectively.

In connection with the sale of Williams' network services operations, Williams has been indemnified by LDDS against any losses related to retained guarantees of \$135 million and \$158 million at December 31, 1997 and 1996, respectively, for lease rental obligations.

Williams has issued other guarantees and letters of credit with off-balance-sheet risk that total approximately \$56 million and \$10 million at December 31, 1997 and 1996, respectively. Williams believes it will not have to perform under these agreements because the likelihood of default by the primary party is remote and/or because of certain indemnifications received from other third parties.

Commodity Price-Risk Management Services

Williams, through Energy Marketing & Trading, provides price-risk management services associated with the energy industry to its customers. These services are provided through a variety of financial instruments, including forward contracts, futures contracts, option contracts, swap agreements and purchase and sale

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

commitments. See Note 1 for a description of the accounting for these trading activities. The net gain from trading activities was \$125.8 million, \$99.2 million and \$65.8 million in 1997, 1996 and 1995, respectively.

Energy Marketing & Trading enters into forward contracts and purchase and sale commitments which involve physical delivery of an energy commodity. Prices under these contracts are both fixed and variable. Swap agreements call for Energy Marketing & Trading to make payments to (or receive payments from) counterparties based upon the differential between a fixed and variable price or variable prices for different locations. The variable prices are generally based on either industry pricing publications or exchange quotations. Energy Marketing & Trading buys and sells option contracts which give the buyer the right to exercise the options and receive the difference between a predetermined strike price and a market price at the date of exercise. The market prices used for option contracts are generally exchange quotations. Energy Marketing & Trading also enters into futures contracts, which are commitments to either purchase or sell a commodity at a future date for a specified price and are generally settled in cash, but may be settled through delivery of the underlying commodity. The market prices for futures contracts are based on exchange quotations.

Energy Marketing & Trading is subject to market risk from changes in energy commodity market prices, the portfolio position of its financial instruments and physical commitments, the liquidity of the market in which the contract is transacted, and changes in interest rates and credit risk.

Energy Marketing & Trading manages market risk through established trading policy guidelines, which are monitored on an ongoing basis. Energy Marketing & Trading attempts to minimize credit-risk exposure to trading counterparties and brokers through formal credit policies and monitoring procedures. In the normal course of business, collateral is not required for financial instruments with credit risk.

The notional quantities for trading activities at December 31 are as follows:

	1997		19	196
	Payor	Receiver	Payor	Receiver
Fixed price:				
Natural gas (TBtu)	1,327.9	1,702.5	1,066.6	1,196.8
Refined products and crude (MMBbls)	337.2	230.7	34.4	26.3
Power (Terawatt Hrs)		16.7		-
Variable price:				
Natural gas (TBtu)	2,091.1	1,508.2	1,584.9	1,123.8
Refined products and crude (MMBbls)		3.1	3.7	3.3
Power (Terawatt Hrs)		2.1	_	-

The net cash flow requirement related to these contracts at December 31, 1997 and 1996, was \$92 million and \$117 million, respectively. At December 31, 1997, the cash flow requirements extend primarily through 2007.

Concentration of Credit Risk

Williams' cash equivalents consist of high quality securities placed with various major financial institutions with high credit ratings. Williams' investment policy limits its credit exposure to any one financial institution.

At December 31, 1997 and 1996, approximately 57 percent and 69 percent, respectively, of receivables are for the sale or transportation of natural gas and related products or services. Approximately 33 percent and 23 percent of receivables at December 31, 1997 and 1996, respectively, are for communications and related services. Natural gas customers include pipelines, distribution companies, producers, gas marketers and industrial users primarily located in the eastern, northwestern and midwestern United States. Communica-

THE WILLIAMS COMPANIES, INC. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

tions' customers include numerous corporations. As a general policy, collateral is not required for receivables, but customers' financial condition and credit worthiness are evaluated regularly.

Note 17. Other financial information

intercompany revenues (at prices that generally apply to sales to unaffiliated parties) are as follows:

		(Millions)	1995
Gas Pipelines:			
Central	\$ 6.1	\$ 9.2	\$ 9.5
Northwest Pipeline	2.8	1.1	1.8
Texas Gas Transmission	7.6	20.5	37.7
Transcontinental Gas Pipe Line	40.5	34.6	34.2
Energy Services:			
Energy Marketing & Trading*	(47.1)	130.7	62.2
Exploration & Production		57.1	4.9
Field Services	32.3	26.2	14.0
Petroleum Services	81.6	67.7	44.6
Other	12.6	9.3	2
	\$262.9	\$356.4	\$209.1

Energy Marketing & Trading intercompany cost of sales, which are netted in revenues consistent with market-value accounting, exceed intercompany revenues in 1997.

Information for business segments is as follows:

	1997	1996	1995
		(Millions)	
Identifiable assets at December 31:			
Gas Pipelines:			
Central	\$ 854.9	\$ 704.8	\$ 709.2
Kern River Gas Transmission	1,083.0	1,081.6	_
Northwest Pipeline	1,161.3	1,153.9	1,147.5
Texas Gas Transmission	1,162.1	1,132.2	1,151.8
Transcontinental Gas Pipe Line	3,413.9	3,305.4	3,159.5
Energy Services:			
Energy Marketing & Trading	725.1	839.1	438.2
Exploration & Production	247.1	200.3	164.6
Field Services	2,038.4	1,995.0	1,939.3
Petroleum Services	904.6	906.5	863.2
Communications	1,312.9	670.6	401.0
Investments	291.4	190.6	307.6
General corporate and other	684.3	238.8	279.3
Consolidated	\$13,879.0	\$12,418.8	\$10,561.2

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

- In the Personal Service Co. The Person of	1997		1996		1995	
And the second of the second o			(h	fillions)		
Additions to property, plant and equipment:						
Gas Pipelines:						
Central	5	60.4	S	50.9	\$	43.5
Kern River Gas Transmission		15.3		4.7		-
Northwest Pipeline		44.4		62.8		130.5
Texas Gas Transmission		74.5		50.1		32.1
Transcontinental Gas Pipe Line		224.8		272.1		238.7
Energy Services:						
Energy Marketing & Trading		37.6		.6		.4
Exploration & Production		63.3		30.3		15.6
Field Services		158.8		205.7		232.1
Petroleum Services		45.0		55.8		87.9
Communications		276.3		66.9		32.4
General corporate and other		161.7		19.0		14.3
Consolidated	5	1,162.1	5	818.9	\$	827.5
Democratical designation and amortisations		Direction of the last of the l	-		777	
Depreciation, depletion and amortization:						
Gas Pipelines:		28.0	5	27.5	2	27.3
Kern River Gas Transmission	,	17.8		15.5	•	
Northwest Pipeline		55.2		43.2		34.9
Texas Gas Transmission		42.5		41.5		38.9
		129.5		113.7		109.1
Transcontinental Gas Pipe Line		129.5		113.7		109.1
Energy Services:						
Energy Marketing & Trading		.7		.6		1.2
Exploration and Production		12.6		10.5		9.8
Field Services		102.7		94.7		100.4
Petroleum Services		35.0		34.1		26.4
Communications		66.8		30.9		20.3
General corporate and other		8.7	_	8.8	-	7.2
Consolidated	\$	499.5	5	421.0	\$	375.5

Identifiable assets are gross assets used by a business segment, including an allocated portion of assets used jointly by more than one business segment. Items such as investments are considered to be general corporate assets rather than identifiable assets of individual business segments.

Note 18. Contingent liabilities and commitments

Rate and regulatory matters and related litigation

Williams' interstate pipeline subsidiaries, including Williams Pipe Line, have various regulatory proceedings pending. As a result of rulings in certain of these proceedings, a portion of the revenues of these subsidiaries has been collected subject to refund. As to Williams Pipe Line, revenues collected subject to refund were \$328 million at December 31, 1997; it is not expected that the amount of any refunds ordered would be significant. Accordingly, no portion of these revenues has been reserved for refund. As to the other pipelines, \$337 million of revenues has been reserved for potential refund as of December 31, 1997.

In 1997, the Federal Energy Regulatory Commission (FERC) issued orders addressing, among other things, the authorized rates of return for three of Williams' interstate natural gas pipeline subsidiaries. All of

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

the orders involve rate cases that became effective between 1993 and 1995 and, in each instance, these cases have been superseded by more recently filed rate cases. In the three orders, the FERC continued its practice of utilizing a methodology for calculating rates of return that incorporates a long-term growth rate component. However, the long-term growth rate component used by the FERC is now a projection of U.S. gross domestic product growth rates. Generally, calculating rates of return utilizing a methodology which includes a long-term growth rate component results in rates of return that are lower than they would be if the long-term growth rate component were not included in the methodology. Each of the three pipeline subsidiaries challenged its respective FERC order in an effort to have the FERC change its rate of return methodology with respect to these and other rate cases. In October 1997, the FERC voted not to reconsider an order issued in one of the three pipeline proceedings, but convened a conference on January 30, 1998, to consider, on an industry-wide basis, issues with respect to pipeline rates of return.

In 1992, the FERC issued Order 636, Order 636-A and Order 636-B. These orders, which were challenged in various respects by various parties in proceedings ruled on by the U.S. Court of Appeals for the D.C. Circuit, require interstate gas pipeline companies to change the manner in which they provide services. Williams' gas pipelines subsidiaries implemented restructurings in 1993. Certain aspects of three of its pipeline companies' restructurings are under appeal.

On July 16, 1996, the U.S. Court of Appeals for the D.C. Circuit issued an order which in part affirmed and in part remanded Order 636. However, the court stated that Order 636 would remain in effect until FERC issued a final order on remand after considering the remanded issues. With the issuance of this decision, the stay on the appeals of individual pipeline's restructuring cases was lifted. The only appeal challenging Northwest Pipeline's restructuring has been dismissed. On February 27, 1997, the FERC issued Order No. 636-C which dealt with the six issues remanded by the D.C. Circuit. In that order, the FERC reaffirmed that pipelines should be exempt from sharing gas supply realignment costs. Requests for rehearing have been filed for the order.

Contract reformations and gas purchase deficiencies

As a result of FERC Order 636, which requires interstate gas pipelines to change the way they do business, each of the natural gas pipeline subsidiaries has undertaken the reformation or termination of its respective gas supply contracts. None of the pipelines has any significant pending supplier take-or-pay, ratable take or minimum take claims.

Current FERC policy associated with Orders 436 and 500 requires interstate gas pipelines to absorb some of the cost of reforming gas supply contracts before allowing any recovery through direct bill or surcharges to transportation as well as sales commodity rates. Under Orders 636, 636-A, 636-B and 636-C, costs incurred to comply with these rules are permitted to be recovered in full, although a percentage of such costs must be allocated to interruptible transportation service.

Pursuant to a stipulation and agreement approved by the FERC, Williams Gas Pipelines Central (Central) has made 11 filings to direct bill take-or-pay and gas supply realignment costs. The total amount approved for direct billing, net of certain amounts collected subject to refunds, is \$67 million. An intervenor has filed protests seeking to have the FERC review the prudence and eligibility of approximately \$40 million of costs covered by these filings. On July 31, 1996, the administrative law judge issued an initial decision rejecting the intervenor's prudency challenge. On September 30, 1997, the FERC, by a two-to-one vote, reversed the administrative law judge and determined that three life-of-lease producer contracts were imprudently entered into in 1982. Central has filed for rehearing, and management plans to vigorously defend the prudency of these contracts. An intervenor has also filed a protest seeking to have the FERC decide whether non-settlement costs are eligible for recovery under Order No. 636. In January 1997, the FERC held that none of the non-settlement costs could be recovered by Central if these costs were not eligible for recovery under Order No. 636. This order was affirmed on rehearing in April 1997. An initial decision from

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

the administrative law judge is expected in the first quarter of 1998. If the FERC's final ruling on eligibility is unfavorable, Central will appeal these orders to the courts. Central will make additional filings under the applicable FERC orders to recover such additional costs as may be incurred in the future.

Because of the uncertainties pertaining to the outcome of these issues currently pending at the FERC and the status of settlement negotiation and various other factors, Central cannot reasonably estimate the costs that may be incurred nor the related amounts that could be recovered from customers. Central is actively pursuing negotiations with the producers to resolve all outstanding obligations under the contracts. Based on the terms of what Central believes would be a reasonable settlement, \$94 million has been accrued as a liability at December 31, 1997, including a \$5 million fourth-quarter 1997 charge to expense for additional absorption of future costs. Central also has an \$88 million regulatory asset at December 31, 1997, for estimated recovery of future costs from customers. Central cannot predict the final outcome of the FERC's rulings on contract prudency and cost recovery under Order No. 636 and is unable to determine the ultimate liability and loss, if any, at this time. If Central does not prevail in these FERC proceedings or any subsequent appeals, and if Central is able to reach a settlement with the producers consistent with the \$94 million accrued liability, the loss could be the total of the regulatory asset and the \$40 million of protested assets. Central continues to believe that it entered into the gas purchase contracts in a prudent manner under FERC rules in place at the time. Central also believes that the future recovery of these costs would be in accordance with the terms of Order No. 636.

In September 1995, Texas Gas received FERC approval of a settlement regarding Texas Gas' recovery of gas supply realignment costs. Through December 31, 1997, Texas Gas has paid approximately \$76 million and expects to pay no more than \$80 million for gas supply realignment costs, primarily as a result of contract terminations. Texas Gas has recovered approximately \$66 million, plus interest, in gas supply realignment costs.

The foregoing accruals are in accordance with Williams' accounting policies regarding the establishment of such accruals which take into consideration estimated total exposure, as discounted and risk-weighted, as well as costs and other risks associated with the difference between the time costs are incurred and the time such costs are recovered from customers. The estimated portion of such costs recoverable from customers is deferred or recorded as a regulatory asset based on an estimate of expected recovery of the amounts allowed by FERC policy. While Williams believes that these accruals are adequate and the associated regulatory assets are appropriate, costs actually incurred and amounts actually recovered from customers will depend upon the outcome of various court and FERC proceedings, the success of settlement negotiations and various other factors, not all of which are presently foreseeable.

Environmental matters

Since 1989, Texas Gas and Transcontinental Gas Pipe Line have had studies under way to test certain of their facilities for the presence of toxic and hazardous substances to determine to what extent, if any, remediation may be necessary. Transcontinental Gas Pipe Line has responded to data requests regarding such potential contamination of certain of its sites. The costs of any such remediation will depend upon the scope of the remediation. At December 31, 1997, these subsidiaries had reserves totaling approximately \$28 million for these costs.

Certain Williams subsidiaries, including Texas Gas and Transcontinental Gas Pipe Line, have been identified as potentially responsible parties (PRP) at various Superfund and state waste disposal sites. In addition, these subsidiaries have incurred, or are alleged to have incurred, various other hazardous materials removal or remediation obligations under environmental laws. Although no assurances can be given, Williams does not believe that the PRP status of these subsidiaries will have a material adverse effect on its financial position, results of operations or net cash flows.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

Transcontinental Gas Pipe Line, Texas Gas and Central have identified polychlorinated biphenyl (PCB) contamination in air compressor systems, soils and related properties at certain compressor station sites. Transcontinental Gas Pipe Line, Texas Gas and Central have also been involved in negotiations with the U.S. Environmental Protection Agency (EPA) and state agencies to develop screening, sampling and cleanup programs. In addition, negotiations with certain environmental authorities and other programs concerning investigative and remedial actions relative to potential mercury contamination at certain gas metering sites have been commenced by Central, Texas Gas and Transcontinental Gas Pipe Line. As of December 31, 1997, Central had recorded a liability for approximately \$17 million, representing the current estimate of future environmental cleanup costs to be incurred over the next six to ten years. The Field Services unit of Energy Services had recorded an aggregate liability of approximately \$12 million, representing the current estimate of its future environmental and remediation costs, including approximately \$5 million relating to former Central facilities. Texas Gas and Transcontinental Gas Pipe Line likewise had recorded liabilities for these costs which are included in the \$28 million reserve mentioned above. Actual costs incurred will depend on the actual number of contaminated sites identified, the actual amount and extent of contamination discovered, the final cleanup standards mandated by the EPA and other governmental authorities and other factors. Texas Gas, Transcontinental Gas Pipe Line and Central have deferred these costs pending recovery as incurred through future rates and other means.

In connection with the 1987 sale of the assets of Agrico Chemical Company, Williams agreed to indemnify the purchaser for environmental cleanup costs resulting from certain conditions at specified locations, to the extent such costs exceed a specified amount. Such costs have exceeded this amount. At December 31, 1997, Williams had approximately \$11 million accrued for such excess costs. The actual costs incurred will depend on the actual amount and extent of contamination discovered, the final cleanup standards mandated by the EPA or other governmental authorities, and other factors.

A lawsuit was filed in May 1993 in a state court in Colorado in which certain claims have been made against various defendants, including Northwest Pipeline, contending that gas exploration and development activities in portions of the San Juan Basin have caused air, water and other contamination. The plaintiffs in the case sought certification of a plaintiff class. In June 1994, the lawsuit was dismissed for failure to join an indispensable party over which the state court had no jurisdiction. The Colorado court of appeals has affirmed the dismissal and remanded the case to Colorado district court for action consistent with the appeals court's decision. Since June 1994, eight individual lawsuits have been filed against Northwest Pipeline and others in U.S. district court in Colorado, making essentially the same claims. The district court has stayed all of the cases involving Northwest Pipeline until the plaintiffs exhaust their remedies before the Southern Ute Indian Tribal Court. Some plaintiffs filed cases in the Tribal court, but none named Northwest Pipeline as a defendant.

Other legal matters

In 1991, the Southern Ute Indian Tribe (the Tribe) filed a lawsuit against Williams Production Company (Williams Production), a wholly-owned subsidiary of Williams, and other gas producers in the San Juan Basin area, alleging that certain coal strata were reserved by the United States for the benefit of the Tribe and that the extraction of coal-seam gas from the coal strata was wrongful. The Tribe seeks compensation for the value of the coal-seam gas. The Tribe also seeks an order transferring to the Tribe ownership of all of the defendants' equipment and facilities utilized in the extraction of the coal-seam gas. In September 1994, the court granted summary judgment in favor of the defendants and the Tribe lodged an interlocutory appeal with the U.S. Court of Appeals for the Tenth Circuit. Williams Production agreed to indemnify the Williams Coal Seam Gas Royalty Trust (Trust) against any losses that may arise in respect of certain properties subject to the lawsuit. In addition, if the Tribe is successful in showing that Williams Production has no rights in the coal-seam gas, Williams Production has agreed to pay to the Trust for distribution to then-current unitholders, an amount representing a return of a portion of the original purchase price paid for the units. On July 16, 1997.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

the U.S. Court of Appeals for the Tenth Circuit reversed the decision of the district court, held that the Tribe owns the coal-seam gas produced from certain coal strata on fee lands within the exterior boundaries of the Tribe's reservation, and remanded the case to the district court for further proceedings. On September 16, 1997, Amoco Production Company, the class representative for the defendant class (of which Williams Production is a part), filed its motion for rehearing en bane before the Court of Appeals. On December 4, 1997, the Tenth Circuit Court of Appeals agreed to rehear the appeal.

In connection with agreements to resolve take-or-pay and other contract claims and to amend gas purchase contracts, Transcontinental Gas Pipe Line and Texas Gas each entered into certain settlements with producers which may require the indemnification of certain claims for additional royalties which the producers may be required to pay as a result of such settlements. In one of the two remaining cases, a jury verdict found that Transcontinental Gas Pipe Line was required to pay to a producer damages of \$23.3 million including \$3.8 million in attorneys' fees. Transcontinental Gas Pipe Line is considering an appeal. In the other remaining case, a producer has asserted damages, including interest calculated through December 31, 1996, of approximately \$6 million.

Producers have received and may receive other demands, which could result in additional claims. Indemnification for royalties will depend on, among other things, the specific lease provisions between the producer and the lessor and the terms of the settlement between the producer and either Transcontinental Gas Pipe Line or Texas Gas. Texas Gas may file to recover 75 percent of any such additional amounts it may be required to pay pursuant to indemnities for royalties under the provisions of Order 528.

In November 1994, Continental Energy Associates Limited Partnership (the Partnership) filed a voluntary petition under Chapter 11 of the Bankruptcy Code with the U.S. Bankruptcy Court, Middle District of Pennsylvania. The Partnership owned a cogeneration facility in Hazleton, Pennsylvania (the Facility). Hazleton Fuel Management Company (HFMC), a subsidiary of Transco Energy, formerly supplied natural gas and fuel oil to the Facility. Pursuant to a court-approved Plan of Reorganization, all litigation involving HFMC has been fully settled, and HFMC received \$6.3 million from the bankruptcy estate, leaving it with approximately \$14 million of outstanding receivables, all of which have been fully reserved.

In addition to the foregoing, various other proceedings are pending against Williams or its subsidiaries which are incidental to their operations.

Summary

While no assurances may be given, Williams does not believe that the ultimate resolution of the foregoing matters, taken as a whole and after consideration of amounts accrued, insurance coverage, recovery from customers or other indemnification arrangements, will have a materially adverse effect upon Williams' future financial position, results of operations or cash flow requirements.

19. MAPCO acquisition

On November 24, 1997, Williams and MAPCO Inc. announced that they had entered into a definitive merger agreement whereby Williams would acquire MAPCO by exchanging 1.665 shares of Williams common stock for each outstanding share of MAPCO common stock. In addition, outstanding MAPCO employee stock options would be converted into Williams common stock. Approximately 96.8 million shares of Williams common stock valued at approximately \$2.8 billion, based on the closing market price of Williams common stock on December 31, 1997, would be issued in the transaction. The transaction, subject to approval by both Williams and MAPCO stockholders and to review under federal anti-trust laws, is expected to close during the first quarter of 1998. MAPCO is engaged in the NGL pipeline, petroleum refining and marketing and propane marketing businesses, and will become part of the Energy Services business unit.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (Continued)

The merger will be accounted for as a pooling of interests. Anticipated changes in accounting methods as a result of the merger are not expected to have a material impact on the financial position or results of operations of the combined entity.

The following unaudited pro forma information combines the results of operations of Williams and MAPCO as if the companies had been combined throughout the periods presented.

	Years Ended December 31,		
	1997	1996	1995
	(Millions,	except per-shar	e amounts)
Revenues	\$8,241.6	\$6,842.9	\$5,655.0
Income from continuing operations	458.6	492.5	363.6
Net income	373.2	459.8	1,392.9
Basic earnings per common share:			
Income from continuing operations	1.09	1.16	.87
Net income	.88	1.08	3.43
Diluted earnings per common share:			
Income from continuing operations	1.06	1.14	.86
Net income	.86	1.06	3.35

Pro forma financial information is not necessarily indicative of results of operations that would have occurred if the companies had been combined throughout the periods presented or of future results of operations of the combined companies.

QUARTERLY FINANCIAL DATA (Unaudited)

Summarized quarterly financial data are as follows (millions, except per-share amounts). Per-share amounts reflect the effect of the two-for-one common stock split and distribution (see Note 15) and the adoption of SFAS No. 128.

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
1997				
Revenues	\$1,001.4	\$1,020.6	\$1,121.0	\$1,266.6
Costs and operating expenses	581.3	625.1	705.3	752.8
Income before extraordinary loss	105.9	107.8	65.3	71.5
Net income (loss)	105.9	107.8	(8.4)	66.1
Basic earnings per common share:				
Income before extraordinary loss	.32	.33	.20	.21
Net income (loss)	.32	.33	(.03)	.19
Diluted earnings per common share:			()	***
Income before extraordinary loss	.31	.32	.19	.21
Net income (loss)	.31	.32	(.03)	.19
1996				5000
Revenues	\$ 893.7	\$ 837.5	\$ 842.2	\$ 957.8
Costs and operating expenses	499.4	493.9	509.3	561.5
Net income	104.9	80.4	71.0	106.0
Basic earnings per common share	.32	.24	.21	.32
Diluted earnings per common share	.31	.24	.21	.31

The sum of earnings per share for the four quarters may not equal the total earnings per share for the year due to changes in the average number of common shares outstanding.

Second-quarter 1997 net income includes a \$44.5 million gain related to the combination of Williams' and Nortel's customer-premise equipment sales and service business (see Note 2 of Notes to Consolidated Financial Statements). Third-quarter 1997 net income includes an extraordinary loss of \$74 million related to the restructuring of Williams' debt portfolio (see Note 8 of Notes to Consolidated Financial Statements).

Second-quarter 1996 net income includes recognition of favorable income tax adjustments totaling \$10 million related to research credits and previously provided deferred income taxes on certain regulated capital projects. Third-quarter 1996 net income includes approximately \$6 million, net of federal income tax effect, from the effects of state income tax adjustments related to 1995.

Selected comparative fourth-quarter data are as follows (millions, except per-share amounts).

A STATE OF THE STA	1997	1996
Operating profit:		
Gas Pipelines:		
Central	\$ 5.6	\$ 10.9
Kern River Gas Transmission	29.7	29.3
Northwest Pipeline	29.5	21.8
Texas Gas Transmission	32.1	29.5
Transcontinental Gas Pipe Line	63.4	61.0
Energy Services:		2400
Energy Marketing & Trading	42.0	13.6
Exploration & Production	10.2	3.7
Field Services	33.5	56.3
Petroleum Services	33.9	18.3
Communications	(51.8)	.6
Other	2.8	(2.9)
Total operating profit	230.9	242.1
General corporate expenses	(18.7)	(11.6)
Interest expense net	(97.4)	(91.9)
Investing income	7.4	4.1
Gain on sale of asset	-	15.7
Minority interest in income of consolidated subsidiaries	(4.5)	_
Other income (expense) net	(1.8)	8.0
Income before income taxes	115.9	166.4
Provision for income taxes	44.4	60.4
Income before extraordinary loss	71.5	106.0
Extraordinary loss	(5.4)	
Net income	\$ 66.1	\$106.0
Basic earnings per common share	\$.19	\$.32
Diluted earnings per common share	\$.19	\$.31

Communications' fourth-quarter 1997 operating profit includes charges totaling approximately \$49.8 million, related to the decision to sell the learning content business, the write-down of assets and the development costs associated with advanced applications. In addition, 1997 general corporate expenses include approximately \$5 million in costs related to the MAPCO acquisition (see Note 19 of Notes to Consolidated Financial Statements).

Field Services' fourth-quarter 1996 operating profit includes a gain of approximately \$20 million from the property insurance coverage associated with construction of replacement gathering facilities. In addition, 1996 segment operating profit and general corporate expenses together include approximately \$10 million related to an all-employee bonus that was linked to achieving record financial performance. In fourth-quarter 1996, Williams recognized a pre-tax gain of \$15.7 million from the sale of certain communication rights.

Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure.

None.

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All other schedules have been omitted since the required information is not present or is not present in amounts sufficient to require submission of the schedule, or because the information required is included in the financial statements and notes thereto.

THE WILLIAMS COMPANIES, INC. SCHEDULE II — VALUATION AND QUALIFYING ACCOUNTS(a)

	100	Additions			
	Beginning Balance	Charged to Costs and Expenses	Other(c) (Millions)	Deductions(b)	Ending Balance
Allowance for doubtful accounts:					
1997	\$ 9.7	\$8.8	\$7.8	\$7.0	\$19.3
1996	11.3	4.1	1.3	7.0	9.7
1995	7.9	3.8	1.6	2.0	11.3

⁽a) Deducted from related assets.

⁽b) Represents balances written off, net of recoveries and reclassifications.

⁽c) Primarily relates to acquisitions of businesses.

PART III

Item 10. Directors and Executive Officers of the Registrant

The information regarding the Directors and nominees for Director of Williams required by Item 401 of Regulation S-K is presented under the heading "Election of Directors" in Williams' Proxy Statement prepared for the solicitation of proxies in connection with the Annual Meeting of Stockholders of the Company for 1998 (the "Proxy Statement"), which information is incorporated by reference herein. A copy of the Proxy Statement is filed as an exhibit to the Form 10-K. Information regarding the executive officers of Williams is presented following Item 4 herein, as permitted by General Instruction G(3) to Form 10-K and Instruction 3 to Item 401(b) of Regulation S-K. Information required by Item 405 of Regulation S-K is included under the heading "Compliance with Section 16(a) of the Securities Exchange Act of 1934" in the Proxy Statement, which information is incorporated by reference herein.

Item 11. Executive Compensation

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The information required by Item 402 of Regulation S-K regarding executive compensation is presented under the headings "Election of Directors" and "Executive Compensation and Other Information" in the Proxy Statement, which information is incorporated by reference herein. Notwithstanding the foregoing, the information provided under the headings "Compensation Committee Report on Executive Compensation" and "Stockholder Return Performance Presentation" in the Proxy Statement are not incorporated by reference herein. A copy of the Proxy Statement is filed as an exhibit to the Form 10-K.

Item 12. Security Ownership of Certain Beneficial Owners and Management

The information regarding the security ownership of certain beneficial owners and management required by Item 403 of Regulation S-K is presented under the headings "Security Ownership of Certain Beneficial Owners and Management" in the Proxy Statement, which information is incorporated by reference herein. A copy of the Proxy Statement is filed as an exhibit to the Form 10-K.

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Item 13. Certain Relationships and Related Transactions

There is no information regarding certain relationships and related transactions required by Item 404 of Regulation S-K to be reported.

PART IV

Item 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K

- (a) 1 and 2. The financial statements and schedule listed in the accompanying index to consolidated financial statements are filed as part of this annual report.
 - (a) 3 and (c). The exhibits listed below are filed as part of this annual report.

Exhibit 2 -

*(a) Agreement and Plan of Merger, dated as of November 23, 1997, and as amended on January 25, 1998, among The Williams Companies, Inc., MAPCO Inc. and TML Acquisition Corp. (filed as Exhibit 2.1 to the Company's Registration Statement on Form S-4, filed January 27, 1998).

Exhibit 3 -

- *(a) Restated Certificate of Incorporation of Williams (filed as Exhibit 4(a) to Form 8-B Registration Statement, filed August 20, 1987).
- *(b) Certificate of Amendment of Restated Certificate of Incorporation, dated May 20, 1994 (filed as Exhibit 3(d) to Form 10-K for the fiscal year ended December 31, 1994).
- *(c) Certificate of Amendment of Restated Certificate of Incorporation dated May 16, 1997 (filed as Exhibit 4.3 to the Registration Statement on Form S-8 filed November 21, 1997).
 - (d) Certificate of Amendment of Restated Certificate of Incorporation, dated February 26, 1998.
- •(e) Certificate of Designation with respect to the \$3.50 Cumulative Convertible Preferred Stock (filed as Exhibit 3.1(c) to the Prospectus and Information Statement to Amendment No. 2 to the Registration Statement on Form S-4, filed March 30, 1995).
- *(f) Certificate of Increase of Authorized Number of Shares of Series A Junior Participating Preferred Stock (filed as Exhibit 3(f) to Form 10-K for the fiscal year ended December 31, 1995).
- (g) Certificate of Increase of Authorized Number of Shares of Series A Junior Participating Preferred Stock, dated December 31, 1997.
- *(h) Rights Agreement, dated as of February 6, 1996, between Williams and First Chicago Trust Company of New York (filed as Exhibit 4 to Williams Form 8-K, filed January 24, 1996).
- (i) By-laws of Williams, as amended (filed, as amended, as Exhibit 3 to Form 10-Q for the quarter ended September 30, 1996).

Exhibit 4 -

- *(a) Form of Senior Debt Indenture between the Company and Chase Manhattan Bank (formerly Chemical Bank), Trustee, relating to the 10%% Debentures, due 2020; the 9%% Debentures, due 2021; the 8%% Notes, due 1998; Medium-Term Notes (9.10%-9.31%), due 2001; the 7½% Notes, due 1999, and the 8%% Debentures, due 2012 (filed as Exhibit 4.1 to Form S-3 Registration Statement No. 33-33294, filed February 2, 1990).
- *(b) Form of Subordinated Debt Indenture between the Company and Chase Manhattan Bank (formerly Chemical Bank), Trustee, relating to 9.60% Quarterly Income Capital Securities, due 2025 (filed as Exhibit 4.2 to Form S-3 Registration Statement No. 33-60397, filed June 20, 1995).

- (c) U.S. \$1,000,000,000 Amended and Restated Credit Agreement, dated as of July 23, 1997, among Williams and certain of its subsidiaries and the banks named therein and Citibank, N.A., as agent.
- *(d) Form of Senior Debt Indenture between the Company and The First National Bank of Chicago, Trustee, relating to 6.50% Notes due 2002; 6.625% Notes due 2004; floating rate notes due 2000; 64% Notes due 2001; and 64% Mandatory Putable/Remarketable Securities due 2012 (filed as Exhibit 4.1 to Registration Statement on Form S-3 filed September 8, 1997).
- *(c) Form of Debenture representing \$360,000,000 principal amount of 6% Convertible Subordinated Debenture Due 2005 (filed as Exhibit 4.7 to the Registration Statement on Form S-8, filed August 30, 1996).
- *(f) Form of Warrant to purchase 11,305,720 shares of the Common Stock of the Company (filed as Exhibit 4.8 to the Registration Statement on Form S-8, filed August 30, 1996).

Exhibit 10(iii) - Compensatory Plans and Management Contracts

- *(a) The Williams Companies, Inc. Supplemental Retirement Plan, effective as of January 1, 1988 (filed as Exhibit 10(iii)(c) to Form 10-K for the year ended December 31, 1987).
- *(b) Form of Employment Agreement, dated January 1, 1990, between Williams and certain executive officers (filed as Exhibit 10(iii) (d) to Form 10-K for the year ended December 31, 1989).
- *(c) Form of The Williams Companies, Inc. Change in Control Protection Plan between Williams and employees (filed as Exhibit 10(iii) (e) to Form 10-K for the year ended December 31, 1989).
- *(d) The Williams Companies, Inc. 1985 Stock Option Plan (filed as Exhibit A to Williams' Proxy Statement, dated March 13, 1985).
- *(e) The Williams Companies, Inc. 1988 Stock Option Plan for Non-Employee Directors (filed as Exhibit A to Williams' Proxy Statement, dated March 14, 1988).
- (f) The Williams Companies, Inc. 1990 Stock Plan (filed as Exhibit A to Williams' Proxy Statement, dated March 12, 1990).
- *(g) The Williams Companies, Inc. Stock Plan for Non-Officer Employees (filed as Exhibit 10(iii) (g) to Form 10-K for the fiscal year ended December 31, 1995).
- *(h) The Williams Companies, Inc. 1996 Stock Plan (filed as Exhibit A to Williams' Proxy Statement, dated March 27, 1996).
- *(i) The Williams Companies, Inc 1996 Stock Plan for Non-Employee Directors (filed as Exhibit B to Williams' Proxy Statement, dated March 27, 1996).
- *(j) Indemnification Agreement, effective as of August 1, 1986, between Williams and members of the Board of Directors and certain officers of Williams (filed as Exhibit 10(iii)(e) to Form 10-K for the year ended December 31, 1986).
- Exhibit 11 Computation of Earnings Per Common and Common-equivalent Share.
- Exhibit 12 Computation of Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividend Requirements.
- Exhibit 20 Definitive Proxy Statement of Williams for 1998 (as filed with the Commission on March 27, 1998).
 - Exhibit 21 Subsidiaries of the registrant.
 - Exhibit 23 Consent of Independent Auditors.
 - Exhibit 24 Power of Attorney together with certified resolution.
 - Exhibit 27 Financial Data Schedule.

Exhibit 27.1 - Restated Financial Data Schedule for the year ended December 31, 1996.

Exhibit 27.2 - Restated Financial Data Schedule for the year ended December 31, 1995.

(b) Reports on Form 8-K.

On October 29, 1997, the Company filed a report on Form 8-K to report the results of the Company's debt tender offer.

On November 15, 1997, the Company filed a report on Form 8-K/A to report the results of the Company's debt tender offer.

On November 27, 1997, the Company filed a report on Form 8-K to report the Company's execution of an Agreement and Plan of Merger, dated November 23, 1997, among the Company, MAPCO Inc., and TML Acquisition Corp., providing for the Company to acquire MAPCO, Inc.

(d) The financial statements of partially-owned companies are not presented herein since none of them individually, or in the aggregate, constitute a significant subsidiary.

Each such exhibit has heretofore been filed with the Securities and Exchange Commission as part of the filing indicated and is incorporated herein by reference.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE WILLIAMS COMPANIES, INC. (Registrant)

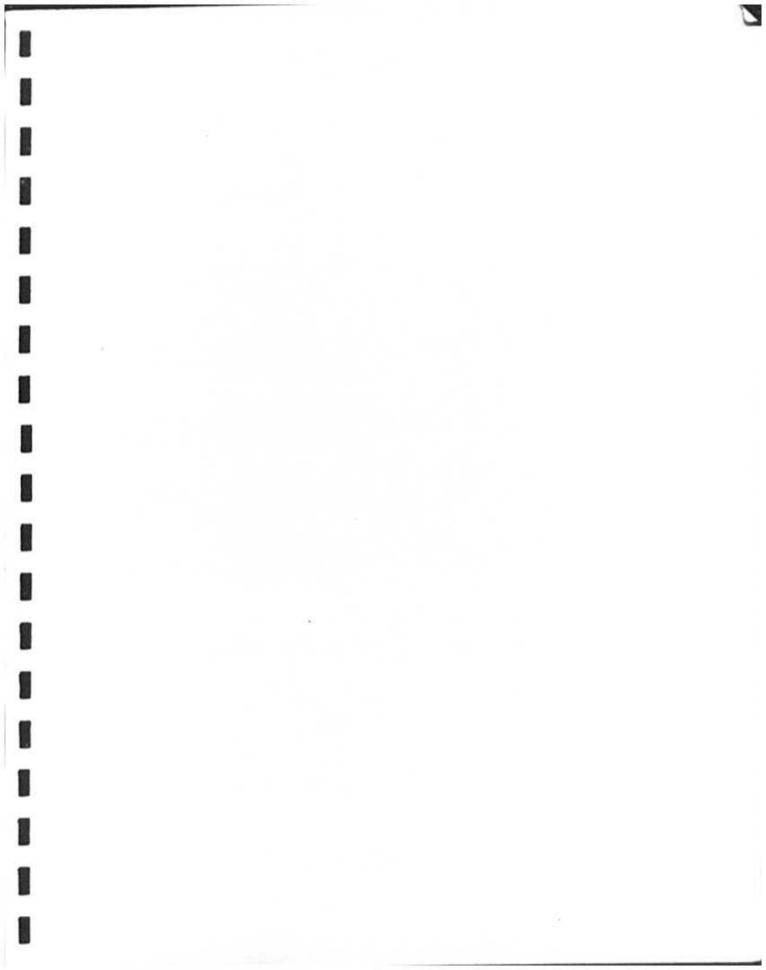
By: /s/ SHAWNA L. GEHRES

Shawna L. Gehres
Attorner-in-fact

Dated: March 30, 1998

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant in the capacities and on the dates indicated.

Signature	Title
/s/ KEITH E. BAILEY* Keith E. Bailey	Chairman of the Board, President, Chief Executive Officer (Principal Executive Officer) and
	Director
Jack D. McCarthy Jack D. McCarthy	Senior Vice President — Finance (Principal Financial Officer)
/s/ GARY R. BELITZ* Gary R. Belitz	Controller (Principal Accounting Officer)
/s/ GLENN A. COX*	Director
/s/ THOMAS H. CRUIKSHANK*	Director
Thomas H. Cruikshank /s/ WILLIAM E. GREEN*	Director
William E. Green	
/s/ PATRICIA L. HIGGINS* Patricia L. Higgins	Director
/s/ W.R. HOWELL* W. R. Howell	Director
/s/ ROBERT J. LAFORTUNE*	Director
Robert J. Lal'ortune /s/ JAMES C. LEWIS*	Director
James C. Lewis	
/s/ JACK A. MACALLISTER* Jack A. MacAllister	Director



DELWIN L. BOTHOF

President Williams Network Applications

Delwin L. Bothof (Del) leads multimedia applications across Williams' extensive fiber and satellite communications networks. This includes Williams Vyvx Services to broadcasters, advertisers, and production studios; Williams Global Access business television and audio- and video-conferencing; ChoiceSeat in-stadium sports entertainment network; Williams Learning Network interactive training and distance learning; and Williams Telemetry wireless telephony communications for the energy and utility industries.

From 1989-1997 he served as the first president of Vyvx, a leading international provider of integrated fiber-optic, satellite and teleport video transmission services.

With more than 25 years of experience, Bothof is well known in the telecommunications industry. Bothof joined Williams after holding a number of engineering, marketing and executive management positions for in the industry. He had served as partner and president of Atlanta-based Tritek Communications, Inc., a provider of integrated communication networks. Before that, he was director of corporate planning and development for BellSouth Corporation and later founded and served as president of BellSouth Ventures Company.

Bothof also served as president of Deka Corporation, a provider of advanced telecommunication systems, and vice president of marketing for Scientific-Atlanta, where he was responsible for the management of all worldwide sales and marketing, corporate strategies, joint ventures and acquisitions. He held numerous positions at the Delcon Division of Hewlett-Packard. Initially, he was engineering project manager responsible for the management and development of a product line which included software and hardware for data communication test instrumentation. He was later promoted to marketing manager and then to general manager.

Bothof holds a bachelor of science degree in Electrical Engineering from the University of Minnesota and a master of science degree in Electrical Engineering from Stanford University. He and his wife, Sally, reside in Tulsa.

HOWARD E. JANZEN

President & Chief Executive Officer Williams Communications

Howard E. Janzen is chief executive officer of Williams Communications, a subsidiary of Williams (NYSE: WMB). He has 18 years of experience in the telecommunications and energy industries, holding a variety of management positions within Williams.

Janzen began his career at Williams as project engineer for Williams Pipe Line in 1979, where he served in numerous management positions culminating as vice president of operations in 1987. In 1991, he became vice president of operations at Williams Natural Gas Company and became its senior vice president and general manager in 1993. He assumed the presidency of the WilTech Group in 1995 and was named chairman of Vyvx, Inc., an international provider of video transmission services via fiber optics, teleport uplinks and satellites. He became president and chief operating officer of Williams Communications in January 1997 and chief executive office in April 1997. Janzen also assumed the role of WilTel chairman when it merged with Nortel Communications Systems' customer premise sales and service organization in April 1997. WilTel is now known as Williams Communications Solutions.

Janzen earned bachelor of science and master of science degrees in Metallurgical Engineering from The Colorado School of Mines. He has also completed the Harvard Business School Program for Management Development.

Janzen lives in Tulsa with his wife, Cherine, and three children. He is vice chair of the Children's Medical Center Board of Trustees and serves on the Board of Trustees for the Hillcrest Healthcare System, where he is vice chair of the Physician Relations and Service Company. He serves on the Gilcrease Museum Board of Directors and is chairman for the National Annual Fund and President's Council for The Colorado School of Mines. He is also active in church related activities.

LAURA A. KENNY

President Williams Vyvx Services

Laura Kenny leads the Williams Vyvx Services unit, a leading international provider of integrated video, fiber-optic, satellite and teleport transmission services. Her responsibilities include strategic planning, marketing, sales, operations and administration for its worldwide presence with nearly 500 employees in 30 offices in the U.S., U.K., Singapore and Australia.

Kenny joined Williams in 1996 as vice president of Marketing and received sales responsibility in 1997. In December of 1997, Kenny assumed all management responsibility for Vyvx. In addition, she chairs Williams Communications' Customer Intimacy Initiative and co-chairs Williams' corporate-wide Chairman's Council on Workplace Diversity.

In more than 17 years as a leader in the telecommunications industry, Kenny has been involved in the development and implementation of strategic sales, marketing and management programs for domestic and international markets. Before joining Williams, Ms. Kenny served as an executive with AT&T, where she held numerous marketing and operations positions. She developed national marketing plans for AT&T Communication Services and the established a software development training institute in Singapore in collaboration with Bell Labs and the Singapore government.

Kenny earned a bachelor of arts degree from Lycoming College in 1978, and subsequently received paralegal certification at Adelphi University. She has attended the Master of Business Administration program at Seton Hall and completed executive development programs at the University of Michigan and Columbia University. She serves on the advisory board of The University of Tulsa College of Engineering. Kenny resides in Tulsa with her husband, Larry Gordon, and two children.

S. MILLER WILLIAMS

Senior Vice President, Corporate Development and Planning Williams Communications

S. Miller Williams is Senior Vice President of Corporate Development and Planning for Williams Communications, a division of Williams (NYSE: WMB).

He has more than 20 years of diversified business experience. Prior to joining Williams, he spent 10 years in real estate development and oil and gas syndications as president of Harbour Group. He joined Williams Telecommunications Systems in 1992 as vice president of corporate development. While there, he was responsible for exploring potential strategic partnerships, acquisitions, investments and projects for enhancing growth for Williams Communications Solutions (formerly WilTel). He has also served as assistant treasurer for Williams, manager of special projects for Williams Pipe Line, and director of international marketing for Agrico Chemical Company.

Williams earned a Master of Business Administration from The University of Tulsa and a Bachelor of Science in Business Administration from the University of North Carolina.

FRANK M. SEMPLE

General Manager, Williams Network Senior Vice President, Williams Communications

Frank Semple is general manager for the Williams Network as well as senior vice president for Williams Communications, a subsidiary of The Williams Companies, Inc. (Williams). He has nearly two decades of experience with Williams and brings to his office a track record of proven leadership skills within several Williams business units.

Prior to his current position, Semple served as senior vice president and chief information officer for Williams Communications. While serving as in numerous management positions with Williams Pipe Line, Semple implemented innovative technology at Williams Pipe Line that positioned that company as the industry leader in customer service and systems. He also held operations and marketing roles at Northwest Pipeline before joining Williams Natural Gas as senior vice president and general manager.

Semple received a bachelor's degree in mechanical engineering from the U.S. Naval Academy and has also completed the Harvard University program for management development.

He resides in Tulsa, Okla. with his wife and two children. Semple serves as a board member for the Campfire Boys & Girls organization in Tulsa.

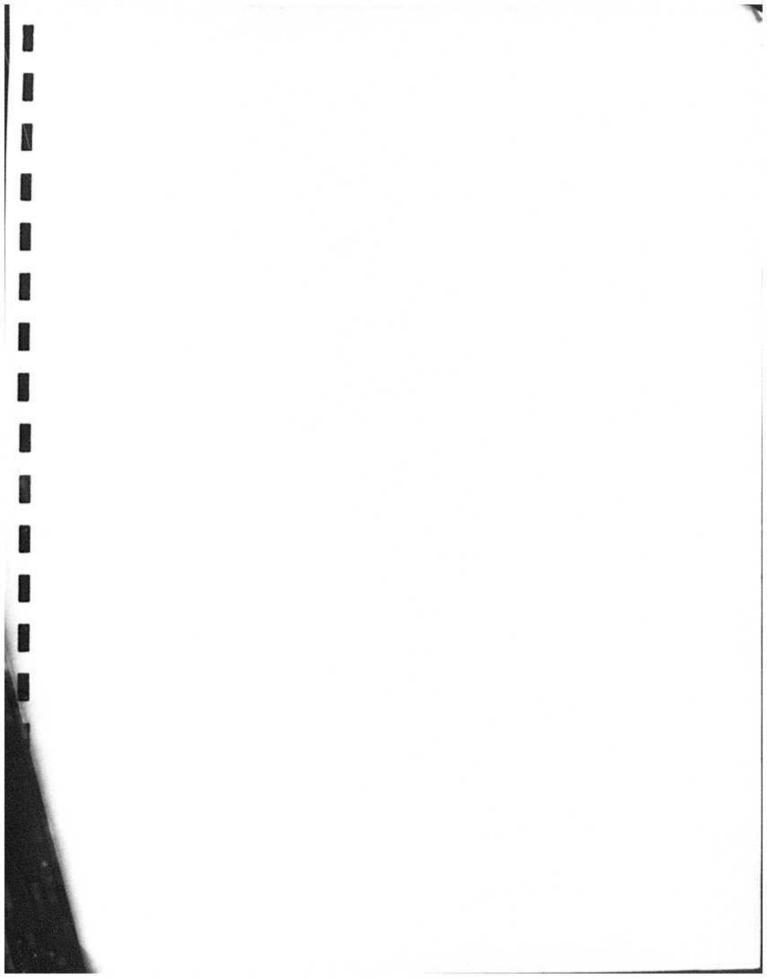
JOSEPH C. TURCOTTE

Vice President Williams Communications Network

Joseph C. Turcotte is vice president of Williams Communications Network and has 13 years of operations and engineering experience in the telecommunications and energy industries.

Turcotte was formerly vice president of Operations and Engineering for Vyvx. Prior to joining Vyvx in 1995, he worked for Williams Pipe Line in supervisory and managerial engineering positions, including director of Information Services.

Turcotte earned a bachelor of science degree in Mechanical Engineering from the University of Minnesota. He also completed the Harvard Professional Management Development Program.



FLORIDA PUBLIC SERVICE COMMISSION

Division of Communications Bureau of Service Evaluation

Williams Communications, Inc. d/b/a Vyvx, Inc.

Florida Tariff No. 1

INTEREXCHANGE TELECOMMUNICATIONS SERVICE

> Florida Public Service Commission Division of Communications Bureau of Service Evaluation 2540 Shumard Oak Boulevard Gunter Building Tallahassee, Florida 32399-0850

Florida Public Service Commission No. 1 Original Sheet 1

TITLE SHEET

FLORIDA TELECOMMUNICATIONS TARIFF

This tariff contains the descriptions, regulations, and rates applicable to the furnishing of service and facilities for telecommunications services provided by Williams Communications, Inc. d/b/a Vyvx, Inc. ("Vyvx" or the "Company"), with principal offices at 111 East 1st Street, Tulsa, Oklahoma 74103-2808. This tariff applies for services furnished within the state of Florida. This tariff is on file with the Florida Public Service Commission, and copies may be inspected, during normal business hours, at the Company's principal place of business.

Issued by: Mickey S. Moon

Director, Regulatory Affairs Williams Communications, Inc. One Williams Center

Florida Public Service Commission No. 1 Original Sheet 2

CHECK SHEET

(Page 1 of 1)

The title page and pages 1-67 inclusive of this Tariff are effective as of the date shown. Original and revised pages, as named below, comprise all changes from the original Tariff in effect on the date indicated. A copy of this tariff is on file at the Florida Public Service Commission. The Tariff may be viewed at the Company's principal office.

PAGE	REVISION	PAGE	REVISION	PAGE	REVISION
Title	Original	23	Original	46	Original
1	Original	24	Original	47	Original
2	Original	25	Original	48	Original
2	Original	26	Original	49	Original
4	Original	27	Original	50	Original
5	Original	28	Original	51	Original
6	Original	29	Original	52	Original
7	Original	30	Original	53	Original
7 8	Original	31	Original	54	Original
9	Original	32	Original	55	Original
10	Original	33	Original	56	Original
11	Original	34	Original	57	Original
12	Original	35	Original	58	Original
13	Original	36	Original	59	Original
14	Original	37	Original	60	Original
15	Original	38	Original	61	Original
16	Original	39	Original	62	Original
17	Original	40	Original	63	Original
18	Original	41	Original	64	Original
19	Original	42	Original	65	Original
20	Original	43	Original	66	Original
21	Original	44	Original	67	Original
22	Original	45	Original		

^{*}New or Revised Pages

Issued	: /	/98
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Effective:____

Issued by: Mickey S. Moon

Director, Regulatory Affairs Williams Communications, Inc. One Williams Center

Florida Public Service Commission No. 1 Original Sheet 3

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Director, Regulatory Affairs Williams Communications, Inc. One Williams Center

Florida Public Service Commission No. 1 Original Sheet 5

APPLICABILITY

This Tariff contains the Service offerings, rates, terms and conditions applicable to the furnishing of private line Services used for transmission and video communications by Vyvx This tariff applies only to Services subject to regulation by the Florida Public Service Commission. This Tariff does not apply to the within described Services that are provided by Vyvx: (a) as interstate or international services; or (b) pursuant to other Vyvx tariffs unless specifically stated therein.

Issued by: Mickey S. Moon

Director, Regulatory Affairs Williams Communications, Inc.

Florida Public Service Commission No. 1 Original Sheet 6

CONCURRING, CONNECTING AND OTHER PARTICIPATING CARRIERS

CONCURRING CARRIERS:

No Concurring Carriers

CONNECTING CARRIERS:

No Connecting Carriers

OTHER PARTICIPATING CARRIERS:

No Participating Carriers

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Director, Regulatory Affairs Williams Communications, Inc.

EXPLANATION OF SYMBOLS

The following are the only symbols used for the purposes indicated below:

- (D) Delete or Discontinue
- (!) Change Resulting in an Increase to a Customer's Bill
- (M) Moved From Another Tariff Location
- (N) New
- (R) Change Resulting in a Reduction to a Customer's Bill
- (T) Change in Text or Regulation but No Change in Rate or Charge

Issued: _/_/98 Effective:_____

Issued by: Mickey S. Moon

Director, Regulatory Affairs Williams Communications, Inc.

TARIFF FORMAT SHEETS

- A. Sheet Numbering -- Sheet numbers appear in the upper right corner of the page. Sheets are numbered sequentially. However, new sheets are occasionally added to the tariff. When a new sheet is added between sheets already in effect, a decimal is added. For example, a new sheet added between sheets 14 and 15 would be 14.1.
- B. Sheet Revision Numbers -- Revision numbers also appear in the upper right corner of each page. These numbers are used to determine the most current sheet version on file with the FPSC. For example, the 4th revised Sheet 14 cancels the 3rd revised Sheet 14. Because of various suspension periods, deferrals, etc., the FPSC follows in their tariff approval process, the most current sheet number on file with the Commission is not always the tariff page in effect. Consult the Check Sheet for the sheet currently in effect.
- C. Section Numbering Sequence There are nine levels of section coding. Each level of coding is subservient to its next higher level:

2. 2.1. 2.1.1. 2.1.1.A. 2.1.1.A.1. 2.1.1.A.1.(a). 2.1.1.A.1.(a).1. 2.1.1.A.1.(a).1.(i). 2.1.1.A.1.(a).1.(i).

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Florida Public Service Commission No. 1 Original Sheet 9

TARIFF FORMAT SHEETS

D. Check Sheets - When a tariff filing is made with the FPSC, an updated check sheet accompanies the tariff filing. The check sheet lists the sheets contained in the tariff, with a cross reference to the current revision number. When new pages are added, the check sheet is changed to reflect the revision. All revisions made in a given filing are designated by an asterisk (*). There will be no other symbols used on this page if these are the only changes made to it (i.e., the format, etc. remains the same, just revised revision levels on some pages). The tariff user should refer to the latest check sheet to find out if a particular sheet is the most current on file with the FPSC.

Issued by: Mickey S. Moon

Director, Regulatory Affairs Williams Communications, Inc.

For the purposes of this Tariff, the following definitions shall apply:

Acceptance/Accepted

The concurrence by Customer and Company that, following Installation, a Service meets the relevant Technical Standards. In any event, once Customer commences using the Service, Acceptance shall be deemed to have occurred.

Access Service Request (ASR)

An order placed with a First-Mile/Last-Mile Service Provider to provide First-Mile and/or Last-Mile Service.

Analog Access

An analog First-Mile or Last-Mile Circuit used to transmit television signals between points.

Ancillary Charges

Charges for supplementary Services as set forth in Sections 4 and 5 which may consist of both nonrecurring and monthly recurring charges.

Approximate-End/Approx-End

At the time of making a request for a Reservation Confirmation and subject to such Service being Available in the Company's sole discretion, a Customer may reserve, on a right of first refusal basis, the relevant Circuit past the Ending Transmission Time as follows: (i) fifteen (15) minutes, if the original reservation is for less than one (1) hour, or (ii) thirty (30) minutes, if the original reservation is for one hour or longer (collectively the "Approx-End Period").

Authorized User

A person, firm, corporation or other entity (including Customer) that either is authorized by the Customer to act as Customer in matters of ordering, changing or canceling Service or is placed in a position by the Customer, either through acts or omissions, to act as Customer in such matters. Such actions by an Authorized User shall be binding on Customer and shall subject Customer to any associated charges.

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Director, Regulatory Affairs Williams Communications, Inc. One Williams Center Tulsa, Oklahoma 74172

Available/Availability

Condition in which Company has on its network a Circuit between specific POPs (as may be requested by Customer) and such Circuit and the related Customer First-Mile and Last-Mile Circuits are not committed to other parties or other Customers and are accessible for Service to Customer, as determined by the Company, in its sole discretion.

Beginning Transmission Time

The date and time specified on a Reservation Confirmation or pursuant to an Early Acceptance, as the case may be, agreed to by Company, as the beginning date and time for transmission of the relevant Occasional Service.

Bill Date/Billing Date

The date on which billing information is compiled and sent to the Customer.

Cancellation

A Customer initiated request to discontinue processing a Service Order for Dedicated Service or a Reservation Confirmation for Occasional Service or to discontinue Service, either in part or in its entirety. Cancellation charges shall be assessed as set forth in Sections 2.4, 4.7 and 5.4.

Channel(s) or Circuit(s)

A dedicated communications path between two or more points.

Commission

The Florida Public Service Commission or any successor agency.

Company

Williams Communications, Inc. d/b/a Vyvx, Inc.

Confirmed Reservation

A request for service which has been confirmed by the Company through the issuance of a Reservation Confirmation.

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Director, Regulatory

Director, Regulatory Affairs Williams Communications, Inc. One Williams Center

Contribution Quality Television Transmission

A television transmission that is of a quality that permits post-processing of the signal and that conforms to the relevant Technical Standards.

Cross Connect

Electrical connection within a POP or Hub of two Circuits in order to complete connectivity between such Circuits, such as, connecting IXC with First-Mile/Last-Mile Circuits, connecting two (2) IXC Circuits, or connecting two (2) First-Mile/Last-Mile Circuits.

Customer

The person, firm, corporation, governmental unit or other entity (including the successors and assigns of such entities and their Authorized Users) which orders Service -- either for its own use or for its use as a resale carrier -- and which is responsible for the payment of charges and for compliance with Company Tariff regulations. A Customer is considered to be an account for billing purposes.

Customer Premise/Customer's Premise

Locations designated by a Customer or Authorized User (regardless as to whether the designated premises are controlled or operated by such Customer) where Service is originated/terminated for Customer's own needs or for the use of third parties.

Dedicated Access

Dedicated First-Mile or Last-Mile Circuits between the Customer's Premises and the Company's POP for origination or termination of Service.

Dedicated Service

Interexchange Service provided from POP to POP by Company on a twenty-four hour a day basis for a Term.

Digital Access

A digital First-Mile or Last-Mile Circuit used to transmit television signals between points.

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Diversity

Customer-designated routing agreed to by an authorized representative of Company which indicates a Customer designated departure from a Company Primary Route. The provision of Diversity with respect to Circuits may entail Circuits routed on physically separate facilities on a geographic or systems basis (to the extent possible, i.e., 100% route Diversity on a POP-to-POP or Customer Premise-to-Customer Premise basis is not guaranteed) between the same city pair where the facilities required to provide the relevant Circuits are determined by Company to be Available. Diversity arrangements shall be developed on an individual case basis, and each Circuit in such arrangement shall be charged for separately.

Domestic

Services pertaining to Origination and Destination POPs within the contiguous United States.

Drop-Off(s)

A POP(s), specified by Customer and agreed to by Company where, in addition to the final destination point, Company shall deliver the Service.

Due Date

The date on which payment is due as indicated on Company's invoice to Customer. The Due Date shall be no earlier than thirty (30) days after the date the invoice is issued.

Duration/Reservation Duration

The greater of (i) the time between the Beginning Transmission Time and the Ending Transmission Time as set forth in a Reservation Confirmation, or (ii) the actual transmission time of Occasional Service relevant to such Reservation Confirmation inclusive of Early Acceptance time, Extension time, and Overage, if any.

Early Acceptance

The advancement to an earlier time, at Customer's request and subject to such Service being Available in the Company's sole discretion, of the Beginning Transmission Time made after a Reservation Confirmation has been sent to Customer. The Ending Transmission Time shall not be changed.

Ending Transmission Time

The date and time specified on a Reservation Confirmation or pursuant to an Extension and agreed to by Company as the ending date and time for transmission of the relevant Occasional Service.

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Event

A reservation which consists of a price or charge associated with the aggregate number of hours of services provided in lieu of an hourly charge.

Exemption Certificate

A written Customer designation which certifies that its dedicated facility should be exempted from the monthly special access surcharge because the Service:

- terminates on a device incapable of connecting Company's network with the local exchange network; or
- (b) is associated with a switched access service that is subject to carrier common line charges; or
- (c) constitutes a private line facility used for Telex Service or radio or television transmissions; or,
- (d) is an open-end termination in a local exchange carrier's switch of an FX line; or
- (e) is a termination that could not make use of a local exchange carrier's common lines.

Extension

The extension or prolonging of an Ending Transmission Time, at Customer's request and subject to such Service being Available in the Company's sole discretion, made after a Reservation Confirmation has been sent and before such transmission has commenced.

Expedite

A Service Order processed at the request of the Customer in a time period shorter than the Company standard Service interval or an ASR processed by a First-Mile or Last-Mile Service Provider in response to a Customer request in a time period shorter than such First-Mile or Last-mile Service Provider's standard interval.

FCC

Federal Communications Commission.

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FCC #1

The Company's tariff for interstate services.

FCC #4

The Company's tariff for international services.

First-Mile Service

The origination portion of the Service between a Customer Premise and a Company POP.

First-Mile and Last-Mile Service Provider

An entity providing First-Mile and/or Last-Mile Service.

Hub

A facility or location where multiple First-Mile or Last-Mile circuits exist for the purpose of crossconnecting to other First-Mile or Last-Mile circuits within the same facility.

Hub Circuit

A First-Mile or Last-Mile circuit interconnecting a Customer or Company to a Hub.

Hub Reservation

A reservation placed with a Hub for cross-connection of Hub circuits.

Individual Case Basis (ICB)

Determinations involving situations where nonstandard arrangements are required to satisfy specialized needs. The nature of such Service requirements makes it difficult or impossible to establish general Tariff provisions for such circumstances. When it becomes possible to determine specific terms and conditions for such offerings, they shall be offered pursuant to such terms and conditions when set forth in writing and subscribed to by authorized representatives of Customer and Company.

Inquiry Reservation

A request for service which has not been confirmed.

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Installation

Establishment of Service.

Interexchange Service ("IXC")

Service provided between POPs to Customer by Company as described in this Tariff.

Interruption

A condition whereby the Service or a portion thereof is inoperative, beginning at the time of notice by the Customer to the TOC that such Service is inoperative and ending at the time of restoration.

Last-Mile Service

The terminating portion of the Service between a Company POP and a Customer Premise.

Local Digital Switching

Reconfiguration of a digital IXC Circuit Cross Connect within a Company POP.

Local Switch

An interconnection of a First-Mile and Last-Mile circuit.

Mbps

Megabits per second.

N/A

Not applicable.

N/C

No charge.

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Non-Preemptible

A level of Service in which the provision of Service is given priority over Preemptible Service as set forth in Section 2.18.

Non-Prime Occasional Service

Occasional Service offered under the terms defined in Section 5 of this Tariff that applies a reduced rate to the Interexchange Service portion of Vyvx'x Standard Occasional Interexchange Service between preset hours.

Occasional Service

Interexchange Service provided from POP to POP by Company for the Duration. Such Service is billed in arrears.

One-Way

Service provided from Point-to-Point in which the transmission of signals is in one direction only.

Overage

At the request of Customer, a transmission may be extended beyond the Ending Transmission Time or Approx-End Period, as the case may be, after the relevant transmission has commenced subject to such Service being Available in the Company's sole discretion.

Payment Method

The manner in which the Customer is authorized by the Company to pay charges for Service.

Physical Change

The modification of an existing Circuit, First-Mile/Last-Mile Circuit, Dedicated Access Channel or port, at the request of the Customer, requiring some physical change or retermination.

Point-to-Point

Service provided between two POP(s)/Customer Premise(s).

SECTION 1 -- TECHNICAL TERMS AND ABBREVIATIONS (Cont'd)

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Point to Multi-Point

Service provided One-Way from one POP/Customer Premise to multiple POPs/Customer Premise, as the case may be.

Point of Presence (POP)

A Company designated location where a facility is maintained for the purpose of providing access to Interexchange Service where Available.

Preemptible

A level of Service in which Non-preemptible Service is given priority in the event of an Interruption as set forth in Section 2.18.

Primary Route

The route along which Service is transmitted which, in the absence of a Diversity arrangement, would be solely determined and used by Company in the provision of Service.

Redundant Routing

A second IXC path between the same origination and destination POPs of Point-to-Point Service.

Requested Service Date

The date requested by the Customer for commencement of Dedicated Service and agreed to by Company.

Reservation Confirmation

Standard Company order confirmation form(s) for Occasional Service, in effect from time to time, sent to Customer which in total includes pertinent billing, technical and other descriptive information which shall enable Company to provide Service.

Restore/Restored

To make Service operative following an Interruption by repair, reassignment, re-routing, substitution of component parts, or otherwise, as determined by the Company or carrier(s) involved.

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Secondary Drop-Off Service\PGAD

Delivery on a Preemptible One-Way IXC Occasional Service basis to one POP of the transmission relevant to an independent Reservation Confirmation for a Point-to-Point or Point to Multi-Point Occasional Service transmission for all or part of such transmission. This Service may be used to provide for separate ordering and billing for a Customer receiving another Customer's transmission provided such reception is authorized by such other Customer.

Service

Any or all service(s) provided to or obtained by Customer, any Authorized User or third party from Company which is described in this Tariff as modified from time to time.

Service Order

Standard Company order form(s), in effect from time to time, or Customer's forms accepted in writing by an authorized representative of Company for Dedicated Service which in total includes pertinent billing, technical and other descriptive information which shall enable Company to provide Service.

Special Promotional Offerings

Authorized trial offerings, discounts, or modifications of Company's regular Service offerings, which may, from time to time, be offered by Company to Customers for a particular Service. Such offerings may be limited to certain dates, times, and locations.

Start of Service

The Requested Service Date or Beginning Transmission Time, as the case may be, or the date or time Service first becomes available in accordance with the relevant Technical Standards, whichever is later.

Tariff

Tariff Commission No. 1, and effective revisions thereto filed by the Company with the Commission.

Technical Standards

Technical Standards for Interexchange Service are governed by the relevant Technical Standards described in Section 3.

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SECTION 1 -- TECHNICAL TERMS AND ABBREVIATIONS (Cont'd)

Television Operation Center (TOC)

Company's designated facility for authorized reporting of Service Interruption.

Term

The period selected by the Customer, agreed to by Company and stated on the relevant Service Order during which Company shall provide and Customer shall accept and pay for the Service described therein.

Two-Way

Service provided by means of two simplex Circuits transmitting in opposite directions between the same two points which may not be synchronous.

Vyvx

Vyvx, Inc. (the Company).

Vyvx Affiliates

A business organization or entity which controls, is controlled by, or is under common control with the Company.

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SECTION 2 -- RULES AND REGULATIONS

- 2.1. Description and Limitations of Services
 - 2.1.1. Any member of the general public (including any natural person or legally organized entity such as a corporation, partnership, or governmental body) is entitled to obtain Service under this Tariff, provided that Company reserves the right to deny Service: (i) to any Customer that, in Company's reasonable opinion, presents an undue risk of nonpayment and refuses to comply with the deposit requirements set forth in Section 2.7.5, (ii) in circumstances in which Company has reason to believe that the use of the Service would violate the provisions of this Tariff or any applicable law or if any applicable law restricts or prohibits provision of the Service, or (iii) if, in Company's sole opinion, insufficient facilities are Available to provide the Service.
 - 2.1.2 Customers reselling or rebilling Service to which this Tariff is applicable must have a Certificate of Public Convenience and Necessity as an interexchange carrier from the Florida Public Service Commission.
 - 2.1.3. The applicability of this Tariff shall be as set forth in Applicability (page five).
 - 2.1.4. Circuits for First-Mile/Last-Mile Service may be provided and billed by a First-Mile and Last-Mile Service Provider that is a local exchange company (LEC). First-Mile/Last-Mile Service may be purchased from carriers other than the LEC only in accordance with Florida Public Service Commission rules unless such service is jurisdictionally interstate. Charges for the First-Mile/Last-Mile Service are available from the relevant First-Mile or Last-Mile Service Provider.
 - 2.1.5. Company, when acting at the Customer's request and/or as Customer's authorized agent, shall make reasonable efforts to arrange for special Service requirements such as Diversity, if it is legally able to do so. Due to the specialized nature of such an arrangement, however, such Service may not be available under this Tariff and Company shall have no obligation to make any tariff filings required to provide such Service.
 - 2.1.6. In addition to the cancellation procedures contained in Section 2.5, the Company may discontinue service upon reasonable notice under the circumstances to the Customer if:
 - 2.1.6.A. the Customer is using the Service in violation of this Tariff; or
 - 2.1.6.B. the Customer is using the Service in violation of any applicable law or regulation.
 - 2.1.7. Dedicated Service begins on the Start of Service date and is provided through the Term relevant to the Service in question. Customer shall pay for such Service for the Term.
 - 2.1.8. At Company's sole discretion, following the expiration of the Term relevant to a Dedicated Service, Service shall continue to be provided in accordance with this Tariff and at the then current month Term charge set forth in Section 4.4 in this Tariff relevant to the Service in question.

- 2.1. Description and Limitations of Services (Cont'd)
 - Occasional Service is provided for the Duration. Customer shall pay for such Service for the Duration.
 - 2.1.10. Eastern Time shall be used in scheduling Occasional Service transmissions, and such time shall be determined according to WWV Time as established by the WWV Radio Station located in Fort Collins, Co. Any Occasional Service scheduled for completion on the hour or half hour shall terminate one (1) minute prior to such time (except when Overage occurs), and such Service shall be deemed fully completed.
 - 2.1.11. Following the expiration of the Ending Transmission Time, Company shall use reasonable efforts, provided Service is Available (as determined solely by Company) and uncommitted, to provide Overage upon the Customer's request at the charges set forth in Section 5.4.2. Overage is provided in fifteen (15) minute increments subject to such Service being Available as determined by the Company, in its sole discretion.
 - 2.1.12. Except as otherwise provided in this Tariff or as specified in writing by the party entitled to receive notice, notices between Customer and Company shall be given in writing to the persons whose names and business addresses appear on the relevant Reservation Confirmation or Service Order and the effective date of any notice shall be the date of delivery of such notice, not the date of mailing. By written notice, Company or Customer may change the party to receive notice and/or the address to which such notice is to be delivered. In the event no Customer or Company address is provided in the relevant Reservation Confirmation of Service Order, notice shall be given to the last known business address of Customer or Company, as the case may be.
 - 2.1.13. At Vyvx's option, any analog/digital conversion needed to make the Customer's signal compatible with the Vyvx network may take place at either the POP or at Customer's premises.

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- 2.1. Description and Limitations of Services (Cont'd)
 - 2.1.14. Hub Reservation Management Service will be provided on a full-time basis from the effective date of the Customer's signed agreement for service through the Cancellation date of Hub Reservation Management Service by the Customer or Company. All Hub reservations for Company-bound IXC traffic reserved by Hub Reservation Management Service Customers will be managed by the Company on behalf of the Customer.

Company will not be responsible for diagnosing, troubleshooting or providing Allowance for any Interruptions occurring over Hub circuits to Customers who do not have an active Hub Reservation Management Service Agreement with the Company.

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SECTION 2 -- RULES AND REGULATIONS (Cont'd)

- 2.2. Other Terms and Conditions
 - 2.2.1. The name(s) of the Customer(s) desiring to obtain the Service must be set forth in the Reservation Confirmation or Service Order.
 - 2.2.2. The Customer shall operate any Company provided equipment in accordance with instructions of the Company or the Company's agent or designee. Failure to do so shall void any Company liability for Interruption of Service and may make Customer responsible for damage to equipment pursuant to Section 2.2.3 below.
 - 2.2.3. Customer shall return to the Company all Company-provided equipment within five (5) days of termination of the Service for which the equipment was used. Said equipment shall be in the same condition as when delivered to Customer, normal wear and tear excepted. Customer shall reimburse the Company, upon demand, for any costs incurred by the Company (e.g., the cost of the equipment) due to Customer's failure to comply with this section.
 - 2.2.4. A Customer shall not use any service mark or trademark of the Company or refer to the Company in connection with any product, equipment, promotion, or publication of the Customer without prior written approval of the Company.
 - 2.2.5. In the event suit is brought or an attorney is retained by the Company to enforce the terms of this Tariff, the Company shall be entitled to recover, in addition to any other remedy, reimbursement for reasonable attorneys' fees, court costs, costs of investigation and other related expenses incurred in connection therewith.
 - 2.2.6. Any legal action or proceeding with respect to the collection of charges due under this Tariff may be brought in the Courts of the State of Oklahoma in and for the County of Tulsa or the United States of America for the Northern District of Oklahoma. By Customer's obtaining Service pursuant to this Tariff, both Customer and Company shall be deemed to have submitted to such jurisdiction, thereby expressly waiving whatever rights may correspond to either of them by reason of their present or future domicile.
 - 2.2.7. The provision of Service shall not create a partnership or joint venture between the Company and Customer, nor result in joint service offerings to their respective customers.

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- 2.2. Other Terms and Conditions (Cont'd)
 - 2.2.8. The discount level, if any, applicable to a Customer for a particular Service or Services shall be the rate or volume discount level in effect at the beginning of the monthly billing period applicable to the Customer for the particular Service or Services.
 - 2.2.9. Dedicated Service requested by Customer and to be provided pursuant to this Tariff shall be requested on Service Orders. Occasional Service requested by Customer and to be provided pursuant to this Tariff may be ordered telephonically, by facsimile transmission, or any other reasonable method sent to Company's Customer Service Group and shall be confirmed by a Reservation Confirmation whereby Customer shall receive written confirmation from Company of Occasional Service it has requested. The business records of Company shall control as to the contents of the Service Order(s) (or other agreed to Customer form(s)) and/or Reservation Confirmation(s). When Customer places a Service Order for Dedicated Service or places an order for Occasional Service, the Customer must provide the Company with the Customer's name and address for billing purposes and a contact name and phone number. Customer must also provide the Company with the contact name, telephone number, and address at each of the premises where Service is to be installed. Each Service Order and Reservation Confirmation shall reference this Tariff. When the Service Order is accepted in writing by Company, or a Reservation Confirmation is sent to Customer and is not disputed by Customer within the earlier of: (A) twenty-fout (24) hours from the time sent to Customer or (B) the Beginning Transmission Time, the relevant Service Order or Reservation Confirmation shall control the final operative obligations between Company and Customer regarding the Services described therein to the extent that it specifies the type of Service, quantity of Circuits, originating and terminating cities, Requested Service Date or Beginning/Ending Transmission Time, Team or Duration and other information necessary for Company to provide the Service to Customer.
 - 2.2.10. Hub Reservation Management Service shall be provided pursuant to a signed Hub Reservation Management Service Agreement and as defined herein commencing one (1) business day after Company receives a signed Hub Reservation Management Service Agreement until one (1) business day after Company receives a written cancellation request for Hub Reservation Management Service, or Company cancels service. Customers may provide to the Company telephone notice of Customer's intent to accept Hub Reservation Management Service, subject to Company's acceptance. Service will thus be effective within 24 hours of such notice and will be provided on the basis that a signed Hub Reservation Management Service Agreement is delivered to the Company within ten (10) business days by the Customer.

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- 2.2. Other Terms and Conditions (Cont'd)
 - 2.2.11. Any other items and conditions that are typed, printed or otherwise included in any Service Order, Reservation Confirmation, or other like form of Customer consent shall be deemed to be solely for the convenience of the parties. No action by Company, including, without limitation, provision of Service to Customer pursuant to such Service Order, Reservation Confirmation, or other like form of Customer consent shall be construed as binding or estopping Company with respect to such term or condition, unless such Service Order, Reservation Confirmation, or other like Customer consent form containing said specific term or condition has been signed by an authorized representative of Company and Customer. Company shall have no obligation except those as set forth in this Tariff or contained in Service Orders, Reservation Confirmations, or other like Customer consent forms and all other representations or agreements, oral or written, shall be of no effect. In the event any provisions set forth in Service Orders (or other agreed to like forms of Customer consent) or Reservation Confirmations conflict with the provisions set forth in this Tariff, the provisions set forth in this Tariff shall prevail.
 - 2.2.12. Unless subject to a Hub Reservation Management Service Agreement, the terms of which services or arrangements shall control, charges for First-Mile and Last-Mile Service procured by Company on behalf of Customer shall be subject to adjustment at such times as Company shall determine, not to exceed the then prevailing charges of the relevant First-Mile or Last-Mile Service Provider as would otherwise be paid directly by Customer for the relevant First-Mile or Last Mile Service, plus the administrative surcharge set forth in Section 2.19.
 - 2.2.13. Upon the scheduled expiration of a Term for Dedicated Service, Service shall automatically be extended subject to written notice of termination by either Company or Customer; such termination shall be effective as of a date not less than thirty (30) days after delivery of said notice to the other party. The charges for Service during any such extension shall not exceed the then current month Term charge set forth in this Tariff and applicable to such Dedicated Service.
 - 2.2.14. Following the expiration of the Ending Transmission Time for Occasional Service, Company shall use reasonable efforts, provided Service is Available (as determined solely by the Company) and uncommitted, to provide Overage upon the Customer's request subject to the relevant charges therefore set forth in this Tariff.

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- 2.2. Other Terms and Conditions (Cont'd)
 - 2.2.15. Customer shall be responsible for procuring any necessary consents to use a third party's First-Mile or Last-Mile Circuit. If a conflict occurs with respect to the use of any First-Mile or Last-Mile Circuit, the party that leases or for whom Company has procured such First-Mile or Last-Mile Circuit shall have priority of use. If Customer is subject to a Reservation Confirmation and subsequently cannot use a relevant First-Mile or Last-Mile Circuit due to the priority of use by a third party, Customer shall be liable for the relevant Cancellation charges set forth in Sections 2.4, 4.7 and 5.4.

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2.3. Liability

- 2.3.1 Except as otherwise specifically provided for in this Tariff, the Company and/or Vyvx Affiliates shall not be liable to Customer or any other person, firm or entity for any failure of performance hereunder if such failure is due to any cause or causes beyond the reasonable control of the Company. Such causes shall include, without limitation, acts of God, fire, explosion, vandalism, sabotage, cable cut, storm or other similar occurrence, any law, order, regulation, direction, action or request of the United States government or of any other government or of any civil or military authority, national emergencies, insurrections, riots, wars, condemnation, strikes, lockouts or work stoppages or other labor difficulties, supplier failures, shortages, breaches or delays, or preemption of existing Services to restore Service in compliance with Part 64, Subpart D, Appendix A, of the FCC's Rules and Regulations or other applicable laws, regulations, or orders.
- 2.3.2. The Company is not liable for any act or omission of any other company or companies (including Vyvx Affiliates) furnishing a portion of the Service or facilities, equipment, or services associated with such Service.
- 2.3.3. The Company and Vyvx Affiliates shall be indemnified and held harmless against and from any court, administrative or agency action, suit or similar proceeding brought against Company and/or Vyvx Affiliates for:
 - 2.3.3.A. claims arising out of or related to the contents transmitted via the Services (whether over the Company network or First-Mile and Last-Mile Circuits) including, but not limited to, claims, actual or alleged, relating to any violation of copyright law, export control laws, failure to procure necessary authorizations, clearances or consents, failure to meet governmental or other technical broadcast standards, or claims that such transmission contents are libelous, slanderous, an invasion of privacy, pornographic, or otherwise unauthorized or illegal;
 - 2.3.3.B. patent infringement claims arising from combining or connecting the Service with equipment and systems of the Customer or Authorized Users;
 - 2.3.3.C. all other claims arising out of any act or omission of the Customer or Authorized Users in connection with any Service provided by the Company;

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- 2.3. Liability (Cont'd)
 - 2.3.3.D. defacement of, or damage to, the premises of Customer and Authorized Users resulting from the installation, and/or removal of facilities or the attachment of instruments, equipment and associated wiring on or from the Customer's Premises. No agents or employees of other participating carriers shall be deemed to be agents or employees of the Company; and
 - 2.3.3.E. claims arising out of the use of Services or associated equipment in an unsafe manner (such as use in an explosive atmosphere) or the negligent or willful act of any person other than the Company, its agents, or employees.
 - 2.3.4. The Customer is responsible for taking all necessary legal steps for interconnecting the Customer provided terminal equipment with the Company facilities. The Customer shall ensure that the signals emitted into the Company's network do not damage Company equipment, injure personnel, degrade Service to other Customers, or otherwise cause a violation of this Tariff or any applicable law or regulation. The Customer is responsible for securing all licenses, permits, rights-of-way, and other arrangements necessary for such interconnection. In addition, the Customer shall comply with applicable First-Mile or Last Mile Service Provider's signal power limitations.
 - 2.3.5. The Company may rely on First-Mile and Last-Mile Service Providers for the performance of other services such as First-Mile and Last-Mile Service. Upon Customer request and execution and delivery of appropriate authorizing documents, the Company may act as agent for Customer in obtaining such First-Mile and Last-Mile Service. Customer's liability for charges hereunder shall not be reduced by untimely installation or non-operation of First-Mile or Last-Mile Service or Customer provided facilities and equipment.
 - 2.3.6. The Customer indemnifies and holds the Company and Vyvx Affiliates harmless from any and all loss, claims, demands, suits, or other action, or any liability whatsoever, whether suffered, made, instituted or asserted by the Customer or by any other party or persons, for any personal injury to, or death of, any person or persons, and for any loss, damage or destruction of any property, whether owned by the Customer or others, caused or claimed to have been caused directly or indirectly by the installation, operation, failure to operate, maintenance, removal, presence, condition, location or use of Service or equipment and facilities of Company associated with the Service, unless such installation, operation, failure to operate, maintenance, condition, location or use is the direct result of the Company's knowing and willful misconduct.

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- 2.3. Liability (Cont'd)
- THE COMPANY SHALL NOT BE LIABLE TO THE CUSTOMER OR ANY OTHER PERSON, FIRM OR ENTITY IN ANY RESPECT WHATSOEVER AS A RESULT OF MISTAKES, ACCIDENTS, ERRORS, OMISSIONS, INTERRUPTIONS, DELAYS, OR DEFECTS IN SERVICE (COLLECTIVELY "DEFECTS" OR "DEFECTIVE SERVICE"). DEFECTS CAUSED BY OR CONTRIBUTED TO, DIRECTLY OR INDIRECTLY, BY ACT OR OMISSION OF CUSTOMER (INCLUDING AUTHORIZED USERS) OR CUSTOMER'S CUSTOMERS, AFFILIATES, AGENTS, REPRESENTATIVES, INVITEES, LICENSES, SUCCESSORS OR ASSIGNS OR WHICH ARISE FROM OR ARE CAUSED BY THE USE OF FACILITIES OR EQUIPMENT OF CUSTOMER OR RELATED PARTIES SHALL NOT RESULT IN THE IMPOSITION OF ANY LIABILITY WHATSOEVER UPON THE 'COMPANY, AND CUSTOMER SHALL PAY TO THE COMPANY ANY REASONABLE COSTS, EXPENSES, DAMAGES, FÉES OR PENALTIES INCURRED BY THE COMPANY AS A RESULT THEREOF, INCLUDING COSTS OF FIRST-MILE AND LAST-MILE SERVICE PROVIDERS' LABOR AND MATERIALS. IN ADDITION, ALL OR A PORTION OF THE SERVICE MAY BE PROVIDED OVER FACILITIES OF THIRD PARTIES, AND THE COMPANY SHALL NOT BE LIABLE TO CUSTOMER OR ANY OTHER PERSON, FIRM OR ENTITY IN ANY RESPECT WHATSOEVER ARISING OUT OF DEFECTS CAUSED BY SUCH THIRD PARTIES, NEITHER COMPANY NOR VYXX AFFILIATES SHALL BE LIABLE FOR ANY DIRECT, INDIRECT, CONSEQUENTIAL, SPECIAL, ACTUAL, PUNITIVE OR ANY OTHER PERSON, FIRM OR ENTITY IN ANY OTHER CAUSE. THE WARRANTIES SET FORTH IN SECTION 2.19.2 AND THE REMEDIES EXPLICITLY SET FORTH IN THIS TARIFF ARE EXCLUSIVE AND IN LIEU OF ALL OTHER WARRANTIES OR REMEDIES, WHETHER EXPRESS, IMPLIED OR STATUTORY, INCLUDING WITHOUT LIMITATION IMPLIED WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE. IN THE EVENT OF AN INTERRUPTION IN SERVICE, ANY DEFECTIVE SERVICE WHATSOEVER OR FAILURE TO PERFORM UNDER THIS TARIFF, NEITHER COMPANY, VYXX AFFILIATES NOR ANY THIRD PARTY PROVIDER OR OPERATOR OF FACILITIES EMPLOYED IN THE PROVISION OF THE SERVICE SHALL BE LIABLE FOR ANY DIRECT, INDIRECT, CONSEQUENTIAL, SPECIAL, ACTUAL, PUNITIVE OR ANY OTHER DAMAGES, OR FOR ANY LOST PROFITS OF ANY KIND OR NATURE WHATSOEVER.

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- 2.3. Liability (Cont'd)
 - 2.3.8. If at any time Service is subject to a Defect as specified in Section 2.3.7 above for thirty (30) days or less, Service shall not be subject to Cancellation, but an appropriate percentage of charges for the directly affected Service shall be abated for the period of Interruption in accordance with Section 2.10. If Defective Dedicated Service continues for more than thirty (30) days, then the directly affected portion of Service may be canceled by either Company or Customer without liability other than Customer's liability for payment for the Dedicated Service in question provided in accordance with the relevant Technical Standards prior to Cancellation.
 - 2.3.9. In the event parties other than Customer (e.g., Customer's customers or Authorized Users) shall have use of the Service directly or indirectly through Customer, Customer shall forever indemnify and hold Company, Vyvx Affiliates and any third-party provider or operator of facilities employed in provision of the Service harmless from and against any and all claims, demands, suits, actions, losses, damages, assessments or payments which may be asserted by said parties arising out of or relating to any Defects or any claims described in Section 2.3.3.
 - 2.3.10. In the event that Company is required to perform a Circuit redesign due to inaccurate information provided by the Customer or Company incurs costs and expenses under circumstances in which such costs and expenses are caused to be incurred by the Customer or reasonably incurred by Company for the benefit of the Customer, the Customer is responsible for the payment of any resulting costs incurred by Company.
 - 2.3.11. Customer agrees to defend the Company against the claims as set forth in this Section 2.3 and to pay all reasonable litigation costs, attorneys' fees, court costs, settlement payments, and any damages awarded or resulting from any such claims.
 - 2.3.12. The failure to give notice of default, to enforce or insist upon compliance with any of the terms or conditions herein, the waiver of any term or conditions herein, or the granting of an extension of time for performance by the Company or the Customer shall not constitute the permanent waiver of any term or condition herein. Each of the provisions shall remain at all times in full force and effect until modified in writing.

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- 2.4. Cancellation of Service by Customer
 - 2.4.1. Except as otherwise provided under Section 2.3 of this Tariff, if a Service Order for Installation of Dedicated Service is delayed for more than thirty (30) days beyond the Requested Service Date, and such delay is not requested or caused by the Customer, the Customer may cancel the portion of Dedicated Service affected thereby without incurring Cancellation charges.
 - 2.4.2. Customer shall be subject to the following Cancellation charges upon Cancellation of Service for the convenience of Customer. In such case, Customer is also liable for any charges, expenses, fees, or penalties incurred by Company, Vyvx Affiliates or other third party providers of Service due to associated Cancellation of First-Mile and/or Last-Mile Service; any costs, expenses, or additional charges reasonably incurred by Company on behalf of Customer as Customer's agent; and an administrative surcharge shall be applied to all such charges as set forth in Section 2.19.
 - 2.4.2.A. Occasional Service. Customer may cancel the Reservation Confirmation without incurring any Cancellation charge with respect to the IXC portion of the Service, provided that the Occasional Service in question is canceled at least seventy-two (72) hours prior to the Beginning Transmission Time. If Customer cancels a Reservation Confirmation less than seventy-two (72) hours, but twenty-four (24) hours or more prior to the Beginning Transmission Time, Customer shall pay a Cancellation charge of fifty percent (50%) of the amount that Customer would have otherwise paid if the Reservation Confirmation had not been canceled. If Customer cancels less than twenty-four (24) hours prior to the Beginning Transmission Time, Customer shall pay one hundred percent (100%) of the amount that Customer would have otherwise paid if the Occasional Service had not been canceled.
 - 2.4.2.B. Dedicated Service. Customer may cancel all or a portion of the Dedicated Service upon written notification thereof to Company sixty (60) days in advance of the effective date of Cancellation. In the event of such Cancellation, Customer shall pay to Company a Cancellation charge in an amount equal to the prorated monthly charge for such canceled Dedicated Service times the number of months in the relevant Term, less the charges for such Dedicated Service actually provided to Customer through the effective date of Cancellation (but in no event less than zero).

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- 2.4. Cancellation of Service by Customer (Cont'd)
 - 2.4.2. (Cont'd)
 - 2.4.2.C. As Company's damages in the event of a Cancellation are difficult or impossible to ascertain, the foregoing provisions providing for a Cancellation charge are intended to establish liquidated damages in the event of a Cancellation of a Service and do not represent a penalty of any kind.
 - 2.4.2.D. Customer may cancel Hub Reservation Management Services upon receipt by Company of one (1) business day advance written notice of cancellation. Such cancellation notice must be delivered via express mail, certified mail or facsimile. No Vyvx cancellation charges shall apply for cancellation of Hub Reservation Management Service. However, Customer will be liable and billed for all Hub Reservation Management Service charges accrued and owed to the Company, including any cancellation charges of the Hub vendor.
 - 2.4.3. Notwithstanding the foregoing, and upon thirty (30) days' prior written notice, either Customer or Company shall have the right, without Cancellation charge or other liability to the other, to cancel the affected portion of the Service, if Company is prohibited by governmental authority from furnishing said portion, or if any material rate or term contained herein and relevant to the affected Service is substantially changed by order of the highest court of competent jurisdiction to which the matter is appealed, the Commission, the FCC, or other local, state or federal government authority.

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- 2.5. Cancellation for Cause by Company
 - 2.5.1. Upon nonpayment of any sum owing to the Company, or upon a violation by Customer of any of the provisions governing the furnishing of Service under this Tariff, the Company may, upon written notification to Customer, without incurring any liability, immediately discontinue the furnishing of such Service. Customer shall be deemed to have cancelled Service as of the date of such disconnection and shall be liable for any Cancellation charges set forth in this Tariff.
 - 2.5.2. Without incurring any liability, the Company may discontinue the furnishing of Service(s) to Customer immediately and without notice if the Company deems that such action is necessary to prevent or to protect against fraud or to otherwise protect its personnel, agents, facilities or Services or under any of the following circumstances:
 - 2.5.2.A. if Customer refuses to furnish information to the Company regarding the Customer's credit-worthiness, its past or current use of common carrier Services or its planned use of Service(s);
 - 2.5.2.B. if Customer provides false information to the Company regarding the Customer's identity, address, credit-worthiness, past or current use of Services, or its planned use of Service(s);
 - 2.5.2.C. if Customer gives Company reasonable cause to believe that Customer shall not comply with a request of the Company for reasonable security for the payment for Service(s);
 - 2.5.2.D. if Customer has been given notice by the Company of any past due amount (which remains unpaid in whole or in part) for any of the Service to which the Customer either subscribes or had subscribed or used;
 - if Customer fails to pay Company any sum due to Company within thirty (30) days of its Due Date;
 - if Customer fails to comply with a request by the Company for reasonable security for the payment of Service;
 - 2.5.2.G. if following seven (7) days after sending Customer written notice of any noncompliance by Customer with any nonpayment terms (other than an unlawful use of the Service), and if such noncompliance with the terms and conditions of this Tariff is not corrected within the seven (7) day period (Service may, however, be discontinued earlier pursuant to this Tariff.);

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- 2.5. Cancellation for Cause by Company (Cont'd)
 - 2.5.2. (Cont'd)
 - 2.5.2.H. if such actions are reasonably appropriate to avoid violation of applicable law; or
 - 2.5.2.I. if there is a reasonable risk that criminal, civil or administrative proceedings or investigations based upon the transmission contents shall be instituted against Company or Vyvx Affiliates.
 - 2.5.3. If at anytime there is a material change in Customer's credit-worthiness, then in addition to any other remedies available to Company pursuant to this Tariff, Company may exercise one or more of the following remedies without incurring any liability: (A) cause Start of Service for Service described in a previously executed Service Order or the Beginning Transmission Time described in a Reservation Confirmation to be withheld; (B) cease providing Service; (C) decline to accept a Service Order from Customer or provide a Reservation Confirmation to Customer for the provision of Service which Company may otherwise be obligated to accept and/or (D) Company may condition its provision of Service on assurance of payment by Customer which shall take the form of a deposit or means to establish reasonable assurance of payment as specified by Company, provided that no such deposit or assurance shall exceed the applicable Installation charges, if any, and/or up to two and one-half months of actual or estimated usage charges for the Service to be provided. A material change in Customer's credit-worthiness shall include, but not be limited to: (A) Customer's default of its obligations to Company under this Tariff or any other agreentent with Company or Vyvx Affiliates; (B) failure of Customer to make full payment of charges due hereunder on or before the Due Date on three or more occasions during any period of twelve or fewer months or Customer's failure to make such payment on or before the Due Date in any two consecutive months; (C) acquisition of Customer (whether in whole or by majority or controlling interest) by an entity which is insolvent, which is subject to bankruptcy or insolvency proceedings, which owes past due amounts to Company, Vyvx Affiliates or any other entity affiliated with Company or which is a greater credit risk than Customer; or, (D) Customer's being subject to or having filed for bankruptcy or insolvency proceedings or the legal insolvency of Customer.
 - 2.5.4. The discontinuance of Service(s) by the Company pursuant to this Section does not relieve the Customer of any obligations to pay the Company for charges accrued for Service(s) which is/are furnished up to the time of discontinuance nor does it relieve the Customer of applicable Cancellation charges. The remedies set forth herein shall not be exclusive and the Company shall at all times be entitled to all rights available to it under either law or equity.

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SECTION 2 -- RULES AND REGULATIONS (Cont'd)

2.6. Use of Service

- 2.6.1. The Services offered herein may be used for any lawful purpose, including residential, business, governmental, or other use, including joint use or resale by Customer. Notwithstanding the joint use, sharing or resale of Service by Customer and regardless of the Company's knowledge of same, the Customer remains liable for all obligations under this Tariff. The Company shall have no liability to any person or entity other than the Customer and only as set forth in Section 2.3. The Customer shall not use nor permit others to use the Service in a manner that could interfere with Services provided to others or that could harm the facilities of the Company or others.
- 2.6.2. The Customer is responsible for the placement of Service Orders or requests for Reservation Confirmations for the Service described herein as well as complying with the provisions of this Tariff. Customer may be required to execute written Service Orders or other documents relating to the Service, but Customer shall be obligated under the terms of this Tariff even if such Service Orders or other documentation have not been executed.
- 2.6.3. Service provided by the Company may upon authorization by the Company be arranged for joint use by Authorized Users. The Authorized User shall be permitted to use such Service in the same manner as the Customer, but subject to the following:
 - 2.6.3.A. One Authorized User must be designated as the Customer. The designated Customer does not necessarily have to have transmission requirements of its own. The Customer must specifically name all Authorized Users in the application for joint use Service. Service Orders may be accepted from and Reservation Confirmations may be sent to such Authorized Users and shall be subject to all regulations of this Tariff.

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- 2.6. Use of Service (Cont'd)
 - 2.6.3.B. All charges for the Service shall be computed as if the Service were to be billed to one Customer. The Authorized User which has been designated as the Customer shall be billed for all components of the Service and shall be responsible for all payments to the Company. In the event that the designated Customer or any Authorized User fails to pay the Company, each Authorized User shall be jointly and severally liable to the Company for all charges associated with its Service as well as any other Authorized User's Service. Each Authorized User must submit to the designated Customer sufficient documentation for the purpose of confirming such Authorized User's acceptance of contingent liability for and guaranty of payment for its portion of all charges billed by the Company for joint use Service to the designated Customer. This documentation must also specify that the Authorized User understands that the Company shall receive a copy of the payment guaranty from the designated Customer. The designated Customer shall be responsible for allocating charges to each Authorized User of joint use Service, and Company shall have no obligation to seek collection from Authorized Users of joint use Service.
 - 2.6.4. In addition to the other provisions in this Tariff, a Customer reselling Service shall be responsible for all interaction and interface with its own subscribers or customers. The reselling of Service by a Customer or reselling of Service with enhancements provided by Customer shall not create a partnership or joint venture between Company and Customer nor result in a joint service offering to any third parties by either Company or the Customer.
 - 2.6.5. Neither the Service furnished by the Company nor transmissions or communications carried over such Service shall be used for any unlawful or fraudulent purposes. Nor shall Service be used for any purpose for which any payment or other compensation is received by the Customer except when the Customer is a communications common carrier, a resale common carrier or an enhanced Service provider who has subscribed to the Service. However, this provision does not preclude an agreement between the Customer and Authorized Users in a joint use arrangement to share the cost of the Service as long as this arrangement generates no profit for anyone participating in a joint use arrangement.

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SECTION 2 - RULES AND REGULATIONS (Cont'd)

- 2.6. Use of Service (Cont'd)
 - 2.6.6. Company's Services are not adapted to the use of recording devices and Customers who use such devices to record transmissions, or for other purposes, do so at their own risk. Neither Customer nor any other entity may record a conversation except as permitted by applicable law.
 - 2.6.7. Any Customer requesting Secondary Drop-Off Service of another Customer's transmission shall be responsible for providing Company with a signed authorization from such other Customer entitling Customer requesting the Secondary Drop-Off Service to receive such transmission, and all Customers shall be responsible for making all arrangements with copyright holders, music licensing organizations, performers' representatives, or other parties for necessary authorizations, clearances or consents with respect to the transmission contents (all such authorizations, clearances or consents referenced in this sentence shall collectively be referred to as "Consents"). Company shall not be liable for any such failure of Customer to obtain Consents and Customer shall indemnify and hold harmless Company and Vyvx Affiliates as set forth in Section 2.3.3.
 - 2.6.8. The Customer recognizes that certain unusual, newsworthy events may cause a great demand for the Company network. In order to provide fair and equitable service to all of the Company network users, Customer agrees as follows: (A) If Customer should request Occasional Service within one (1) hour or less of a requested transmission time for such Service which shall occur over or as a part of any period greater than sixty (60) minutes, Company shall have the right to interrupt such Occasional Service in excess of any period greater than sixty (60) minutes from the commencement of the first transmission period; or (B) If Customer requests Occasional Service within one (1) hour or less of a requested transmission time for Occasional Service requiring multiple Channels between the same POPs for an extended length of time, Company shall have the right to limit the number of such Channels.

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2.7. Payment Arrangements

- 2.7.1 The Customer is responsible for payment of all charges for Services furnished to the Customer or Authorized User. This includes payment for Services specifically requested by the Customer. This responsibility is not changed due to any use, misuse, or abuse of the Customer's Service or Customer provided equipment by third parties, the Customer's employees, or the public.
- 2.7.2. Unless the Company requires an advance Payment Method or other arrangement due to Customer's presenting an undue risk of nonpayment, payment for Services shall be made in the manner set forth in Section 2.7.3 and .4 with respect to the appropriate Services ordered. Customer shall remit payment to Company at the remittance address indicated on Company's invoices to Customer. In the event Customer fails to pay Company's invoice in full or remit payment to the proper address on or before the Due Date, Customer shall also pay a late fee in the amount of the lesser of one and one-half percent (1½%) of the unpaid balance per month or the maximum lawful rate under applicable state law. If a Customer presents an undue risk of nonpayment at any time, the Company may require that Customer pay its bills within a specified number of days and to make such payments in cash or the equivalent of cash.

2.7.3. Dedicated Service

All pro-rated monthly recurring charges (charges for monthly Service provided for less than a calendar month). Installation and other nonrecurring charges associated with Dedicated Service shall be due on the first day of the month following the month in which the Service was provided. Payment for all monthly recurring charges for full months during which Dedicated Service is to be provided following Start of Service shall be due in advance on the first day of that month. Dedicated Service provided for a Term of less than one (1) month shall be billed in the month following the month in which Service was provided. For the purposes of computing charges and/or credits in this Tariff for periods of less than a calendar month, a month is considered to have 30 days.

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- 2.7. Payment Arrangements (Cont'd)
 - 2.7.4. Occasional Service

Payment for all charges associated with Occasional Service shall be due on the first day of the month following the Billing Date set forth on the Company invoice to Customer for such Service.

Company shall invoice Customer monthly for Occasional Service for the period between the first of the prior month to the end of such prior month ("Occasional Billing Period"). The Occasional Billing Period shall be subject to changes at the sole option of Company.

2.7.5. In determining whether a Customer presents an undue risk of nonpayment, the Company shall consider the following factors: (A) the Customer's payment history (if any) with the Company and Vyvx Affiliates, (B) Customer's ability to demonstrate adequate ability to pay for the Service, (C) credit and related information provided by Customer, lawfully obtained from third parties or publicly available, and (D) information relating to Customer's management, owners and affiliates (if any). A Customer who presents an undue risk of nonpayment may be required at any time to provide the Company with a security deposit, in cash or the equivalent of cash, up to an amount equal to the applicable Installation charges, if any, and/or up to two and on-half months of actual or estimated usage charges for the Service to be provided. Such applicants or Customers may also be required, at any time, whether before or after the company's charges for its Services as the Company may deem necessary, including without limitation, advance payments for Service, third party guarantees of payment, letters of credit, pledges or other grants of security interests in such Customer's assets, and similar arrangements. The required deposit or other security, including any advance Payment Method, may be increased or decreased by the Company as it deems appropriate in the light of changing conditions, provided that the amount of any deposit or other security shall not exceed the applicable Installation charges, if any, and/or up to two and one-half months of actual or estimated usage charges for the Service to be provided. In addition, the Company shall be entitled to require such an applicant or Customer to pay all its bills within a specified period of time, and to make such payments in cash or the equivalent of cash. In case of a cash deposit, simple interest at the rate of 7% per annum shall be credited or paid to the Customer while the deposit is held by the Company. At the Company's option, such deposit may be refunded to the Customer'

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SECTION 2 -- RULES AND REGULATIONS (Cont'd)

- 2.7. Payment Arrangements (Cont'd)
 - 2.7.6. Disputes with respect to charges must be presented to the Company in writing within three (3) months from the date the invoice is rendered or such invoice shall be deemed to be correct and binding on the Customer. Any amounts so disputed by Customer which have not been paid to Company, shall be paid to Company or resolved in favor of Customer by mutual agreement between Customer and Company within sixty (60) days of the Due Date. Company shall subsequently refund to Customer any such amounts that are determined to be billed by Company in error. Any disputes not resolved may be brought before the Florida Public Service Commission.
 - 2.7.7. If a First-Mile or Last-Mile Service Provider of Service procured on behalf of Customer by Company has established or establishes a special access surcharge, the Company shall bill the surcharge to Customer. The Company shall cease billing the special access surcharge upon receipt of an Exemption Certificate from Customer or if the surcharge is removed by the First-Mile or Last-Mile Service Provider.
 - 2.7.8. In the event the Company incurs fees or expenses, including attorney's fees, in collecting, or attempting to collect, any charges owed the Company, the Customer shall be liable to the Company for the payment of all such fees and expenses reasonably incurred.
 - 2.7.9. If a Customer whose account has been closed has a credit balance remaining, the Company shall transfer the credit to another account of the Customer, if there is one, or shall mail a check for the balance to the Customer promptly following the written request of Customer.
 - 2.7.10. Promotional and other credits offered by Company in marketing its Services cannot be assigned. Such credits must be used by the Customer to whom they were offered or the Customer who earned them under the provisions of the offer.
 - 2.7.11. The Installation charges set forth in this Tariff contemplate Installations made in normal locations and under normal working conditions.

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- 2.7. Payment Arrangements (Cont'd)
 - 2.7.12. Subject to any limitations set forth in applicable laws and regulations, Company shall have the right to back bill Customer for any Services which Company failed to invoice at a prior time.
 - 2.7.13. Hub Reservation Management Service

Payment for all charges associated with Hub Reservation Management Service shall be due on the first day of the month following the Billing Date set forth on the Company invoice to Customer for such Service.

Company shall invoice Customer monthly for Hub Reservation Management Service for the period between the first of the prior month to the end of such prior month ("Hub Reservation Management Service Billing Period"). The Hub Reservation Management Service Billing Period shall be subject to change at the sole option of the Company.

2.8. Assignment

The obligations set forth in this Tariff shall be binding upon and inure to the benefit of the parties hereto and their respective successors or assigns, provided, however, that the Customer shall not assign or transfer its rights or obligations without the prior written consent of the Company.

- 2.9. Tax Adjustments
 - 2.9.1. All stated charges in this Tariff are computed by the Company exclusive of any federal, state, or local use, excise, gross receipts, sales or privilege taxes, duties, fees, or similar liabilities (other than the general income or property taxes of Company) whether charged to or against the Company or its Customer. Such taxes, fees, etc. shall be paid by the Customer in addition to the charges stated in this Tariff. All such taxes, duties, and fees shall each be shown as a separate line item on the Customer's monthly invoice.

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2.9. Tax Adjustments (Cont'd)

2.9.2. A surcharge is imposed on all charges for Service originating at addresses in states which levy a gross receipts tax on Customer's operations. Pending the conclusion of any litigation challenging a jurisdiction's right to impose any tax. Company may elect to impose and collect a surcharge covering such tax, unless otherwise constrained by court order or direction, or it may elect to waive any surcharge. If it has collected a surcharge or tax and the challenged surcharge or tax is found to have been invalid and unenforceable, Company shall credit or refund such sums to each affected Customer if either Company has retained such funds or Company has remitted such funds to the collecting jurisdiction and the funds have been returned to Company. The surcharge shall be shown as a separate line item on the Customer's monthly invoice.

2.10. Allowance for Interruptions

2.10.1. No credit allowances shall be made for:

٠	No credit allov	vances shall be made for:
	2.10.1.A.	Interruptions caused by the negligence (including the provision of inaccurate information) of the Customer or other authorized by the Customer to use the Customer's Service.
	2.10.1.B.	Interruptions during any period which the Company or its agents are not afforded access to any Customer premise where Service is originated or terminated.
	2.10.1.C.	Interruptions during any period when the Customer or user has released the Service to the Company for maintenance or rearrangement purposes, or for the implementation of a Customer Service Order or Reservation Confirmation.
	2.10.1.D.	Interruptions during periods when the Customer elects not to release the Service for testing or repair and continues to use it on an impaired basis.
	2.10.1.E.	Interruptions not reported to the Company.
	2.10.1.F.	Interruptions occurring prior to Start of Service.
	2.10.1.G.	Interruptions for Hub Reservation Management Service caused by Customer's equipment.
	2.10.1.H.	Interruptions caused by Customers directly booking or placing Hub Reservations between Customer and Company Hub circuits.

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2.10. Allowance for Interruptions (Cont'd)

2.10.2.A.

- 2.10.2. Credit shall be given for Interruptions as follows:
 - Dedicated Service. Company warrants that Interexchange Dedicated Service shall conform to the relevant Technical Standards set forth in Section 3. Following the Start of Service date, if Customer reports an Interruption in Service to Company at the TOC and the affected Service is not Restored as warranted within one-half hour of such report, Customer shall, upon request directed to the Customer's designated customer service representative, receive a credit at the rate of 1/1440 of the monthly recurring charges applicable to Service directly affected by such Interruption for each half hour or major fraction thereof in excess of the first half hour during which such Service fails to conform to the relevant Technical Standards, as provided in the formula:

Credit = A x $\frac{B}{1440}$

Where A = The number of half hours or major fraction thereof of interruptions in excess of the first half hour; and

B = The monthly recurring charges.

If a portion of the Service fails to conform to the relevant Technical Standards at any time and over a period of thirty (30) days, the Customer may notify Company in writing of its conditional intent to cancel such Service in accordance with the Cancellation provisions herein. If, over a period of thirty (30) days after receipt of such notice, the Service fails to conform to the relevant Technical Standards, the Customer may terminate the affected portion of the Service for such cause and without a Cancellation charge at the expiration of the notice period.

2.10.2.B. Occasional Service. Company warrants that Interexchange Occasional Service shall conform to the relevant Technical Standards set forth in Section 3. Following the Beginning Transmission Time, if Customer reports an Interruption in Occasional Service to the TOC, Customer shall receive a credit determined by multiplying the applicable minute charge for such affected Occasional Service by the number of minutes (rounded to the nearest full minute) that such Interruption occurred.

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2.10. Allowance for Interruptions (Cont'd)

2.10.C. Hub Reservation Management Service

Reservation Management Service to the TOC, Customer shall receive a credit for both Hub Reservation Management Service charges, if any, and the affected IXC Service determined by multiplying the applicable per minute charge for such affected Hub Reservation Management Service and IXC Service by the number of minutes (rounded to the nearest full minute) that such Interruption occurred, provided that in no event will Customer receive total credits under this tariff greater than the per minute amounts that would otherwise be owing. No credit will be given in the event a Customer places a Hub Reservation directly with the appropriate Hub vendor.

- 2.10.3. Notice of Interruption should be reported by the Customer to the TOC. An Interruption ends when the Service is Restored. If the Customer reports the Service to be inoperative but declines to release it for testing and repair, the Service is deemed to be impaired, but not subject to an Interruption nor corresponding credit as provided in Section 2.10.2.
- 2.10.4. If the Customer elects to use another means of transmission during the period of Interruption, the Customer is solely responsible for payment of the charges for the alternate transmission service used.
- 2.10.5. Preemptions as described in Section 2.18 shall be credited as Interruptions.
- 2.10.6. The credit provided in Section 2.10.2 is Customer's sole and exclusive remedy for any Interruption in the Service.

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- 2.11. Method for Calculation of Airline Mileage
 - 2.11.1. The airline mileage between two cities can be calculated using the Vertical (V) and Horizontal (H) coordinates of the serving wire centers associated with the Company's POP locations. The method for calculating the airline mileage is obtained by reference to AT&T's Tariff F.C.C. No. 10 according to the following formula:

The square root of:

$$(V_1 - V_2)^2 + (H_1 - H_2)^2$$

where V, and H, correspond to the V&H coordinates of City 1 and V $_2$ and H $_2$ correspond to the V&H coordinates of City 2.

Example:

V H
City 1 5004 1406
City 2 5987 3424

The square root of:

$$(5004 - 5987)^2 + (1406 - 3424)^2$$

The result is 709.83 miles. Any fractional miles are rounded to the next higher whole number; therefore, the airline mileage for this example is 710 miles.

2.11.2. Airline Mileage is used to calculate the charge for Dedicated Interexchange Service set forth in Section 4.3.

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2.12. Collocation of Customer Equipment

The Company shall consider requests from Customers or prospective Customers to locate Customer equipment at Company's POPs, provided space is determined, solely by Company, to be Available and uncommitted. Such collocation of Customer equipment shall be solely for the purpose of interconnecting such Customer equipment with Company's Service, subject to (A) the Company's current and forecasted physical space requirements, taking into account available space, at the relevant POP, (B) any applicable lease or occupancy restrictions imposed on the Company, (C) the technical and operational compatibility of the Customer's equipment with the Company equipment and Services, (D) the Company's security and revenue requirements, and (E) other terms and conditions to which the Customer contractually shall commit.

2.13. Change in Service Arrangement

When a change in Service arrangement is made, such as a change of First-Mile or Last-Mile Circuits, First-Mile and Last-Mile Service Provider charges and/or Ancillary Charges may apply depending on the nature of the change in Service arrangement requested.

2.14. Inspection

The Company may, upon notice, make such tests and inspections as may be necessary to determine that the requirements of this Tariff are being complied with in the installation, operation or maintenance of Customer or the Company's equipment. The Company may interrupt the Service at any time, without penalty to the Company, because of departure from any of these requirements.

2.15. Testing and Adjustment

Upon reasonable notice, the Channels provided by the Company shall be made available to the Company for such tests and adjustments as may be necessary to maintain them in satisfactory condition; no interruption allowance shall be granted for the time during which such tests and adjustments are made.

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- 2.16. Interconnection with Other Carriers
 - 2.16.1. Service furnished by the Company may be connected with Services or facilities of another carrier. Such interconnection may be made as authorized by the Company at the Company POP, at a Point of Presence of another carrier, or at the Customer Premises, or premises of an Authorized User. Service furnished by the Company is not part of a joint undertaking with such other carriers.
 - 2.16.2. Any special interface equipment or facilities necessary to achieve compatibility between the facilities of the Company and other participating carriers shall be provided at the Customer's expense. Upon the Customer's request and acting as its authorized agent, the Company shall attempt to make the necessary arrangements for such interconnection.
- 2.17. Restoration of Service

The use and restoration of Service in emergencies shall be in accordance with Part 64, Subpart D of the Federal Communications Commission's Rules and Regulations to the extent it is applicable, which specifies the priority system for such activities.

- 2.18. Preemptive Procedures
 - 2.18.1. Company shall use reasonable efforts to reroute and Restore Service in the event of an Interruption due to a Defect in the Interexchange Service. Company shall Restore Customers in the following order: Redundant Routing Customers, Non-Preemptible Service Customers, and Preemptible Service Customers. Service to Preemptible Customers shall be replaced by Service to Non-Preemptible Customers if insufficient facilities exist on the network to accommodate restoration of all existing Circuits. If a Non-Preemptible Customer's Beginning Transmission Time has not started when restoration procedures begin, such Customer's Service shall be rescheduled and shall not replace then current transmissions of Company Service to others on the Company network.
 - 2.18.2. A Customer whose Service is replaced by preemptible transmission shall receive credit as described in Section 2.10.2.

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SECTION 2 -- RULES AND REGULATIONS (Cont'd)

2.19. Administrative Surcharges

The Customer shall be liable for any charges which the Company may incur in provisioning third party facilities for Customer's use in conjunction with the Service, e.g., First-Mile/Last-Mile Circuits, provision of on-site technician, Cancellation, Expedite, etc. The charge to Customer for this Service shall be the actual charge for such service as incurred by the Company from the third party provider ("Provider Charge") plus a Company administrative surcharge of 15% of such Provider Charge. Company shall invoice Customer for such charges.

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SECTION 3 -- TECHNICAL STANDARDS

3.1. Application of Technical Standards

The following Technical Standards for Services set forth objectives for Company to follow. In no circumstance shall these Technical Standards be construed as creating any warranty on the part of Company, with the exception of those warranties expressly set forth in the preceding Sections of this Tariff. Company does not warrant the First-Mile and Last-Mile Service.

- 3.2. Technical Standards Defined
 - 3.2.1. The following are the Technical Standards for Service which is a Broadcast Contribution Quality Television Transmission Service with One-Way Analog Access:
 - 3.2.1.A. Signal interface specifications defined in ANSI T1.502-1988 and those publications referenced therein for System M-NTSC video and associated audio signal interface standards.
 - 3.2.1.B. Quality Standards
 - 3.2.1.B.1. General

Standards for Service apply independently for First-Mile and Last Mile Circuits and Interexchange Service from POP to POP and exclude non-performance due to circumstances listed in Section 2.3.1 and .2 or Interruptions as set forth in Section 2.10.1. First-Mile and Last-Mile Circuit standards apply on a One-Way basis between each Customer Premise Network Interface Point ("CPNIP") and the Company POP. Interexchange Service standards apply on a One-Way basis between the originating and terminating Company POP. The actual End-to-End performance of the Service (CPNIP) shall be a combined function of the First-Mile and Last-Mile Circuits and Interexchange Service performance and may be affected by the Customer provided equipment, dependent on the type and quality of Customer equipment used.

3.2.1.B.2. Interexchange Service Standards

The performance of the Interexchange portion of the Service is measured by the standards set forth in the Medium Haul transmission standards of the ANSI T1.502-1988 and those publications referenced therein, as limited by the relevant television enabling equipment, for transmissions of System M-NTSC Video and associated audio channels.

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SECTION 3 -- TECHNICAL STANDARDS (Cont'd)

- 3.2. Technical Standards Defined (Cont'd)
 - 3.2.1.B.3. First-Mile and Last-Mile Circuit Standards

The performance of First-Mile and Last-Mile Circuit is measured by the standards set forth in the applicable transmission parameters of the ANSI T1.502-1988 and those publications referenced therein for the transmission of System M-NTSC video and associated audio channels.

- 3.2.2. The following are the Technical Standards for Service which is a Broadcast Contribution Quality Television Transmission Service with Digital Access:
 - 3.2.2.A. Signal Interface Specifications

Defined in ANSI Standard T1.102 and T1.105 (formerly AT&T Compatibility Bulletin 119) and Technical Reference Publication 62411.

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SECTION 3 -- TECHNICAL STANDARDS (Cont'd)

3.2. Technical Standards Defined (Cont'd)

3.2.2. (Cont'd)

3.2.2.B. Quality Standards

3.2.2.B.1. General

Standards for Service apply independently for First-Mile and Last-Mile Circuits and Interexchange Service from POP to POP and exclude non-performance due to circumstances listed in Section 2.3.1 and .2 or Interruptions as set forth in Section 2.10.1. First-Mile and Last-Mile Circuit standards apply on a One-Way basis between each Customer Premise Network Interface Point ("CPNIP") and the Company POP. Interexchange Service standards apply on a One-Way basis between the originating and terminating Company POP. The actual End-to-End performance of the Service (CPNIP to CPNIP) shall be a combined function of the First-Mile and Last-Mile Circuits and Interexchange Service performance and may be affected by the Customer provided equipment, dependent on the type and quality of Customer equipment used.

3.2.2.B.2. Interexchange Standards

Defined in ANSI Standard T1.102 and T1.503 (formerly AT&T Compatibility Bulletin 119) and Technical Reference Publication 62411.

3.2.2.B.3. First-Mile and Lart-Mile Circuit Standards

Defined in ANSI Standard T1.102 and T1.503 (formerly AT&T Compatibility Bulletin 119) and Technical Reference Publication 62411.

3.2.3. Notwithstanding the foregoing, at Company's option, Company may provide a comparable transmission alternative, e.g. satellite transmission, ("Alternative Transmission"). Such Alternative Transmission shall comply with the respective standards commonly used in the industry for such service.

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SECTION 4 -- DEDICATED SERVICE OFFERING

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SECTION 5 -- OCCASIONAL SERVICE OFFERING

5.1. Definition and Description

Occasional Service is offered to the Customer as a reservation based, switched, One-Way or Two-Way Point-to-Point or a Point to Multi-Point Channel on a Preemptible and Non-Preemptible basis. The various types of Occasional Service are subject to Availability between Company designated POPs in the cities set forth in Section 8. The Interexchange Service charges for fifteen (15), thirty (30), forty-five (45) and sixty (60) minute periods, applicable to Occasional Service are set forth below. Occasional Service is offered in fifteen (15) minute billing increments. Occasional Service ordered (as stated on the relevant Reservation Confirmation) for a period of time in excess of sixty (60) minutes shall be billed at a pro-rated sixty (60) minute charge for each fifteen (15) minute period. Other charges which may be applicable are Ancillary Charges (Section 5.4), Cancellation Charges (Section 2.4 and 5) and Taxes (Section 2.9.1 and .2).

- 5.2. Occasional Interexchange Service
 - 5.2.1. Company's Occasional Interexchange Service provides One-Way or Two-Way, POP to POP transmission designed for use in video and associated audio transmission applications on a Preemptible basis. One-Way Occasional Interexchange Service provides one(1) System M-NTSC video channel and up to three (3) associated audio channels (50Hz to 15kHz).
 - Early Acceptance, Extension and/or Overage may be provided pursuant to Customer's request subject to Availability.
 - 5 2.3. Customer may order, if Available, an Approx-End. Once an Approx-End Period has commenced, the Customer shall be charged through the end of the Approx-End Period, in the following increments, unless Customer timely and adequately has informed Company that the transmission is to end prior to the beginning of the Approx-end Period. Reservations 60 minutes or iess receive Approx-Ends of 15 minutes. Reservations greater than 60 minutes receive Approx-Ends of 30 minutes, available in 15 minute increments. Upon Customer's request and subject to the Service being Available, if a transmission continues past the Approx-End Period, the Service shall be in Overage and subject to the Overage charges in Section 5.4.2.

The Approx-End shall be reserved for Customer on a right of first refusal basis. If Company receives a request from a different Customer for the same Service time, Company shall notify the Customer with the Approx-End reservation. Within the earlier of: (A) one (1) hour after such notification or (B) fifteen (15) minutes prior to the Beginning Transmission Time, Customer must notify Company's Customer Service Group that Customer is committing to such Service through the Approx-End Period or Customer shall not receive Service through the Approx-End Period. Once making such a commitment, Customer shall be liable for the relevant charges.

SECTION 5 - OCCASIONAL SERVICE OFFERING (Cont'd)

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- 5.2. Occasional Interexchange Service (Cont'd)
 - 5.2.4. The Beginning Transmission Time and Ending Transmission Time shall be the same for each simplex Circuit of a Two-Way transmission ordered by Customer.
- 5.3. Occasional Preemptible Interexchange Service Charges
 - 5.3.1.A. Charges set forth below are charges which apply to Point-to-Point, Preemptible Occasional Interexchange Service.

Reserved									One	Two
Time Period									Way	Way
15 minutes				ï	4				\$ 140	\$ 210
30 Minutes							्		\$ 250	\$ 375
45 Minutes			٠			÷			\$ 360	\$ 540
60 Minutes									\$ 440	\$ 660

5.3.1.B. Between the hours of 1:00 a.m. and 6:00 a.m. Eastern Time, Company will provide One-Way, Preemptible Occasional Interexchange Service ("Non-Prime Occasional Service") between Company POPs.

									One Way
15 minutes							٠		\$ 95
30 minutes				Ų.					\$ 150
45 minutes			ĺ.		į.				\$ 205
60 minutes									\$ 265

Customer must specify this Non-Prime Occasional Service when requesting the Reservation Confirmation. Only reservations which start and end during the five hour Non-Prime Occasional Service window are eligible to receive this discounted pricing.

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- 5.3. Occasional Preemptible Interexchange Service Charges (Cont'd)
 - 5.3.2. Charges set forth below are charges which apply to the One-Way IXC portion of Preemptible. Point to Multi-Point Occasional Interexchange Service. Charges are determined according to the number of destination POPs. The minimum billing increment for each destination POP charge is fifteen (15) minutes.

Charges for Point to Multi-Point Occasional Service

Reserved time period of less than 60 minutes: The charge shall be the relevant One-Way, Point-to-Point, Preemptible Occasional Interexchange Service charge (set forth in Section 5.3.1) plus a charge of \$50 for each additional destination POP above the initial Point-to-Point destination.

Reserved time period of 60 minutes or greater: The charge for the initial 60 minutes shall be the 60 minute rate for One-Way, Point-to Point Preemptible Occasional Interexchange Service (set forth in Section 5.3.1) plus a charge of \$50 per hour for each additional destination POP above the initial Point-to-Point destination. Such charge shall be pro-rated for each additional 15 minute increment beyond the initial 60 minutes of reserved time.

5.3.3. Charges set forth below are charges which apply to PGAD/Secondary Drop-Off Service. PGAD/Secondary Drop-Off Service shall start no earlier than the Beginning Transmission Time and end no later than the Ending Transmission Time of the relevant Point-to-Point or Point to Multi-Point Occasional Service transmission to which it is associated. PGAD/Secondary Drop-Off Service shall be billed in sixty (60) minute all increments, i.e., there shall be a full hour charge for any fraction of an hour.

Per PGAD/Secondary Drop-Off Service\$75 per hour

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5.4. Ancillary Charges

5.4.1. Local Switching

Charges apply when a Customer requests the temporary Cross Connect of one Customer owned First-Mile/Last-Mile Circuit to another First-Mile/Last-Mile Circuit both of which are terminated in the same POP, provided such Circuits are Available. This Service shall be provided for the transmission of broadcast television or for other interstate uses only except to the extent applicable laws and regulations permit other uses. Such Cross Connect shall terminate at any time any relevant First-Mile/Last-Mile Circuit is required pursuant to a Reservation Confirmation.

- 5.4.1.A. Customer-to-Customer Local Switch The charge for a Local Switch between one Customer First-Mile Circuit and another Customer Last-Mile Circuit within the same POP shall be \$25 per switch, or fraction thereof, not to exceed 24 hours.
- 5.4.1.B. Customer-to-Hub Local Switch -- The per switch charge for cross connecting a Customer First-Mile/Last-Mile Circuit to a Hub circuit provisioned by Company and within the same TSC shall be \$25 per hour or fraction thereof.

5.4.2. Overage Charges

- 5.4.2.A. The charge for Overage with respect to a Reservation Confirmation with a reserved time of sixty (60) minutes or longer shall be at the proportionate sixty (60) minute charge as set forth in Section 5.3.
- 5.4.2.B. The charge for overage per each fifteen (15) minutes of Overage for Point-to-Point, Preemptible IXC Occasional Service with respect to a Reservation Confirmation with a reserved time of less than sixty (60) minutes shall be at the appropriate fifteen (15) minute rate for the applicable service or services.

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- 5.4. Ancillary Charges (Cont'd)
 - 5.4.2. (Cont'd)
 - 5.4.2.C. The following charges apply per each fifteen (15) minutes of Overage for One-Way, Point to Multi-Point, Preemptible IXC Occasional Service with respect to a Reservation Confirmation with a reserved time of less than sixty (60) minutes. The charge shall be the 15 minute rate for One-Way, Point-to-Point, Preemptible Occasional Interexchange Service (set forth in Section 3.3.1) plus a charge of \$50 for each additional destination POP above the initial Point-to-Point destination.
 - 5.4.2.D. The following charges apply per each fifteen (15) minutes of Overage for One-Way. Point to Multi-Point, Preemptible IXC Occasional Service with respect to a Reservation Confirmation with a reserved time of sixty (60) minutes or greater. The charge shall be at the proportionate sixty (60) minute charge as set forth in Section 5.3.2 for reserved time of 60 minutes or greater.
 - 5.4.3. Cancellations

A Cancellation charge applies when a Customer cancels a transmission prior to or after the Beginning Reservation Time as set forth in Section 2.4. However, if the associated Occasional Service transmission of a Secondary Drop-Off Service is canceled, the Secondary Drop-Off Service shall be automatically canceled, and Cancellation charges shall not apply to the Secondary Drop-Off Service. If only the Secondary Drop-Off Service is canceled and not the associated Occasional Service transmission, the Cancellation charges set forth in Section 2.4 shall apply to the Secondary Drop-Off Service.

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5.4. Ancillary Charges (Cont'd)

5.4.4. Change in Reservation

Any change or rescheduling of a reservation shall subject the Customer to Cancellation charges except for Early Acceptance, Extension or Overage. Notwithstanding the foregoing, a Reservation Confirmation may be rescheduled to a different date and Beginning Transmission Time if Available ("Postponed Reservation") with no Cancellation charge for the Interexchange portion of the Occasional Service, provided the Postponed Reservation is for the same or longer length of transmission time and between the same two points as the original Reservation Confirmation. If the different date and Beginning Transmission Time requested by Customer is not Available, Customer shall not be charged a Cancellation charge for the Interexchange portion of the Occasional Service. A Reservation Confirmation shall be postponed only once. A Postponed Reservation which is subsequently canceled shall receive a 100% Cancellation charge notwithstanding Section 2.4.2.

5.4.5. On-Site Technician Charge

The Company may provide, when available, non-Company on-site technicians for a transmission at the Customer's request.

The charge for this service shall be the charge of the service as received by the Company from the vendor pursuant to applicable tariffs and rates. In addition, the Company shall also add a 15% administrative surcharge pursuant to Section 2.19.

5.4.6. Vendor Connectivity Charges

Customers who request that Service be terminated at another carrier's or vendor's facility for further transmission or enhancement can schedule for the Company to coordinate all of the applicable reservations. The Customer shall then be billed for all applicable charges. The charge for this Service shall be the charge incurred by the Company from such other carrier or vendor, as the case may be, plus an administrative surcharge of fifteen percent (15%) pursuant to Section 2.19. Vendor Connectivity charges do not apply where Hub Reservation Management Service is employed by Customer.

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- 5.4. Ancillary Charges (Cont'd)
 - 5.4.7. Premise Equipment Charges

All Customer Premise equipment provided by Company shall be provided under contract between Customer and Company.

5.4.8. Non-Standard Charges

Non-standard Installation/maintenance/engineering charges apply as follows:

5.4.8.A. Charges apply when the Customer requests Installation or Circuit changes during non-business hours and when the Customer requests the provision of engineering design or other activities which are not normally provided as a part of the design and Installation of Service.

Normal business hours are 8:00 a.m. - 5:00 p.m., Monday through Friday, excluding legal holidays.

Additional Installation/Maintenance/Engineering Charges

5.4.8.A.1 Normal Business Hours \$125.00 per hour per person

5.4.8.A.2. After Normal Hours \$150.00 per hour per person

5.4.8.A.3. All reasonable expenses including, but not limited to lodging, travel and meal expenses, if any, incurred which are relevant to providing such Installation, maintenance and engineering Service.

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- 5.4. Ancillary Charges (Cont'd)
 - 5.4.8. Non-Standard Charges (Cont'd)
 - 5.4.8.B. Charges apply when the Customer requests a Company technician at the Customer Premises or when Defects occur as a result of problems in the Customer's equipment. Normal business hours are 8:00 a.m. 5:00 p.m., Monday through Friday, excluding legal holidays. Rates are based upon a two-hour minimum.

Company Technician Charges

5.4.8.B.1. Normal Business Hours . . . \$ 80.00 per hour per person

5.4.8.B.2. After Normal Hours \$ 120.00 per hour per person

5.4.8.B.3. Sundays and Holidays \$ 120.00 per hour per person

- 5.4.8.B.4. All reasonable expenses including, but not limited to lodging, travel and meal expenses, if any, incurred which are relevant to providing such Installation,main-tenance and engineering Service.
- 5.4.8.C. All non-standard charges are in addition to any similar charges incurred from any third party vendor which shall be passed on to Customer plus an administrative surcharge as set forth in Section 2.19.

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- 5.4. Ancillary Charges (Cont'd)
 - 5.4.9. Any port connections to a Company switch or a Company video hub switch with respect to Customer's First-Mile and Last-Mile Circuits shall collectively be referred to as "Switchport(s)" for the purposes of this Tariff. If Switchports are in demand so that it limits, in Company's sole discretion, Company's ability to fulfill other customer's requests, Company shall give Customer the option to vacate the Switchport(s) or Customer agrees that it shall use, in the aggregate, the monetary equivalent of five (5) hours of Occasional Service for each Switchport used by Customer each month or pro rata portion thereof ("Switchport Commitment"). In the event Customer does not incur actual charges for Occasional Service in excess of the aggregate Switchport Commitment for any month, Customer shall pay Company, for each such month, the difference between such actual charges and the aggregate Switchport Commitment ("Deficiency Charge"). The foregoing provision represents a good faith estimate of, and bears a reasonable relationship to, the actual damages of Company in the event of such deficiency and does not represent a penalty.
 - 5.4.10. Collocation charges apply when a Customer contracts with Company to utilize space in a POP for placement of Customer owned and maintained equipment associated with Services Company provides. Collocation Services are not currently available under this Tariff. If Company does provide Collocation Services, all pricing for collocation including: floor space, power, rack space, cross-connect panels, etc., will be based on Customer requirements and filed as separate charges in this Tariff.
 - 5.4.11. All ancillary charges are in addition to any similar charges incurred from any third party vendor which shall be passed on to Customer plus an administrative surcharge as set forth in Section 2.19.

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- 5.4. Ancillary Charges (Cont'd)
 - 5.4.12. Service Premium Charges

Service premium charges allow Customer to further enhance their reservations with the Company.

5.4.12.A. Non-Preemptible Service

Non-Preemptible Service is a premium enhancement which provides security from preemption due to network events as set forth in Section 2.18.

Non-Preemptible Interexchange Service Charge Total charge for Preemptible IXC Service multiplied by 1.5

5.4.12.B. Redundant Routing

Redundant Routing may be provided by Company, if Available, as an option to Customer who wants to ensure a higher level of protection in delivering critical transmission signals. Redundant Routing is provided for Point-to-Point Service, only. Redundant Routing provides for a second IXC path between the same origination and destination POPs.

Redundant Routing Charge
One charge is applied to both IXC paths at a rate equal to the total charge for the relevant one (1) Interexchange Circuit multiplied by 2.0

- 5.5. First-Mile/Last-Mile Service Charges and Administrative Surcharge
 - 5.5.1. First-Mile/Last-Mile Service charges are subject to the provisions of Section 2.2.11. The rate information relevant to the First-Mile/Last-Mile Service charges are available from the relevant First-Mile or Last-Mile Service Provider.
 - 5.5.2. Customer shall be subject to charges, including an administrative surcharge as set forth in Section 2.19 for any facilities procured by Company on behalf of Customer from third party providers as set forth in Section 2.19.

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SECTION 6 -- ADDITIONAL SERVICE OFFERINGS

6.1. ImageNet

6.1.1. Description of Service - ImageNet Service provides for the transmission of 45 Mbps component digital video signals as specified in CCIR601 4:2:2, and the provision of four associated 15 Kbz audio channels between Company's network POPs.

ImageNet Service requires a DS-3 digital local access channel between Company and Customer sites transmitting a compressed D-1 signal and adhering to ANSI T1.102 & T1.105 1988 specifications. Customer premise equipment for encoding and decoding is not included.

6.1.2. Terms and Conditions - ImageNet is available as a one-way or two-way occasional or dedicated service as provided and defined in Sections 1, 2, 4, 5, 7, 8 and 9 of this Tariff.

The company will provide DS-3 level interexchange network support and circuit routing for ImageNet Service.

- 6.1.3. Occasional Service -
 - 6.1.3.1. Base Rates, Point to Point Transmissions

	One	Two
	Way	Way
15 minutes	\$140	\$210
30 minutes	\$250	\$375
45 minutes	\$360	\$540
60 minutes	\$440	\$660

Reservations greater than 60 minutes will be billed at the prorated 60 minute rate, in 15 minute increments following the first 60 minutes.

- 6.1.3.2. Point to Multipoint Transmissions Drop-off service is provided as set forth in Section 5.3.3 of this Tariff. The charge for each additional site is \$50 per hour, prorated in 15 minute increments following the first 60 minutes.
- 6.1.3.3. PGAD/Secondary Drop-off PGAD/Secondary drop-offs are \$75 per hour, prorated in 15-minute increments following the first 60 minutes.
- 6.1.4. Dedicated Service ImageNet can be used on a full-time dedicated basis as defined in Section 4 of this Tariff.

SECTION 6 -- ADDITIONAL SERVICE OFFERINGS (Cont'd)

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- 6.2. Hub Reservation Management Service
 - 6.2.1. Description of Services. Under Hub Reservation Management Service ("HRMS") Company provides for the reservation, troubleshooting support and billing of Hub circuit Cross Connects for Company broadcast video traffic between the Company and the Customer via a Hub vendor. Customers that are not active Hub Reservation Management Service Customers will not receive this support.
 - 6.2.2. Terms & Conditions. Hub Reservation Management Service is available on a full-time basis only for all Services provided by Company. Customers may order Hub Reservation Management Service upon three business days written notice and under a signed Agreement. Once the Customer receives HRMS, the Company will be the agent for the Customer at all video Hubs where Hub Reservations are required as a result of using services provided by the Company. Hub Reservation Management Service can be canceled with one business day written notice to Company's Traffic Department.

Hub Reservation Management Service is only applicable at Hubs where the Company has local connectivity. Hub Reservation Management Service is provided on an as-facilities-exist basis.

- 6.2.3. Rates. Hub Reservation Management Service will be billed either on a Switched-basis or on a Usage-basis, depending on the type of charge received from the respective Hub vendor, if any. The Company reserves the right to change rates for this Service from time to time as set forth in this Tariff. In the event that a Hub charges on both a Switched- and Usage-basis, both charges will apply.
 - 6.2.3.A. Switched-based Charge: Charges applied only once per Hub reservation and do not recur for the duration of such reservation:

Charge per Switch-based Hub reservation: \$25

 Usage-based Charge: Charge applied in half-hour increments, or fraction thereof, for Hub reservations:

Charge per Usage-based Hub reservation: \$45.00 per half-hour

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SECTION 7 - SPECIAL PROMOTIONAL OFFERINGS

7.1. General Service Promotion

The Company shall from time to time provide Customers with one or a combination of the following General Service Promotion offerings designed to attract new subscribers or to increase subscriber awareness of a particular Tariff offering, or to retain subscribers as follows: (A) with respect to Dedicated Service a credit up to one month's recurring Dedicated Interexchange Service charge net of all discounts per year of the Term; (B) waive or reduce Company's Installation charges; (C) waive or reduce the Installation charges for First-Mile/Last-Mile Service associated with Interexchange Service; and/or (D) waive or reduce certain Ancillary Charges. These General Service Promotions may be limited to certain dates, times, Services, Availability and geographical areas at the sole discretion of Company.

7.2. Volume Commitment Promotion

From time to time Company shall provide Customers, which have made volume commitments to order Interexchange Service, with at least five (5) hours of One-Way, Interexchange Service or at least two and one half (2 ½) hours of Two-Way, Interexchange Service at no charge. This Volume Commitment Promotion may be limited to certain dates, times, Services, Availability and geographical areas at the sole discretion of Company.

Demonstration Promotion

From time to time at Company's discretion, Company shall provide Customers with Service at no charge for the purpose of demonstrating such Service. This Demonstration Promotion may be limited to certain dates, times, Services, Availability and geographical areas at the sole discretion of Company.

7.4. Notice

The Company shall provide thirty (30) days' notice to the Florida Public Service Commission before offering promotions to customers.

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SECTION 8 -- OCCASIONAL SERVICE AVAILABILITY

Subject to the terms and conditions of this Tariff (including provisions relating to Availability), the Company serves the following cities in Florida:

Jacksonville Miami Orlando Tampa

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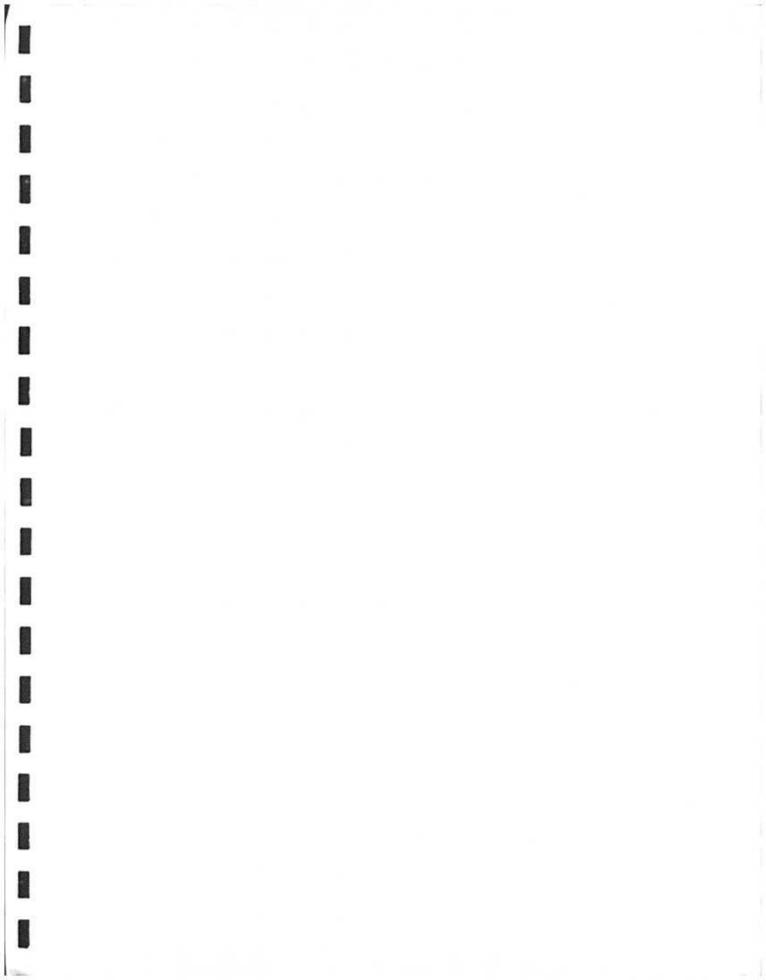
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