BLACK HILLS CORP /SD/
Form 10-Q
November 09, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2006.

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES ACT OF 1934
For the transition period from __________ to __________.

Commission File Number 001-31303

Black Hills Corporation
Incorporated in South Dakota IRS Identification Number 46-0458824
625 Ninth Street
Rapid City, South Dakota 57701

Registrant s telephone number (605) 721-1700

Former name, former address, and former fiscal year if changed since last report
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 x No o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer	x	Accelerated filer	o	Non-accelerated filer	o

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes	o	No	x

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

Class	Outstanding at October 31, 2006
Common stock, $1.00 par value	33,313,142 shares

TABLE OF CONTENTS

BLACK HILLS CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
	(in thousands, except per share amounts)			
Operating revenues	$ 157,608	$ 149,008	$ 483,312	$ 433,813
Operating expenses:				
Fuel and purchased power	47,740	49,758	151,150	134,849
Operations and maintenance	16,490	18,014	60,566	55,071
Administrative and general	19,721	21,669	64,776	60,403
Depreciation, depletion and amortization	24,141	22,039	67,407	62,362
Taxes, other than income taxes	8,570	8,869	26,667	25,483
Project development cost write - off		8,931		9,495
Impairment of long-lived assets		50,279		50,279
	116,662	179,559	370,566	397,942
Operating income (loss)	40,946	(30,551)	112,746	35,871
Other income (expense):				
Interest expense	(12,400)	(11,089)	(37,310)	(36,421)
Interest income	389	331	1,403	1,294
Other income, net	106	139	517	819
	(11,905)	(10,619)	(35,390)	(34,308)
Income (loss) from continuing operations before equity in earnings of unconsolidated subsidiaries, minority interest and income taxes	29,041	(41,170)	77,356	1,563
Equity in earnings of unconsolidated subsidiaries	615	3,434	(16)	7,788
Minority interest	(95)	(74)	(273)	(199)
Income tax (expense) benefit	(7,362)	14,026	(23,939)	(2,367)
Income (loss) from continuing operations	22,199	(23,784)	53,128	6,785
Income (loss) from discontinued operations, net of taxes	81	(119)	7,060	22
Net income (loss)	22,280	(23,903)	60,188	6,807
Preferred stock dividends				(159)
Net income (loss) available for common stock	$ 22,280	$ (23,903)	$ 60,188	$ 6,648
Weighted average common shares outstanding:				
Basic	33,187	32,967	33,157	32,660
Diluted	33,560	32,967	33,526	33,100
Earnings (loss) per share:				
Basic				
Continuing operations	$ 0.67	$ (0.73)	$ 1.60	$ 0.20
Discontinued operations			0.21	
Total	$ 0.67	$ (0.73)	$ 1.81	$ 0.20
Diluted				

Continuing operations	$ 0.66	$ (0.73)	$ 1.59	$ 0.20
Discontinued operations			0.21	
Total	$ 0.66	$ (0.73)	$ 1.80	$ 0.20
Dividends paid per share of common stock	$ 0.33	$ 0.32	$ 0.99	$ 0.96

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

BLACK HILLS CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(unaudited)

	September 30, 2006	December 31, 2005	September 30, 2005
	(in thousands, except share amounts)		
ASSETS			
Current assets:			
Cash and cash equivalents	$ 47,716	$ 31,817	$ 46,060
Restricted cash			700
Receivables (net of allowance for doubtful accounts of $4,007; $4,685 and $4,317, respectively)	195,571	264,695	240,110
Materials, supplies and fuel	91,490	122,521	179,387
Derivative assets	66,990	20,681	33,184
Income tax receivable	11,524		
Deferred income taxes			6,803
Other assets	7,830	7,842	6,666
Assets of discontinued operations	1,043	122,158	119,019
	422,164	569,714	631,929
Investments	23,709	27,558	24,906
Property, plant and equipment	2,180,639	1,928,559	1,898,313
Less accumulated depreciation and depletion	(574,925)	(518,525)	(510,401)
	1,605,714	1,410,034	1,387,912
Other assets:			
Derivative assets	3,197	1,898	4,722
Goodwill	30,563	29,847	28,455
Intangible assets (net of accumulated amortization of $25,072; $22,734 and $21,954, respectively)	25,209	27,548	28,328
Other	38,177	53,646	47,391
	97,146	112,939	108,896
	$ 2,148,733	$ 2,120,245	$ 2,153,643
LIABILITIES AND STOCKHOLDERS EQUITY			
Current liabilities:			
Accounts payable	$ 181,255	$ 202,639	$ 192,202
Accrued liabilities	82,098	72,514	71,610
Derivative liabilities	18,937	26,141	114,941
Deferred income taxes	5,001	1,443	
Notes payable	147,000	55,000	42,000
Current maturities of long-term debt	17,103	11,771	11,690
Accrued income taxes		11,650	16,022
Liabilities of discontinued operations	4,131	92,818	86,720
	455,525	473,976	535,185
Long-term debt, net of current maturities	632,295	670,193	672,770
Deferred credits and other liabilities:			
Deferred income taxes	170,286	134,533	128,798
Derivative liabilities	2,913	2,623	6,096
Other	101,819	95,116	90,853
	275,018	232,272	225,747
Minority interest in subsidiaries	5,198	4,925	5,034
Stockholders equity:			
Common stock equity			
Common stock $1 par value; 100,000,000 shares authorized; Issued 33,330,841; 33,222,522 and 33,200,699 shares, respectively	33,331	33,223	33,201

Additional paid-in capital	407,488	404,035	403,822
Retained earnings	338,420	313,217	297,204
Treasury stock at cost 34,720; 66,938 and 73,805 shares, respectively	(883)	(1,766)	(1,909)
Accumulated other comprehensive income (loss)	2,341	(9,830)	(17,411)
	780,697	738,879	714,907
	$ 2,148,733	$ 2,120,245	$ 2,153,643

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

4

BLACK HILLS CORPORATION

CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

(unaudited)

	Nine Months Ended September 30, 2006	2005
	(in thousands)	
Operating activities:		
Income from continuing operations	$ 53,128	$ 6,785
Adjustments to reconcile income from continuing operations to net cash provided by operating activities:		
Depreciation, depletion and amortization	67,407	62,362
Impairment of long-lived assets		50,279
Net change in derivative assets and liabilities	2,136	2,894
Deferred income taxes	32,042	(17,617)
Distributed earnings in associated companies	4,304	1,954
Change in operating assets and liabilities, net of acquisition-		
Materials, supplies and fuel	(6,389)	(19,058)
Accounts receivable and other current assets	59,005	(14,068)
Accounts payable and other current liabilities	(61,878)	39,932
Other operating activities	26,239	15,489
Net cash provided by operating activities of continuing operations	175,994	128,952
Net cash (used in) provided by operating activities of discontinued operations	(1,583)	5,276
Net cash provided by operating activities	174,411	134,228
Investing activities:		
Property, plant and equipment additions	(153,820)	(86,897)
Proceeds from sale of assets		103,010
Payment for acquisition, net of cash acquired	(75,425)	(67,331)
Other investing activities	(454)	5,615
Net cash used in investing activities of continuing operations	(229,699)	(45,603)
Net cash provided by (used in) investing activities of discontinued operations	40,160	(6,966)
Net cash used in investing activities	(189,539)	(52,569)
Financing activities:		
Dividends paid	(32,954)	(31,612)
Common stock issued	3,560	12,822
Increase in short-term borrowings, net	92,000	18,000
Long-term debt issuances	90,000	
Long-term debt repayments	(122,566)	(91,675)
Other financing activities	(1,171)	(730)
Net cash provided by (used in) financing activities of continuing operations	28,869	(93,195)
Net cash used in financing activities of discontinued operations		
Net cash provided by (used in) financing activities	28,869	(93,195)
Increase (decrease) in cash and cash equivalents	13,741	(11,536)
Cash and cash equivalents:		
Beginning of period	34,198*	64,507**
End of period	$ 47,939*	$ 52,971**
Supplemental disclosure of cash flow information:		
Non-cash investing and financing activities-		
Property, plant and equipment acquired with accrued liabilities	$ 31,481	$ 9,711
Cash paid during the period for-		
Interest	$ 35,317	$ 31,551
Net income taxes paid	$ 12,806	$ 2,403

___

*Includes approximately $0.2 million at September 30, 2006 and $2.4 million at December 31, 2005 of cash included in discontinued operations.

**Includes approximately $6.9 million at September 30, 2005 and $8.6 million at December 31, 2004 of cash included in discontinued operations.

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

BLACK HILLS CORPORATION

Notes to Condensed Consolidated Financial Statements

(unaudited)

(Reference is made to Notes to Consolidated Financial Statements

included in the Company s 2005 Annual Report on Form 10-K)

(1) MANAGEMENT S STATEMENT

The financial statements included herein have been prepared by Black Hills Corporation (the Company) without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations; however, the Company believes that the footnotes adequately disclose the information presented. These financial statements should be read in conjunction with the financial statements and the notes thereto, included in the Company s 2005 Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC).

Accounting methods historically employed require certain estimates as of interim dates. The information furnished in the accompanying financial statements reflects all adjustments which are, in the opinion of management, necessary for a fair presentation of the September 30, 2006, December 31, 2005 and September 30, 2005 financial information and are of a normal recurring nature. Some of the Company s operations are highly seasonal and revenues from, and certain expenses for, such operations may fluctuate significantly among quarterly periods. Demand for natural gas is sensitive to seasonal heating and industrial load requirements, as well as changes in market price. The results of operations for the three and nine months ended September 30, 2006, are not necessarily indicative of the results to be expected for the full year. All earnings per share amounts discussed refer to diluted earnings per share unless otherwise noted.

(2) RECLASSIFICATIONS

Certain 2005 amounts in the financial statements have been reclassified to conform to the 2006 presentation. These reclassifications include reflecting a net presentation for derivative assets and liabilities that are subject to master netting agreements which provide for the legal right of offset of amounts due to and due from the same counterparty under the agreement. At September 30, 2005, current derivative assets and current derivative liabilities on the accompanying Condensed Consolidated Balance Sheet have been reduced by approximately $133.5 million and non-current derivative assets and non-current derivative liabilities have been reduced by approximately $1.7 million to reflect the legal right of offset and conform to the December 31, 2005 and September 30, 2006 presentation. These reclassifications did not have an effect on the Company s total stockholders equity or net income available for common stock as previously reported.

(3) RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS

SFAS No. 123 (Revised 2004)

On December 16, 2004, the Financial Accounting Standards Board, or FASB, issued FASB Statement No. 123 (Revised 2004) Share-Based Payment, or SFAS 123(R), which is a revision of SFAS Statement No. 123, Accounting for Stock-Based Compensation (SFAS 123). SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values.

The Company previously accounted for its employee equity compensation stock option plans under the provisions of APB No. 25 and no stock-based employee compensation cost is reflected in net income for the three and nine month periods ended September 30, 2005 for stock options.

As of January 1, 2006, the Company applied the provisions of SFAS 123(R) using the modified prospective method, recognizing compensation expense for all awards granted after the date of adoption and for the unvested portion of previously granted awards that were outstanding at the date of adoption. Adoption of SFAS 123(R) did not have a significant effect on the Company s consolidated financial position, results of operations or cash flows. See Note 11, Common Stock, for further discussion of stock-based compensation plans.

EITF Issue No. 04-6

On March 17, 2005, the Emerging Issues Task Force (EITF) issued EITF Issue No. 04-6, Accounting for Stripping Costs Incurred during Production in the Mining Industry (EITF 04-6). EITF 04-6 provides that stripping costs incurred during the production phase of a mine are variable production costs that should be included in the costs of the inventory produced during the period that the stripping costs are incurred. EITF 04-6 is effective for the first reporting period in fiscal years beginning after December 15, 2005. Upon adoption of EITF 04-6 on January 1, 2006, the Company recorded a $2.0 million cumulative effect adjustment to write-off previously recorded deferred charges, with the offset decreasing retained earnings. Additionally, since January 1, 2006, stripping costs are expensed at the time incurred.

EITF Issue No. 04-13

On September 28, 2005 the FASB ratified the consensus reached under EITF Issue No. 04-13, Accounting for Purchases and Sales of Inventory with the Same Counterparty, (EITF 04-13) which determines if such transactions should be reported on a gross basis or a net basis.

EITF 04-13 is effective for new arrangements entered into, and modifications or renewals of existing arrangements, in reporting periods beginning after March 16, 2006. The adoption did not have a significant effect on the Company s consolidated financial position, results of operations or cash flows.

7

(4) RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

SFAS No. 157

During September 2006 the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS 157) and applies under other accounting pronouncements that require or permit fair value measurements. This Statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP), and expands disclosures about fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. Management is currently evaluating the impact SFAS 157 will have on the Company s consolidated financial statements.

SFAS No. 158

During September 2006 the FASB issued Statement of Financial Accounting Standards No. 158 Employers Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106 and 132(R) (SFAS 158). This Statement requires the recognition of the overfunded or underfunded status of defined benefit postretirement plans as an asset or liability in the statement of financial position, recognition of changes in the funded status in comprehensive income, measurement of the funded status of a plan as of the date of the year-end statement of financial position, and provides for related disclosures. SFAS 158 is effective for the recognition of the funded status as an asset or liability in the statement of financial position, recognition of changes in the funded status in comprehensive income, and the related disclosures in financial statements issued for fiscal years ending after December 15, 2006. Effective for fiscal years ending after December 15, 2008, SFAS 158 will require the measurement of the funded status of the plan to coincide with the date of the year end statement of financial position. Management is currently evaluating the impact SFAS 158 will have on the Company s consolidated financial statements.

FIN 48

During June 2006 the FASB issued FASB Interpretation No. 48 Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement 109 (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with FASB Statement No. 109 Accounting for Income Taxes (FAS 109) and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 is effective for fiscal years beginning after December 15, 2006 with the impact of adoption to be reported as a cumulative effect of an accounting change. Management is currently evaluating the impact FIN 48 will have on the Company s consolidated financial statements.

SAB No. 108 Effects of Prior Year Misstatements on Current Year Financial Statements

During September 2006 the staff of the SEC released SAB No. 108 on Considering the Effects of Prior Year Misstatements When Quantifying Misstatements in Current Year Financial Statements. SAB No. 108 provides guidance on how the effects of the carryover or reversal of prior year financial statement misstatements should be considered in quantifying a current year misstatement. Prior practice allowed the evaluation of materiality on the basis of (1) the error quantified as the amount by which the current year income statement was misstated (rollover method) or (2) the cumulative error quantified as the cumulative amount by which the current year balance sheet was misstated (iron curtain method). Reliance on either method in prior years could have resulted in misstatement of the financial statements. The guidance provided in SAB No. 108 requires both methods to be used in evaluating materiality. Immaterial prior year errors may be corrected with the first filing of prior year financial statements after adoption. The cumulative effect of the correction can either be reported in the carrying amounts of assets and liabilities as of the beginning of that fiscal year, and the offsetting adjustment made to the opening balance of retained earnings for that year, or by restating prior periods. Appropriate disclosure of the nature and amount of each individual error being corrected in the cumulative adjustment, as well as a disclosure of when and how each error being corrected arose and the fact that the errors had previously been considered immaterial. SAB No. 108 is effective January 1, 2007. Management is currently evaluating the impact this bulletin might have on the Company s consolidated financial statements.

(5) MATERIALS, SUPPLIES AND FUEL

The amounts of materials, supplies and fuel included on the accompanying Condensed Consolidated Balance Sheets, by major classification, are provided as follows (in thousands):

Major Classification	September 30, 2006	December 31, 2005	September 30, 2005
Materials and supplies	$ 30,160	$ 24,567	$ 24,435
Fuel	9,387	7,544	8,745
Gas held by energy marketing*	51,943	90,410	146,207
Total materials, supplies and fuel	$ 91,490	$ 122,521	$ 179,387

* As of September 30, 2006, December 31, 2005 and September 30, 2005, market adjustments related to natural gas held by energy marketing and recorded in inventory were $(29.8) million, $6.6 million and $61.0 million, respectively.

The gas inventory held by the Company s energy marketing subsidiary is held under various contractual storage arrangements. The gas is being held in inventory to capture the price differential between the time at which it was purchased and a sales date in the future. A substantial majority of the gas was economically hedged at the time of purchase either through a fixed price physical or financial forward sale.

(6) LONG-TERM DEBT AND GUARANTEES

On July 12, 2006 the Company s subsidiary, Black Hills Colorado, LLC, entered into a Second Amended and Restated Credit Agreement to refinance the floating rate project debt for the Valmont and Arapahoe plants in the amount of $90.0 million. The maturity date of the amortizing borrowings is July 2013. In conjunction with the refinancing, the Company made a payment in the amount of $21.3 million on the $111.3 million principal outstanding at June 30, 2006 and expensed approximately $0.7 million of unamortized deferred finance costs associated with the First Amended and Restated Credit Agreement. In addition, as of July 12, 2006, the Company has guaranteed during the term of the debt the payment obligations of Black Hills Colorado, LLC, to the Bank of Nova Scotia, as administrative agent under the Credit Agreement, for up to $30 million. The cost of borrowings under the facility is determined based upon the Company s corporate credit ratings; at the current ratings levels, the facility has a borrowing spread on Eurodollar loans of 87.5 basis points over LIBOR (which equates to a 6.25 percent, three-month borrowing rate as of September 30, 2006).

On May 24, 2006 the Company entered into an Amended and Restated Credit Agreement for the project financing floating rate debt for Wygen I. The agreement extended the maturity date of the $111.1 million tranche of the financing from June 2006 to June 2008 to coincide with the maturity date of the remaining $17.2 million tranche. The cost of borrowings under the financing is determined based upon the Company s corporate credit ratings; at the Company s current ratings levels, the financing has a borrowing spread on Eurodollar loans of 62.5 basis points over LIBOR (which equates to a 5.95 percent, one-month borrowing rate as of September 30, 2006). In conjunction with the Amended and Restated Credit Agreement, the Company entered into an Amended and Restated Guarantee in favor of Wygen Funding, Limited Partnership, which continues the Company s guarantee obligations under the Wygen I plant lease.

In addition to the guarantees discussed above, during the nine months ended September 30, 2006 the Company had the following changes to its guarantees:

Issued and amended a Guarantee for payment under various transactions by Cheyenne Light with Tenaska Marketing Ventures for $2.0 million, expiring in 2007.

Extinguished a guarantee of up to $3.0 million of Enserco Energy Inc. s obligations to Fortis Capital Corp. and other lenders under its credit facility.

Expiration of a guarantee of an interest rate swap transaction with Union Bank of California.

At September 30, 2006, we had guarantees totaling $187.9 million in place.

(7) EARNINGS PER SHARE

Basic earnings per share from continuing operations is computed by dividing income from continuing operations by the weighted-average number of common shares outstanding during the period. Diluted earnings per share from continuing operations gives effect to all dilutive common shares potentially outstanding during a period. A reconciliation of Income from continuing operations and basic and diluted share amounts is as follows (in thousands):

Period ended September 30, 2006	Three Months		Nine Months	
	Income	Average Shares	Income	Average Shares
Income from continuing operations	$ 22,199		$ 53,128	
Basic available for common shareholders	22,199	33,187	53,128	33,157
Dilutive effect of:				
Stock options		91		85
Estimated contingent shares issuable for prior acquisition		158		158
Others		124		126
Diluted available for common shareholders	$ 22,199	33,560	$ 53,128	33,526

Period ended September 30, 2005	Three Months		Nine Months	
	Income	Average Shares	Income	Average Shares
Income (loss) from continuing operations	$ (23,784)		$ 6,785	
Less: preferred stock dividends			(159)	
Basic available for common shareholders	(23,784)	32,967	6,626	32,660
Dilutive effect of:				
Stock options				164
Estimated contingent shares issuable for prior acquisition				158
Others				118
Diluted available for common shareholders	$ (23,784)	32,967	$ 6,626	33,100

(8) COMPREHENSIVE INCOME

The following table presents the components of the Company s comprehensive income (loss)

(in thousands):

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Net income (loss)	$ 22,280	$ (23,903)	$ 60,188	$ 6,807
Other comprehensive income (loss), net of tax:				
Fair value adjustment on derivatives designated as cash flow hedges	7,425	(11,095)	12,587	(15,260)
Reclassification adjustments on cash flow hedges settled and included in net income	(246)	3,262	(416)	5,441
Unrealized gain on available-for-sale securities				15
Comprehensive income (loss)	$ 29,459	$ (31,736)	$ 72,359	$ (2,997)

(9) INCOME TAXES

The Company s effective tax rates differ from the federal statutory rate as follows:

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
	35.0%	35.0%	35.0%	35.0%
State income tax	0.3	1.1	0.5	(2.1)
Percentage depletion in excess of cost	(1.5)	0.7	(1.3)	(6.0)
IRS exam tax adjustment*	(7.3)		(2.8)	
Tax return true-up	(1.3)	1.5	(0.5)	(4.5)
Other	(0.3)	(1.2)	0.2	3.5
	24.9%	37.1%	31.1%	25.9%

---

* As a result of the settlement of an Internal Revenue Service (IRS) exam of the tax years 2001-2003 with respect to certain tax positions taken by the Company, a reduction to income tax expense of approximately $2.2 million was recorded in the third quarter of 2006.

(10) PROCEEDS RECEIVED ON INSURANCE CLAIMS

In late 2005 and the first half of 2006, the Company s Las Vegas II power plant experienced unplanned outages due to damage to three of its gas turbines and two of its steam turbines. The outages lasted approximately six months as repairs were made to the turbines. The Company has filed insurance claims for reimbursement of repair expenditures and business interruption losses in the amount of approximately $11.1 million. At September 30, 2006, the Company has provided for the receipt of insurance proceeds of approximately $4.3 million. Approximately $0.4 million was applied to reduce capitalized repair costs included in Property, plant and equipment on the accompanying Condensed Consolidated Balance Sheet and $2.2 million for repair costs and $1.7 million for business interruption were applied as a reduction to Operations and maintenance expense on the accompanying Condensed Consolidated Statement of Income. While the Company is pursuing additional reimbursement from the insurance carrier, the carrier asserts that certain deductibles, exclusions and limitations apply preventing any future claims reimbursements. There can be no assurance that the Company will obtain any additional recovery from the insurance carrier.

(11) COMMON STOCK

Equity Compensation Plans

The Company has several employee equity compensation plans, which allow for the granting of stock, restricted stock, restricted stock units, stock options and performance shares. The Company has 1,082,894 shares available to grant at September 30, 2006.

At September 30, 2006, the Company had one stock-based employee compensation plan under which it can grant stock options to its employees and three prior plans with stock options outstanding. Prior to January 1, 2006, the Company accounted for these plans under the recognition and measurement principles of Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees (APB 25), and related interpretations. Prior to 2006, no stock-based compensation expense related to stock options was reflected in net income as all options granted had an exercise price equal to the market value of the underlying common stock on the date of grant. However, the Company did recognize stock-based compensation expense for other non-vested share awards including restricted stock and restricted stock units, performance shares and directors phantom shares.

The following table illustrates the effect on net income (loss) and earnings (loss) per share if the Company had applied the fair value recognition provisions of SFAS 123 to stock-based employee compensation (in thousands, except per share amounts):

	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2005
Net (loss) income available for common stock, as reported	$ (23,903)	$ 6,648
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(126)	(389)
Pro forma net income available for common stock	$ (24,029)	$ 6,259
Earnings (loss) per share:		
Basic as reported		
Continuing operations	$ (0.73)	$ 0.20
Discontinued operations		
Total	$ (0.73)	$ 0.20
Diluted as reported		
Continuing operations	$ (0.73)	$ 0.20
Discontinued operations		
Total	$ (0.73)	$ 0.20
Basic pro-forma		
Continuing operations	$ (0.73)	$ 0.19
Discontinued operations		
Total	$ (0.73)	$ 0.19
Diluted pro-forma		
Continuing operations	$ (0.73)	$ 0.19
Discontinued operations		
Total	$ (0.73)	$ 0.19

On January 1, 2006 the Company adopted the fair value recognition provisions of SFAS 123(R) requiring the recognition of expense related to the fair value of stock-based compensation awards. The Company elected the modified prospective transition method. Under this method, compensation expense is recognized for all stock-based awards granted prior to, but not yet vested as of January 1, 2006 and all stock-based awards granted subsequent to January 1, 2006. Adoption of SFAS 123(R) did not have a material effect on the Company s consolidated financial position, results of operations or cash flows. Compensation expense is determined using the grant date fair value estimated in accordance with the provisions of SFAS 123(R) and is recognized over the vesting periods of the individual plans. Total stock-based compensation expense for the three months ended September 30, 2006 and 2005 was $0.1 million ($0.1 million, after tax) and $1.1 million ($0.7 million, after tax), respectively, and for the nine months ended September 30, 2006 and 2005 was $1.8 million ($1.2 million, after tax) and $3.1 million ($2.0 million, after tax), respectively, and is included in administrative and general expense on the accompanying Condensed Consolidated Statements of Income. In accordance with the modified prospective transition method of SFAS 123(R), financial results for prior periods have not been restated. As of September 30, 2006, total unrecognized compensation expense related to stock options and other non-vested stock awards is $3.5 million and is expected to be recognized over a weighted-average period of 1.8 years.

In November 2005, the FASB issued FASB Staff Position (FSP) No. FAS 123 (R)-3, Transition Election Related to Accounting for the Tax Effects of Share-Based Payment Awards. FSP 123(R)-3 provides an alternative method of calculating the excess tax benefits available to absorb tax deficiencies recognized subsequent to the adoption of SFAS 123(R). The calculation of excess tax benefits reported as an operating cash outflow and a financing inflow in the Consolidated Statements of Cash Flows required by FSP No. 123(R)-3 differs from that required by SFAS 123(R). The Company has until January 1, 2007 to make a one-time election to adopt the transition method described in FSP No. 123 (R)-3. The Company is currently evaluating FSP No. FAS 123 (R)-3; however, the one-time election is not expected to affect the Company s results of operations.

Stock Options

The Company has granted options with an option exercise price equal to the fair market value of the stock on the day of the grant. The options granted vest one-third each year for three years and expire after ten years from the grant date.

A summary of the status of the stock option plans at September 30, 2006 is as follows:

	Shares (in thousands)	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Balance at January 1, 2006	854	$ 29.56		
Granted	15	33.17		
Forfeited/cancelled	(18)	33.53		
Expired				
Exercised	(71)	27.99		
Balance at September 30, 2006	780	$ 29.68	5.5	$ 3,066
Exercisable at September 30, 2006	680	$ 29.58	5.1	$ 2,739

The weighted-average grant-date fair value of options granted during the nine months ended September 30, 2006 and 2005 was $3.79 and $6.93, respectively. The total intrinsic value of options (the amount by which the market price of the stock on the date of exercise exceeded the exercise price of the option) exercised during the nine months ended September 30, 2006 and 2005 was $0.5 million and $5.1 million, respectively. The total fair value of shares vested during each of the nine months ended September 30, 2006 and 2005 was $0.4 million and $0.7 million, respectively.

The fair value of share-based awards is estimated on the date of grant using the Black-Scholes option pricing model. The fair value is affected by the Company s stock price as well as a number of assumptions. The assumptions used to estimate the fair value of share-based awards are as follows:

Valuations Assumptions[1]	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Weighted average risk-free interest rate[2]	4.94%	3.90%
Weighted average expected price volatility[3]	21.54%	42.27%
Weighted average expected dividend yield[4]	3.98%	4.17%
Expected life in years[5]	7	7

[1] Forfeitures are estimated using historical experience and employee turnover.

[2] Based on treasury interest rates with terms consistent with the expected life of the options.

[3] Based on a blended historical and implied volatility of the Company s stock price in 2006 and historical volatility only in 2005.

[4] Based on the Company s historical and expectation of future dividend payouts and may be subject to substantial change in the future.

[5] Based upon historical experience.

Net cash received from the exercise of options for the nine months ended September 30, 2006 and 2005 was $2.0 million and $10.0 million, respectively. The tax benefit realized from the exercise of shares granted for the nine months ended September 30, 2006 and 2005 was $0.2 million and $1.8 million, respectively, and was recorded as an increase to equity.

As of September 30, 2006, there was $0.3 million of unrecognized compensation expense related to stock options that is expected to be recognized over a weighted-average period of 0.9 years.

Restricted Stock and Restricted Stock Units

The fair value of restricted stock and restricted stock unit awards equals the market price of the Company s stock on the date of grant.

The shares carry a restriction on the ability to sell the shares until the shares vest. The shares substantially vest one-third per year over three years, contingent on continued employment. Compensation cost related to the awards is recognized over the vesting period.

A summary of the status of the restricted stock and non-vested restricted stock units at September 30, 2006 is as follows:

	Stock And Stock Units (in thousands)	Weighted Average Grant Date Fair Value
Balance at January 1, 2006	90	$ 30.71
Granted	42	35.20
Vested	(37)	29.33
Forfeited	(2)	32.12
Balance at September 30, 2006	93	$ 33.25

The weighted-average grant-date fair value of restricted stock and restricted stock units granted in the nine months ended September 30, 2006 and 2005 was $35.20 and $30.03, per share, respectively. The total fair value of shares vested during the nine months ended September 30, 2006 and 2005 was $1.3 million and $1.2 million, respectively.

As of September 30, 2006, there was $2.0 million of unrecognized compensation expense related to non-vested restricted stock and non-vested restricted stock units that is expected to be recognized over a weighted-average period of 1.9 years.

Performance Share Plan

Certain officers of the Company and its subsidiaries are participants in a performance share award plan, a market-based plan. Performance shares are awarded based on the Company s total shareholder return over designated performance periods as measured against a selected peer group. In addition, the Company s stock price must also increase during the performance periods.

Participants may earn additional performance shares if the Company s total shareholder return exceeds the 50th percentile of the selected peer group. The final value of the performance shares may vary according to the number of shares of common stock that are ultimately granted based upon the performance criteria.

Outstanding Performance Periods at September 30, 2006 are as follows:

Grant Date	Performance Period	Target Grant of Shares (in thousands)
March 1, 2004	March 1, 2004 December 31, 2006	23
January 1, 2005	January 1, 2005 December 31, 2007	39
January 1, 2006	January 1, 2006 December 31, 2008	34

The performance awards are paid 50 percent in cash and 50 percent in common stock. The cash portion accrued is classified as a liability and the stock portion is classified as temporary equity. In the event of a change-in-control performance awards are paid 100 percent in cash. If it is ever determined that a change-in-control is probable, the equity portion will be reclassified as a liability. At September 30, 2006, the Company had $0.6 million of temporary equity.

A summary of the status of the Performance Share Plan at September 30, 2006 and changes during the nine-month period ended September 30, 2006, is as follows:

	Equity Portion		Liability Portion	
	Shares (in thousands)	Weighted-Average Grant Date Fair Value	Shares (in thousands)	Weighted-Average September 30, 2006 Fair Value
Balance at January 1, 2006	38	$ 29.95	38	
Granted	17	32.06	17	
Forfeited	(1)	29.95	(1)	
Vested	(6)	29.92	(6)	
Balance at September 30, 2006	48	$ 30.70	48	$ 23.61

The weighted-average grant-date fair value of performance share awards granted in the nine months ended September 30, 2006 and 2005 was $32.06 and $29.97, per share, respectively. The grant date fair value for the performance shares granted in 2006 was determined by Monte Carlo simulation using a blended volatility of 21 percent comprised of 50 percent historical volatility and 50 percent implied volatility and the average risk-free interest rate of the three-year U.S. Treasury security rate in effect as of the grant date. The grant date fair value for the performance shares issued in 2005 was equal to the market value of the common stock on the grant date.

During the nine months ended September 30, 2006, the Company issued 11,667 shares of common stock and paid $0.4 million for the Performance Period of March 1, 2004 to December 31, 2005, for a total intrinsic value of $0.8 million. The payout was fully accrued at December 31, 2005.

As of September 30, 2006, there was $1.2 million of unrecognized compensation expense related to outstanding performance share plans that is expected to be recognized over a weighted-average period of 1.8 years.

Other Plans

The Company issued 36,685 shares of common stock with an intrinsic value of $910,000 in the nine months ended September 30, 2006 to certain key employees under the Short-term Annual Incentive Plan, a performance-based plan. The payout was fully accrued at December 31, 2005.

(12) EMPLOYEE BENEFIT PLANS

Defined Benefit Pension Plan

The Company has two non-contributory defined benefit pension plans (Plans). One Plan covers employees of the Company and the following subsidiaries who meet certain eligibility requirements: Black Hills Service Company, LLC, Black Hills Power, Inc., Wyodak Resources Development Corp., and Black Hills Exploration and Production, Inc. The other Plan covers employees of the Company s subsidiary, Cheyenne Light, Fuel and Power Company, who meet certain eligibility requirements.

The components of net periodic benefit cost for the two Plans are as follows (in thousands):

	Three Months Ended September 30, 2006	2005	Nine Months Ended September 30, 2006	2005
Service cost	$ 649	$ 576	$ 1,947	$ 1,728
Interest cost	1,041	995	3,123	2,985
Expected return on plan assets	(1,247)	(1,157)	(3,741)	(3,471)
Amortization of prior service cost	38	54	114	162
Amortization of net loss	227	296	681	888
Net periodic benefit cost	$ 708	$ 764	$ 2,124	$ 2,292

The Company made a $1.2 million contribution to the Cheyenne Light Pension Plan in the first quarter of 2006; no additional contributions are anticipated to be made to the Plans during the 2006 fiscal year.

Supplemental Non-qualified Defined Benefit Plans

The Company has various supplemental retirement plans for key executives of the Company (Supplemental Plans). The Supplemental Plans are non-qualified defined benefit plans.

The components of net periodic benefit cost for the Supplemental Plans are as follows (in thousands):

	Three Months Ended September 30, 2006	2005	Nine Months Ended September 30, 2006	2005
Service cost	$ 87	$ 86	$ 261	$ 258

Interest cost	270	252	810	756
Amortization of prior service cost	3	2	9	6
Amortization of net loss	199	157	597	471
Net periodic benefit cost	$ 559	$ 497	$ 1,677	$ 1,491

The Company anticipates that it will need to make contributions to the Supplemental Plans for the 2006 fiscal year of approximately $0.7 million. The contributions are expected to be made in the form of benefit payments.

Non-pension Defined Benefit Postretirement Healthcare Plans

Employees who are participants in the Company s Postretirement Healthcare Plans (Healthcare Plans) and who meet certain eligibility requirements are entitled to postretirement healthcare benefits.

The components of net periodic benefit cost for the Healthcare Plans are as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005	2006	2005
Service cost	$ 164	$ 185	$ 492	$ 555
Interest cost	203	232	609	696
Amortization of net transition obligation	38	37	114	111
Amortization of prior service cost	(6)	(6)	(18)	(18)
Amortization of net loss		25		75
Net periodic benefit cost	$ 399	$ 473	$ 1,197	$ 1,419

The Company anticipates that it will make contributions to the Healthcare Plans for the 2006 fiscal year of approximately $0.2 million. The contributions are expected to be made in the form of benefits payments.

It has been determined that the Company s post-65 retiree prescription drug plans are actuarially equivalent and qualify for the Medicare Part D subsidy. The decrease in net periodic postretirement benefit cost due to the subsidy is as follows (in thousands):

	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2006
Service cost	$ (25)	$ (75)
Interest cost	(28)	(84)
Amortization of net loss	(18)	(54)
Total decrease to net periodic postretirement benefit cost	$ (71)	$ (213)

(13) IMPAIRMENT TESTING OF OIL AND NATURAL GAS PROPERTIES

The Company s oil and gas segment follows the full cost method of accounting for its oil and gas properties. Under the full cost method, costs related to acquisition, exploration and development drilling activities are capitalized. The net capitalized costs are subject to a ceiling test that limits these costs to the estimated present value of future net revenues from proved reserves based on a single day s spot market prices, and the lower of cost or fair value of unproved properties. Rules mandated by the Securities and Exchange Commission require that future net revenues be based on end-of-period spot market prices, with consideration for alternate prices only to the extent provided for by contractual arrangements, and discounted at a 10 percent interest rate. If the net capitalized costs exceed the full cost ceiling at period end, a permanent non-cash write-down would be required to be charged to earnings in that period unless subsequent market price changes eliminate or reduce the indicated write-down.

In accordance with the Company s full cost method of accounting for its oil and gas properties, we conducted our quarterly ceiling test as of September 30, 2006. Spot market prices for natural gas, particularly in the Rocky Mountain region where a predominant portion of the Company s reserves are located, experienced a drastic and brief decline at the end of the period ended September 30, 2006. If the spot market prices on September 28, 2006, the market trading date for September 30, 2006 natural gas deliveries, were used the ceiling limitation would have exceeded the Company s net capitalized costs and accordingly no ceiling test write-down would have been indicated. Average wellhead adjusted natural gas and crude oil prices on this date were $3.16 per Mcf and $55.39 per barrel, respectively. When using the spot market prices on September 29, 2006, the last market trading day of the period, the calculation resulted in an indicated $15.5 million pre-tax impairment of the Company s oil and gas properties at September 30, 2006. Average wellhead adjusted natural gas and crude oil spot prices used on this date in the ceiling test calculation were $2.79 per Mcf and $55.39 per barrel, respectively. The Company does not believe this short-term decline in natural gas prices impacts the long-term economic value of its oil and gas properties as its average reserve life is approximately 15 years with individual well lives ranging up to 40 years.

Subsequent to September 30, 2006 natural gas prices both nationwide and in the Rocky Mountain region increased significantly. In accordance with the full cost accounting rules the Company recalculated its full cost "ceiling" using November 2, 2006 average wellhead adjusted spot prices of $5.88 per Mcf and $48.69 per barrel, respectively. These prices resulted in a "ceiling" limit significantly in excess of the Company's net capitalized costs, thereby eliminating the need to take a charge to earnings and write-down the carrying value of the Company's oil and gas properties.

(14) IMPAIRMENT OF LONG-LIVED ASSETS AND CAPITALIZED DEVELOPMENT COSTS

Due to a significant increase in the long-term forecasts for natural gas prices during the third quarter of 2005, the operation of the Company s Las Vegas I gas-fired power plant (Las Vegas I) became uneconomic. Accordingly, the Company assessed the recoverability of the carrying value of Las Vegas I in accordance with the provisions of SFAS No. 144 Accounting for the Impairment of Long-lived Assets (SFAS 144).

Las Vegas I is a 53 megawatt, natural gas-fired, combined-cycle turbine operating under a contract as a qualifying facility as defined by the Public Utility Regulatory Policies Act of 1978. Under the contract, which extends through 2024, the Company sells capacity and energy to Nevada Power Company and accepts price risk associated with the plant s fuel requirements. While the Company s oil and gas exploration and production operation produces gas sufficient to cover the plant s fuel requirements thus providing an internal hedge, SFAS 144 requires the determination of asset impairment at each asset group which has separately identifiable cash flows.

The carrying value of the assets tested for impairment was $60.3 million. The assessment resulted in an impairment charge in September, 2005 of $50.3 million to write down the related Property, plant and equipment by $44.7 million, net of accumulated depreciation of $11.1 million, and intangible assets by $5.6 million, net of accumulated amortization of $1.5 million. This charge reflects the amount by which the carrying value of the facility exceeded its estimated fair value determined by its estimated future discounted cash flows. This charge is included as a component of Operating expenses on the accompanying Condensed Consolidated Statements of Income. Operating results from Las Vegas I are included in the Power Generation Segment.

In addition, during the three-month period ended September 30, 2005, the Company recorded an $8.9 million pre-tax charge for the write-off and expensing of certain capitalized costs for various energy development projects determined less likely to advance, and costs related to unsuccessfully bid projects during the third quarter of 2005. The Company determined these projects were less likely to advance, due to reduced economic feasibility of gas-fired power generation in the expected sustained high-priced natural gas environment, increased expectations of reliance on renewable or coal-fired generation, and a perceived preference of utilities in certain regions to acquire existing merchant generation at significant discounts as an alternative to entering into contracts for capacity and energy from new generation. These costs had been capitalized as management believed it was probable that such costs would ultimately result in acquisition or construction of the projects. This charge is included as a component of Operating expenses on the accompanying Condensed Consolidated Statements of Income. For segment reporting the development costs are included in Corporate results.

(15) SUMMARY OF INFORMATION RELATING TO SEGMENTS OF THE COMPANY S BUSINESS

The Company s reportable segments are those that are based on the Company s method of internal reporting, which generally segregates the strategic business groups due to differences in products, services and regulation. As of September 30, 2006, substantially all of the Company s operations and assets are located within the United States. On March 1, 2006, the Company completed the sale of the operating assets of Black Hills Energy Resources, Inc. and related subsidiaries, the Company s crude oil marketing and pipeline transportation business which for segment reporting was classified in the Energy marketing and transportation segment; and on June 30, 2005 the Company completed the sale of its subsidiary, Black Hills FiberSystems, Inc., which operated as the Company s Communications segment (see Note 19). The financial information of the related crude oil marketing and pipeline transportation business and communications segment has been reclassified into Discontinued operations on the accompanying condensed consolidated financial statements.

The Company conducts its operations through the following six reporting segments: Retail Services group consisting of the following segments: Electric utility, which supplies electric utility service to western South Dakota, northeastern Wyoming and southeastern Montana; and Electric and gas utility, acquired January 21, 2005, which supplies electric and gas utility service to Cheyenne, Wyoming and vicinity; and Wholesale Energy group, consisting of the following segments: Coal mining, which engages in the mining and sale of coal from its mine near Gillette, Wyoming; Oil and gas, which explores for and produces oil and gas primarily in the Rocky Mountain region, with non-operated interests in Texas, California, Oklahoma and other states; Energy marketing, which markets natural gas, crude oil and related services to customers in the Midwest, Southwest, Rocky Mountain, West Coast and Northwest regions; and Power generation, which produces and sells power and capacity to wholesale customers with plants concentrated in Colorado, Nevada, Wyoming and California.

Segment information follows the same accounting policies as described in Note 22 of the Company s 2005 Annual Report on Form 10-K. In accordance with the provisions of SFAS No. 71, Accounting for the Effects of Certain Types of Regulation (SFAS 71), intercompany fuel sales to the electric utility are not eliminated.

Segment information included in the accompanying Condensed Consolidated Statements of Income is as follows (in thousands):

Three Month Period Ended September 30, 2006	External Operating Revenues	Inter-segment Operating Revenues	Income (Loss) from Continuing Operations
Retail services:			
Electric utility	$ 52,467	$ 723	$ 5,764
Electric and gas utility	24,479		953
Wholesale energy:			
Coal mining	6,055	3,391	1,908
Oil and gas	22,969		3,006
Energy marketing	6,327		2,378
Power generation	42,700		9,839
Corporate	11		(1,649)
Inter-segment eliminations		(1,514)	
Total	$ 155,008	$ 2,600	$ 22,199

Three Month Period Ended September 30, 2005	External Operating Revenues	Inter-segment Operating Revenues	Income (Loss) from Continuing Operations
Retail services:			
Electric utility	$ 48,336	$ 938	$ 1,888
Electric and gas utility	23,501		(127)
Wholesale energy:			
Coal mining	5,537	2,945	1,643
Oil and gas	22,800	7	5,109
Energy marketing	3,398		(1,206)
Power generation	43,076		(24,587)*
Corporate	93		(6,504)**
Inter-segment eliminations		(1,623)	
Total	$ 146,741	$ 2,267	$ (23,784)

* Loss from continuing operations includes $32.7 million after-tax impairment charge for Las Vegas I.

** Loss from continuing operations includes $5.8 million after-tax for the write-off and expensing of certain capitalized project development costs.

Nine Month Period Ended September 30, 2006	External Operating Revenues	Inter-segment Operating Revenues	Income (Loss) from Continuing Operations
Retail services:			
Electric utility	$ 142,676	$ 1,518	$ 13,099
Electric and gas utility	97,907		3,214
Wholesale energy:			
Coal mining	15,905	9,579	4,091
Oil and gas	69,519		10,439
Energy marketing	34,907		13,249
Power generation	114,991		14,310
Corporate	43		(5,274)
Inter-segment eliminations		(3,733)	
Total	$ 475,948	$ 7,364	$ 53,128

Nine Month Period Ended September 30, 2005	External Operating Revenues	Inter-segment Operating Revenues	Income (Loss) from Continuing Operations
Retail services:			
Electric utility	$ 133,295	$ 1,387	$ 9,619
Electric and gas utility	78,034		1,028
Wholesale energy:			
Coal mining	15,717	9,144	4,860
Oil and gas	61,504	7	14,346
Energy marketing	16,193		2,187
Power generation	121,366		(14,601)*
Corporate	647		(10,654)**
Inter-segment eliminations		(3,481)	
Total	$ 426,756	$ 7,057	$ 6,785

* Loss from continuing operations includes $32.7 million after-tax impairment charge for Las Vegas I.
** Loss from continuing operations includes $6.2 million after-tax for the write-off and expensing of certain capitalized project development costs.

Other than the sale of the assets of the crude oil marketing and transportation business and its reclassification to Discontinued operations, and the acquisition of certain oil and gas assets in the Piceance Basin in Colorado, the Company had no material changes in the assets of its reporting segments, as reported in Note 22 of the Notes to Consolidated Financial Statements in the Company s 2005 Annual Report on Form 10-K, beyond changes resulting from normal operating activities.

(16) RISK MANAGEMENT ACTIVITIES

The Company actively manages its exposure to certain market risks as described in Note 2 of the Notes to Consolidated Financial Statements in the Company s 2005 Annual Report on Form 10-K. Details of derivative and hedging activities included in the accompanying Condensed Consolidated Balance Sheets and Condensed Consolidated Statements of Income are as follows:

Trading Activities

Natural Gas and Crude Oil Marketing

The Company s natural gas and crude oil marketing subsidiary, Enserco Energy Inc. (Enserco), recently began marketing crude oil in the Rocky Mountain region out of the Company s Golden, Colorado offices. Our primary strategy involves executing physical crude oil purchase contracts with producers, and reselling into various markets. These transactions are primarily entered into as back-to-back purchases and sales, effectively locking in a marketing fee equal to the difference between the sales price and the purchase price, less transportation costs. Under FAS 133, mark-to-market accounting for the related commodity contracts in the Company s back-to-back strategy results in an acceleration of marketing margins locked in for the term of the contracts. These are generally short-term contracts with automatic renewals (typically monthly) if there is no notice of cancellation. The realized and unrealized gains and losses from the oil marketing activities are shown net on the accompanying Condensed Consolidated Income Statement within Operating revenues .

The contract or notional amounts and terms of the Company s natural gas and crude oil marketing activities and derivative commodity instruments are as follows:

	Outstanding at September 30, 2006		Outstanding at December 31, 2005		Outstanding at September 30, 2005	
	Notional Amounts	Latest Expiration (months)	Notional Amounts	Latest Expiration (months)	Notional Amounts	Latest Expiration (months)
(in thousands of MMbtus)						
Natural gas basis swaps purchased	146,331	16	43,507	22	51,155	18
Natural gas basis swaps sold	153,530	18	53,665	22	60,522	18
Natural gas fixed - for - float swaps purchased	44,600	18	17,083	23	19,979	26
Natural gas fixed - for - float						