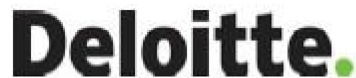

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholder of
Public Service Company of North Carolina, Incorporated
Cayce, South Carolina

We have audited the accompanying consolidated financial statements of Public Service Company of North Carolina, Incorporated and subsidiaries (the "Company") which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of income, comprehensive income, cash flows, and changes in common equity for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards required that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

March 16, 2018

Public Service Company of North Carolina, Incorporated and Subsidiaries
Consolidated Balance Sheets

Thousands of dollars	December 31, 2017	December 31, 2016
Assets		
Gas Utility Plant	$ 2,304,759	$ 1,966,829
Accumulated Depreciation	(487,433)	(454,376)
Goodwill, net of writedown of $229,590	209,824	209,824
Gas Utility Plant, Net	2,027,150	1,722,277
Investments	18,257	27,854
Current Assets:		
Cash and cash equivalents	6,851	13,133
Receivables, net of allowance for uncollectible accounts of $710 and $532	150,783	132,261
Receivables-affiliated companies	4,496	4,251
Receivables-income taxes	-	1,667
Inventories (at average cost):		
Stored gas	31,976	28,542
Materials and supplies	11,414	10,732
Prepayments and other	2,357	4,075
Total Current Assets	207,877	194,661
Deferred Debits and Other Assets:		
Regulatory assets	104,134	100,131
Other	434	598
Total Deferred Debits and Other Assets	104,568	100,729
Total	$ 2,357,852	$ 2,045,521
Capitalization and Liabilities		
Common Stock - no par value, 1,000 shares outstanding	$635,239	$634,681
Retained Earnings	174,592	143,134
Accumulated Other Comprehensive Loss	(1,318)	(1,489)
Total Common Equity	808,513	776,326
Long-Term Debt, net	598,700	449,024
Total Capitalization	1,407,213	1,225,350
Current Liabilities:		
Short-term borrowings	98,661	71,800
Accounts payable	77,277	45,439
Accounts payable-affiliated companies	30,460	10,225
Customer deposits and customer prepayments	28,513	27,537
Taxes accrued	2,235	3,488
Interest accrued	9,524	6,396
Dividends declared	11,800	6,550
Other	5,306	7,054
Total Current Liabilities	263,776	178,489
Deferred Credits and Other Liabilities:		
Deferred income taxes, net	175,746	291,735
Pension and other postretirement benefits	78,103	77,384
Regulatory liabilities	390,471	233,295
Asset retirement obligations	38,681	35,607
Other	3,862	3,661
Total Deferred Credits and Other Liabilities	686,863	641,682
Commitments and Contingencies (Note 8)	-	-
Total	$ 2,357,852	$ 2,045,521

See Notes to Consolidated Financial Statements.

Public Service Company of North Carolina, Incorporated and Subsidiaries
Consolidated Statements of Income

Thousands of dollars	December 31, 2017	December 31, 2016
Operating Revenues	$ 470,248	$ 423,011
Cost of Gas	187,023	162,990
Margin	283,225	260,021
Operating Expenses:		
Operation and maintenance	101,455	102,367
Depreciation and amortization	53,024	51,659
Other taxes	13,688	14,520
Total Operating Expenses	168,167	168,546
Operating Income	115,058	91,475
Other Income (Expense):		
Other revenues	29,643	28,779
Other expenses	(6,660)	(12,845)
Interest charges, net of allowance for borrowed funds used during construction of $2,624 and $1,014	(28,469)	(25,177)
Allowance for equity funds used during construction	8,426	3,303
Total Other Income (Expense)	2,940	(5,940)
Income Before Income Taxes and Earnings (Loss) from Equity Method Investments	117,998	85,535
Income Tax Expense	(41,287)	(32,468)
Income Before Earnings (Loss) from Equity Method Investments	76,711	53,067
Earnings (Loss) from Equity Method Investments	(4,263)	3,752
Net Income	$ 72,448	$ 56,819

See Notes to Consolidated Financial Statements.

Public Service Company of North Carolina, Incorporated and Subsidiaries
Consolidated Statements of Comprehensive Income

Thousands of dollars	December 31, 2017	December 31, 2016
Net Income	$ 72,448	$ 56,819
Other Comprehensive Income (Loss), net of tax:		
Unrealized Losses on Cash Flow Hedging Activities of Equity Method Investees:		
Losses arising during period, net of tax of $(212) and $(27)	(341)	(47)
Losses reclassified to earnings from equity method investments, net of tax of $282 and $37	482	62
Net unrealized losses on cash flow hedging activities of equity method investees	141	15
Deferred Costs of Employee Benefit Plans:		
Losses arising during period, net of tax of $(34) and $(151)	(58)	(258)
Amortization reclassified to net income (see Note 7), net of tax of $52 and $51	88	87
Net deferred costs of employee benefit plans	30	(171)
Other Comprehensive Income (Loss)	171	(156)
Total Comprehensive Income	$ 72,619	$ 56,663

See Notes to Consolidated Financial Statements.

Public Service Company of North Carolina, Incorporated and Subsidiaries
Consolidated Statements of Cash Flows

Thousands of dollars	December 31, 2017	December 31, 2016
Cash Flows From Operating Activities:		
Net income	$ 72,448	$ 56,819
Adjustments to reconcile net income to net cash provided from operating activities:		
Distributions from equity method investment, net of earnings	98	(49)
Deferred income taxes, net	51,174	46,268
Depreciation and amortization	57,668	52,221
Allowance for equity funds used during construction	(8,426)	(3,303)
Changes in certain assets and liabilities:		
Receivables	(18,766)	(37,859)
Income taxes receivable	1,667	12,378
Inventories	(36,575)	(7,682)
Regulatory assets	(4,121)	(13,575)
Regulatory liabilities	(8,279)	(1,846)
Accounts payable	648	16,532
Customer deposits and customer prepayments	977	(1,458)
Taxes accrued	(1,253)	3,210
Other assets	(6,520)	(9,548)
Other liabilities	4,878	680
Net Cash Provided From Operating Activities	105,618	112,788
Cash Flows From Investing Activities:		
Property additions and construction expenditures	(278,341)	(170,617)
Proceeds from investments	2,779	1,786
Net Cash Used For Investing Activities	(275,562)	(168,831)
Cash Flows From Financing Activities:		
Proceeds from issuance of long-term debt	149,583	99,568
Repayment of long-term debt	-	(575)
Dividends	(35,740)	(33,700)
Contributions from parent	558	-
Short-term borrowings - affiliate, net	22,400	-
Short-term borrowings, net	26,861	(2,019)
Net Cash Provided From Financing Activities	163,662	63,274
Net Increase (Decrease) in Cash and Cash Equivalents	(6,282)	7,231
Cash and Cash Equivalents, January 1	13,133	5,902
Cash and Cash Equivalents, December 31	$ 6,851	$ 13,133
Supplemental Cash Flow Information:		
Cash for - Interest (net of capitalized interest of $2,624 and $1,014)	$ 23,185	$ 22,297
- Income taxes paid	8,389	16,244
- Income taxes received	24,990	43,577
Noncash Investing and Financing Activities:		
Accrued construction expenditures	$ 38,468	$ 10,023

See Notes to Consolidated Financial Statements.

Public Service Company of North Carolina, Incorporated and Subsidiaries
Consolidated Statements of Changes in Common Equity

	Common Stock				Accumulated Other Comprehensive Income (Loss)			
Thousands of dollars	Share	Amount	Capital in Excess of Par	Retained Earnings	Gains (Losses) on Cash Flow Hedges	Deferred Employee Benefit Plans Cost	Total AOCI	Total
Balance as of January 1, 2016	1	$ 1	$ 634,680	$ 119,165	$ (12)	$ (1,321)	$(1,333)	$752,513
Net Income				56,819				56,819
Other Comprehensive Income (Loss):								
Losses arising during the period					(47)	(258)	(305)	(305)
Losses/amortization reclassified from AOCI					62	87	149	149
Total Comprehensive Income (Loss)				56,819	15	(171)	(156)	56,663
Dividends Declared				(32,850)				(32,850)
Balance as of December 31, 2016	1	1	634,680	143,134	3	(1,492)	(1,489)	776,326
Net Income				72,448				72,448
Other Comprehensive Income (Loss):								
Losses arising during the period					(341)		(341)	(341)
Losses/amortization reclassified from AOCI					482	30	512	512
Total Comprehensive Income				72,448	141	30	171	72,619
Capital contributions from parent, net			558					558
Dividends Declared				(40,990)				(40,990)
Balance as of December 31, 2017	1	$ 1	$ 635,238	$ 174,592	$ 144	$ (1,462)	$(1,318)	$808,513

Authorized shares of common stock were 1,000 as of December 31, 2017 and 2016.

See Notes to Consolidated Financial Statements.

Public Service Company of North Carolina, Incorporated and Subsidiaries
Notes to Consolidated Financial Statements

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and Principles of Consolidation

Public Service Company of North Carolina, Incorporated (PSNC Energy, and together with its consolidated subsidiaries, the Company), a public utility, was organized as a North Carolina corporation in 1938. Effective January 1, 2000, SCANA Corporation (SCANA), a South Carolina holding company, acquired the Company. As a result, the Company became a wholly owned subsidiary of SCANA, incorporated under the laws of South Carolina. The Company engages predominantly in the purchase, sale, transportation and distribution of natural gas to residential, commercial and industrial customers in North Carolina.

The accompanying consolidated financial statements include the accounts of PSNC Energy and its subsidiary companies, Clean Energy Enterprises, Inc., PSNC Blue Ridge Corporation, and PSNC Cardinal Pipeline Company. The Company reports certain investments using the equity method of accounting. Significant intercompany balances and transactions have been eliminated in consolidation.

The Company has evaluated subsequent events through March 16, 2018, which is the date these financial statements were issued.

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 reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Utility Plant

Utility plant is stated at original cost. The costs of additions, replacements and betterments to utility plant, including direct labor, material and indirect charges for engineering, supervision and an allowance for funds used during construction (AFC), are added to utility plant accounts. The original cost of utility property retired or otherwise disposed of is removed from utility plant accounts and generally charged to accumulated depreciation. The costs of repairs and replacements of items of property determined to be less than a unit of property or that do not increase the asset's life or functionality are charged to expense.

AFC is a noncash item that reflects the period cost of capital devoted to plant under construction. This accounting practice results in the inclusion of, as a component of construction cost, the costs of debt and equity capital dedicated to construction investment. AFC is included in rate base investment and depreciated as a component of plant cost in establishing rates for utility services. PSNC Energy calculated AFC using average composite rates, developed on a pre-tax basis, of 10.5% and 11.8% for the years ended December 31, 2017 and 2016, respectively.

The Company records provisions for depreciation and amortization using the straight-line method based on the estimated service lives of the various classes of property, and in most cases, includes provisions for future cost of removal. The composite weighted average depreciation rate for utility plant assets was 3.0% at December 31, 2017 and 2.9% at December 31, 2016. Depreciation rates for utility plant are approved by the North Carolina Utilities Commission (NCUC). PSNC Energy is required to conduct a depreciation study every five years and propose new depreciation rates for approval. The last depreciation study was conducted as of December 31, 2015 and resulted in changes being made to depreciation rates effective January 1, 2017.

Goodwill

The Company considers certain amounts categorized by the Federal Energy Regulatory Commission (FERC) as "acquisition adjustments" to be goodwill. The Company tests goodwill for impairment annually as of January 1, unless indicators, events or circumstances require interim testing to be performed. Accounting guidance adopted by the Company gives it the option to perform a qualitative assessment of impairment ("step zero"). Based on this qualitative assessment, if the Company determines that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, the Company is not required to proceed with the two-step quantitative assessment. If the quantitative assessment becomes necessary, step one requires estimation of the fair value of the reporting unit and the comparison of that amount to its carrying value. If this step indicates an impairment (carrying value in excess of fair value), then step two, measurement of the amount of the goodwill impairment (if any), is required. Should a write-down be required, such a charge would be treated as an operating expense.

For each period presented, assets with a carrying value of $210 million for PSNC Energy (Gas Distribution segment), net of a writedown of $230 million taken in 2002, were classified as goodwill. The Company utilized the step zero qualitative assessment in its evaluations as of January 1, 2018 and as of January 1, 2017 and was not required to use the two-step quantitative assessment.

Cash and Cash Equivalents

Temporary cash investments having original maturities of three months or less at time of purchase are considered to be cash equivalents. These cash equivalents are generally in the form of commercial paper, certificates of deposit, repurchase agreements, and treasury bills.

Receivables

Customer receivables reflect amounts due from customers arising from the delivery of energy or related services and include both billed and unbilled amounts earned pursuant to revenue recognition practices described below. Customer receivables are generally due within one month of receipt of invoices which are presented on a monthly cycle basis.

Inventories

Materials and supplies include the average costs of pipe, fittings, meters, appliances and appliance parts. Stored gas includes the average cost of natural gas. Natural gas is charged to inventory when purchased and is expensed at weighted average cost, as used, and recovered through the purchased gas adjustment mechanism approved by the NCUC.

PSNC Energy utilizes an asset management and supply service agreement with a counterparty for certain natural gas storage facilities. Such counterparty held, through an agency relationship, 39% and 40% of PSNC Energy's natural gas inventory at December 31, 2017 and December 31, 2016, respectively, with a carrying value of $11.5 million and $9.8 million, respectively. Under the terms of this agreement, PSNC Energy receives storage asset management fees, of which 75% are credited to customers. This agreement expires on March 31, 2019.

Income Taxes

The Company is included in the consolidated federal income tax return of SCANA. Under a joint consolidated income tax allocation agreement, each SCANA subsidiary's current and deferred tax expense is computed on a stand-alone basis. Deferred tax assets and liabilities are recorded for the tax effects of all significant temporary differences between the book basis and tax basis of assets and liabilities at currently enacted tax rates. Deferred tax assets and liabilities are adjusted for changes in such tax rates through charges or credits to regulatory assets or liabilities if they are expected to be recovered from, or passed through to, customers; otherwise, such adjustments are charged or credited to income tax expense. See Note 4 for a discussion of the impact of adjustments recorded upon enactment of The Tax Cuts and Jobs Act (Tax Act). Also, under provisions of the income tax allocation agreement, certain tax benefits of the parent holding company are distributed in cash to taxpaying affiliates, including the Company, in the form of capital contributions. The Company received capital distributions of $0.6 million under such provisions in 2017, and did not receive or return capital distributions under such provisions in 2016.

Regulatory Assets and Regulatory Liabilities

PSNC Energy records costs that have been or are expected to be allowed in the ratemaking process in a period different from the period in which the costs would be charged to expense or records revenue in a period different from the period in which the revenue would be recorded by a nonregulated enterprise. These expenses deferred for future recovery from customers or obligations to be refunded to customers are primarily classified in the balance sheet as regulatory assets and regulatory liabilities (see Note 2) and are amortized consistent with the treatment of the related costs or revenues in the ratemaking process. Certain deferred amounts expected to be recovered or repaid within 12 months are classified in the balance sheet as Receivables or Customer deposits and customer prepayments, respectively.

Debt Issuance Premiums, Discounts and Other Costs

Premiums, discounts and debt issuance costs are presented within long-term debt and are amortized as components of interest charges over the terms of the respective debt issues.

Environmental

PSNC Energy maintains an environmental assessment program to identify and evaluate current and former operations sites that could require environmental clean-up. As site assessments are initiated, estimates are made of the amount of expenditures, if any, deemed necessary to investigate and remediate each site. Environmental remediation liabilities are accrued when the criteria for loss contingencies are met. These estimates are refined as additional information becomes available; therefore, actual expenditures could differ significantly from the original estimates. Probable and estimable costs are accrued related to environmental sites on an undiscounted basis. Amounts estimated and accrued to date for site assessments and clean-up relate solely to regulated operations. Amounts expected to be recovered through rates are recorded in regulatory assets and, if applicable, amortized over approved amortization periods. Other environmental costs are expensed as incurred.

Income Statement Presentation

The Company presents the revenues and expenses of its regulated business within operating income. All other activities, which primarily include appliance sales and service, are presented within other income (expense).

Revenue Recognition

PSNC Energy records revenues during the accounting period in which it provides services to customers and includes estimated amounts for natural gas delivered and facility charges not billed. Unbilled revenues totaled $48.1 million at December 31, 2017 and $34.6 million at December 31, 2016 and are included in Receivables on the balance sheet.

PSNC Energy's purchased gas adjustment (Rider D) mechanism authorized by the NCUC allows the recovery of all prudently incurred gas costs, including the results of its hedging program, from customers. Any difference between actual gas costs and amounts contained in rates is deferred for subsequent refund to or collection from customers, with interest, through cost of gas. The Rider D mechanism includes commodity and fixed gas costs; premiums, transaction fees, margin requirements and any realized gains or losses from PSNC Energy's hedging activities; margin losses on negotiated gas sales to certain large commercial/industrial customers; and gas costs that were uncollectible from certain customers.

PSNC Energy is authorized by the NCUC to utilize a customer usage tracker (CUT) which allows it to adjust base rates semi-annually for residential and commercial customers based on average per customer consumption, whether impacted by weather or other factors. Any difference between actual margin and normalized margin under the CUT mechanism is deferred for subsequent refund to or collection from customers, with interest, through cost of gas. PSNC Energy establishes its commodity cost of gas for large commercial and industrial customers on the basis of market prices for natural gas as approved by the NCUC.

Sales taxes that are billed to and collected from customers are recorded as liabilities until they are remitted to the respective taxing authority. Such taxes are not included in revenues or expenses in the statements of income.

New Accounting Matters

Recently Adopted

In the first quarter of 2017, PSNC Energy adopted the following accounting guidance issued by the Financial Accounting Standards Board (FASB). The adoption of this guidance had no impact on its financial statements except as indicated.

- Guidance issued in July 2015 requires most inventory to be measured at the lower of cost and net realizable value.
- Guidance issued in October 2016 requires entities to recognize the income tax consequences of an intra-entity transfer of an asset, other than inventory, when the transfer occurs.

In January 2017, the FASB issued accounting guidance to simplify the accounting for goodwill impairment by removing Step 2 of the goodwill impairment test. The guidance is effective for years beginning in 2020, though early adoption after January 1, 2017 is allowed. PSNC Energy adopted this guidance on January 1, 2018, and its adoption had no impact on its financial statements.

Pending Adoption

In the first quarter of 2018, PSNC Energy will adopt the following accounting guidance issued by the FASB.

- Guidance issued in May 2014 for revenue arising from contracts with customers supersedes most prior revenue recognition guidance, including industry-specific guidance. This new revenue recognition model provides for a five-step analysis in determining when and how revenue is recognized, and requires revenue recognition to depict the transfer of promised goods or services to customers, based on the transfer of control, in an amount that reflects the consideration a company expects to receive in exchange for those goods or services. In addition, this guidance requires disclosure of the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The analysis of contracts with customers to which the guidance might be applicable has been completed and activities of the FASB's Transition Resource Group for Revenue Recognition, particularly as they relate to the treatment of CIAC, ARP and the collectability of revenue of utilities subject to rate regulation have been considered. PSNC Energy has concluded that its use of CIAC is outside the scope of the new revenue recognition guidance. PSNC Energy's CUT allow for revenue adjustments to be recognized prior to amounts being reflected in customer bills. These revenue adjustments, which give rise to regulatory assets or liabilities, represent ARPs that are outside the scope of the new guidance and will be reported as Other operating revenue separately from revenue from contracts with customers on the statement of income. An evaluation of the enhanced disclosure requirements is being completed, including determining the appropriate disaggregation of revenue.

  PSNC Energy will adopt this guidance using the modified retrospective method, and comparative periods will not be restated. PSNC Energy does not anticipate that the adoption of this guidance will have any material impact on its financial statements, but its adoption will result in additional disclosures. The adoption of this guidance will not result in a cumulative effect adjustment to beginning retained earnings.

- Guidance issued in January 2016 changes how entities measure certain equity investments and financial liabilities, among other things. Entities will be required to make a cumulative-effect adjustment to beginning retained earnings as of the beginning of the fiscal year in which the guidance is effective, with certain of exceptions. PSNC Energy expects to adopt this guidance when required in the first quarter of 2018 and does not anticipate that its adoption will have a significant impact on its financial statements.

- Guidance issued in August 2016 is intended to reduce diversity in cash flow statement classification related to certain transactions, and entities must apply the guidance retrospectively to all periods presented. The adoption of this guidance will have no impact on the financial statements of PSNC Energy.

- Guidance issued in November 2016 clarifies how restricted cash should be presented on the statement of cash flows, and entities must apply the guidance retrospectively to all periods presented. The adoption of this guidance will have no impact on the financial statements of PSNC Energy.

- Guidance issued in March 2017 changes the required presentation of net periodic pension and postretirement benefit costs. Under this guidance, such costs will be separated into service cost components and other components. The service cost components will be presented in the same line item (or items) as other compensation costs arising from services rendered by employees during the period. The other components will be reported in the income statement separately from the service cost component and outside operating income. Only the service cost component will be eligible for capitalization in assets. Entities must apply this guidance on a retrospective basis for the presentation of the service cost component and the other components, and on a prospective basis for the capitalization of only the service cost component. As permitted, service cost and other costs disclosed in related footnotes to previously issued financial statements will be used when estimating retrospective changes for such costs in the income statements for prior periods. Due to regulatory overlay, non-service cost components related to regulated operations that are capitalized in assets under current accounting guidance will be deferred within regulatory assets in the future. As a result, the adoption of this guidance will not have a material impact on the financial statements of PSNC Energy.

PSNC Energy will adopt the following accounting guidance issued by the FASB when indicated below.

In February 2016, the FASB issued accounting guidance related to the recognition, measurement and presentation of leases. The guidance applies a right-of-use model and, for lessees, requires all leases with a duration over 12 months to be recorded on the balance sheet, with the rights of use treated as assets and the payment obligations treated as liabilities. Further,and without consideration of any regulatory accounting requirements which may apply, depending primarily on the nature of the assets and the relative consumption of them, lease costs will be recognized either through the separate amortization of the right-of-use asset and the recognition of the interest cost related to the payment obligation, or through the recording of a combined straight-line rental expense. For lessors, the guidance calls for the recognition of income either through the derecognition of assets and subsequent recording of interest income on lease amounts receivable, or through the recognition of rental income on a straight-line basis, also depending on the nature of the assets and relative consumption. In January 2018, FASB amended this accounting guidance to provide an optional transition practical expedient that would allow adopters to not evaluate under the new guidance existing or expired land easements that were not previously accounted for as leases under existing guidance. The new guidance is effective for years beginning in 2019, and PSNC Energy does not anticipate that its adoption will impact its financial statements other than increasing amounts reported for assets and liabilities on the balance sheet and changing the place on its statements of income on which certain expenses are recorded. No impact on net income (loss) is expected. The identification and analysis of leasing and related contracts to which the guidance might be applicable has begun. In addition, PSNC Energy has begun implementation of a third-party software tool that will assist with initial adoption and ongoing compliance. Specifically, preliminary system configuration has been completed and data from certain leases are being entered.

In June 2016, the FASB issued accounting guidance requiring the use of a current expected credit loss impairment model for certain financial instruments. The new model is applicable to trade receivables and most debt instruments, among other financial instruments, and in certain instances may result in impairment losses being recognized earlier than under current guidance. PSNC Energy must adopt this guidance beginning in 2020, including interim periods, though the guidance may be adopted in 2019. PSNC Energy has not determined when this guidance will be adopted or what impact it will have on its financial statements.

In August 2017, the FASB issued accounting guidance to simplify the application of hedge accounting. Among other things, the new guidance will enable more hedging strategies to qualify for hedge accounting, will allow entities more time to perform an initial assessment of hedge effectiveness, and will permit an entity to perform a qualitative assessment of effectiveness for certain hedges instead of a quantitative one. For cash flow hedges that are highly effective, all changes in the fair value of the derivative hedging instrument will be recorded in other comprehensive income and will be reclassified to earnings in the same period that the hedged item impacts earnings. Fair value hedges will continue to be recorded in current earnings, and any ineffectiveness will impact the income statement. In addition, changes in the fair value of a derivative will be recorded in the same income statement line as the earnings effect of the hedged item, and

additional disclosures will be required related to the effect of hedging on individual income statement line items. The guidance must be applied to all outstanding instruments using a modified retrospective method, with any cumulative effect adjustment recorded to opening retained earnings as of the beginning of the first period in which the guidance becomes effective. PSNC Energy expects to adopt this guidance when required in the first quarter of 2019, though early adoption is permitted, and has not determined what impact such adoption will have on its financial statements.

In February 2018, the FASB issued accounting guidance allowing entities to reclassify from Accumulated Other Comprehensive Income (AOCI) to retained earnings any amounts for stranded tax effects resulting from the Tax Act. The guidance must be applied either in the period of adoption or retrospectively to each period in which the effect of the change was recognized. PSNC Energy must adopt this guidance beginning in 2019, including interim periods, though the guidance may be adopted earlier. PSNC Energy has not determined when this guidance will be adopted or what impact it will have on its statements of financial position. No impact is expected on statements of income or cash flows.

2. RATE AND OTHER REGULATORY MATTERS

Rate Matters

PSNC Energy's Rider D rate mechanism allows it to recover from customers all prudently incurred gas costs and certain related uncollectible expenses as well as losses on negotiated gas and transportation sales. PSNC Energy had undercollected from customers $1.2 million at December 31, 2017, primarily due to hedging activities, and $2.8 million at December 31, 2016, primarily due to fixed gas costs. PSNC had overcollected from customers $11.9 million at December 31, 2017 and $9.4 million at December 31, 2016 primarily due to commodity costs and off system gas sales. PSNC Energy records undercollected amounts in Receivables and overcollected amounts in Customer deposits and customer prepayments on the consolidated balance sheets.

PSNC Energy establishes rates using a benchmark cost of gas approved by the NCUC, which may be periodically adjusted to reflect changes in the market price of natural gas. PSNC Energy revises its tariffs as necessary to track these changes and accounts for any over- or under‑collection of the delivered cost of gas in its deferred accounts for subsequent rate consideration. The NCUC reviews PSNC Energy's gas purchasing practices annually. In addition, PSNC Energy utilizes a CUT, a decoupling mechanism, which allows it to adjust its base rates semi-annually for residential and commercial customers based on average per customer consumption. PSNC Energy had undercollected from customers $29.2 million at December 31, 2017 and $30.0 million at December 31, 2016 for certain CUT program costs, and had overcollected from customers $0.7 million at December 31, 2016 for certain CUT program costs. Undercollections at December 31, 2017 were not significant. Undercollected amounts are included in Receivables and overcollected amounts are included in Customer deposits and customer prepayments on the consolidated balance sheets.

On October 28, 2016, the NCUC granted PSNC Energy a net annual increase of approximately $19.1 million, or 4.39%, in rates and charges to customers, and set PSNC Energy's authorized return on equity at 9.7%. In addition, the NCUC has authorized PSNC Energy to use a tracker mechanism to recover the incurred capital investment and associated costs of complying with federal standards for pipeline integrity and safety requirements that are not in current base rates. PSNC Energy has filed biannual applications to adjust its rates for this purpose, and the NCUC has approved those applications for the incremental annual revenue requirements, as follows:

Rates Effective	Incremental Increase
March 1, 2017	$1.9 million
September 1, 2017	$0.7 million

In December 2017, in connection with PSNC Energy's 2017 Annual Prudence Review, the NCUC determined that PSNC Energy's gas costs, including all hedging transactions, were reasonable and prudently incurred during the 12 months ended March 31, 2017.

On January 3, 2018, the NCUC sought reports from its jurisdictional utilities as to how they planned to respond to the Tax Act. In its response on February 1, 2018, PSNC Energy proposed certain adjustments to its rates that, if enacted,

would serve to reduce amounts that are currently being collected from customers based on pre-Tax Act rates. PSNC Energy cannot determine when the NCUC may take action on this matter.

Regulatory Assets and Regulatory Liabilities

PSNC Energy has significant cost-based, rate-regulated operations and recognizes in its financial statements certain revenues and expenses in different periods than do other enterprises. As a result, PSNC Energy has recorded regulatory assets and regulatory liabilities which are summarized in the following tables. Substantially all of its regulatory assets are either explicitly excluded from rate base or are effectively excluded from rate base due to their being offset by related liabilities.

Thousands of dollars	December 31, 2017	December 31, 2016
Regulatory Assets:		
Accumulated deferred income taxes	-	$ 8,275
Asset retirement obligations	$ 23,924	22,046
Deferred employee benefit plan costs	31,381	33,376
Pipeline integrity management costs	43,291	29,459
Environmental remediation costs	5,174	6,524
Other	364	451
Total Regulatory Assets	$ 104,134	$ 100,131
Regulatory Liabilities:		
Accumulated deferred income taxes	$ 161,137	-
Asset removal costs	229,314	$ 224,178
Other	20	9,117
Total Regulatory Liabilities	$ 390,471	$ 233,295

Accumulated deferred income taxes contained within regulatory assets represent deferred tax liabilities that arise from utility operations that have not been included in customer rates. A portion of these regulatory assets are related to depreciation and are netted within regulatory liabilities in the current period.

Asset retirement obligations (ARO) represents the regulatory asset associated with conditional AROs related to transmission and distribution properties. These regulatory assets are expected to be recovered over the related property lives which may range up to approximately 90 years.

Employee benefit plan costs have historically been recovered as they have been recorded under generally accepted accounting principles. Deferred employee benefit plan costs represent pension and other postretirement benefit costs which were accrued as liabilities and treated as regulatory assets pursuant to an NCUC order. These deferred benefit costs are expected to be recovered through utility rates, primarily over average service periods of participating employees, up to approximately 11 years.

Pipeline integrity management costs represent operating and maintenance costs incurred to comply with federal regulatory requirements related to natural gas pipelines. PSNC Energy is recovering costs totaling $4.4 million annually through 2021. PSNC Energy is continuing to defer pipeline integrity costs, and as of December 31, 2017 costs of $26.6 million have been deferred pending future approval of rate recovery.

Environmental remediation costs represent costs associated with the assessment and clean-up of sites currently or formerly owned by PSNC Energy. Remediation costs totaling $6.9 million are being recovered over a five-year period that will end in 2021.

Accumulated deferred income taxes contained within regulatory liabilities represent (i) excess deferred income taxes arising from the remeasurement of deferred income taxes upon the enactment of the Tax Act (certain of which are

protected under normalization regulations and will be amortized over the remaining lives of related property, and certain of which will be amortized to the benefit of customers over a prescribed period as instructed by regulators), offset by deferred income taxes that arise from utility operations that have not been included in customer rates (a portion of which relate to depreciation and are expected to be recovered over the remaining lives of the related property which may range up to approximately 90 years). See also Note 4.

Asset removal costs represent estimated net collections through depreciation rates of amounts to be incurred for the removal of assets in the future.

The NCUC has reviewed and approved through specific orders most of the items shown as regulatory assets. Other regulatory assets include, but are not limited to, certain costs which have not been specifically approved for recovery by the NCUC. In recording such costs as regulatory assets, management believes the costs will be allowable under existing rate-making concepts that are embodied in rate orders received by PSNC Energy. The costs are currently not being recovered, but are expected to be recovered through rates in future periods. In the future, as a result of deregulation or other changes in the regulatory environment or changes in accounting requirements, PSNC Energy could be required to write off its regulatory assets and liabilities. Such an event could have a material effect on the Company's results of operations, liquidity or financial position in the period the write-off would be recorded.

3. LONG-TERM DEBT AND SHORT-TERM DEBT

Long-Term Debt

Long-term debt by type with related weighted average interest rates and maturities at December 31 is as follows:

		2017		2016	
Thousands of dollars	Maturity	Balance	Rate	Balance	Rate
Medium-Term Notes (unsecured)	2021-2047	$ 400,000	4.32%	$ 250,000	4.41%
Senior Debentures	2020-2026	200,000	6.88%	200,000	6.88%
Total debt		600,000		450,000	
Unamortized debt issuance costs		$ (1,300)		$ (976)	
Total long-term debt, net		$ 598,700		$ 449,024	

There are no long-term debt maturities in 2018, 2019 or 2022. Maturities are expected to be $100 million in 2020 and $150 million in 2021.

In June 2017, PSNC Energy issued $150 million of 4.18% senior notes due June 30, 2047. In June 2016, PSNC Energy issued $100 million of 4.13% senior notes due June 22, 2046. Proceeds from these sales were used to repay short-term debt, to finance capital expenditures, and for general corporate purposes.

PSNC Energy's note purchase and debenture purchase agreements contain provisions that could limit the payment of cash distributions, including dividends, on PSNC Energy's common stock. These agreements generally limit the sum of distributions to an amount that does not exceed $30 million plus 85% of Consolidated Net Income (as therein defined) accumulated after December 31, 2008 plus the net proceeds of issuances by PSNC Energy of equity or convertible debt securities (as therein defined). As of December 31, 2017, this limitation would permit PSNC Energy to pay cash distributions in excess of $100 million.

Lines of Credit and Short-Term Borrowings

At December 31, 2017 and 2016, PSNC Energy had available the following committed lines of credit and commercial paper borrowings outstanding:

Thousands of dollars	2017	2016
Committed long-term lines of credit	$ 200,000	$ 200,000
Commercial paper (270 or fewer days)	98,661	71,800
Weighted average interest rate	1.93%	1.07%
Available	$ 101,339	$ 128,200

PSNC Energy is party to a five-year credit agreement of $200 million that expires in December 2020. The credit agreement is used for general corporate purposes, including liquidity support for PSNC Energy's commercial paper program and working capital needs. The committed long-term facilities is a revolving line of credit under credit agreements with a syndicate of banks. Wells Fargo Bank, National Association, Bank of America, N.A. and Morgan Stanley Bank, N.A. each provide 9.5% of the credit facility, JP Morgan Chase Bank, N.A., Mizuho Corporate Bank, Ltd., TD Bank N.A., Credit Suisse AG, Cayman Islands Branch, UBS Loan Finance LLC, MUFG Union Bank, N.A., and Branch Banking and Trust Company each provide 7.9%, and Royal Bank of Canada and U.S. Bank National Association each provide 5.5%. Two other banks provide the remaining support. The Company pays fees to the banks as compensation for maintaining the committed lines of credit. Such fees were not material in any period presented.

PSNC Energy participates in a utility money pool with certain other SCANA subsidiaries. Money pool borrowings and investments bear interest at short-term market rates. PSNC Energy’s interest income and interest expense from money pool transactions were not significant during any period presented. PSNC had money pool borrowings due to an affiliate of $22.4 million at December 31, 2017 and no money pool borrowings or investments due to an affiliate at December 31, 2016. Amounts due to an affiliate are included within Accounts payable--affiliated companies on PSNC Energy's consolidated balance sheets.

Action by Credit Ratings Agencies

In the third quarter of 2017, two credit ratings agencies lowered their ratings for SCANA and its rated subsidiaries, including PSNC Energy and South Carolina Electric & Gas Company (SCE&G), citing a decline in the regulatory environment of SCE&G as a principal reason for the downgrades, and both agencies maintained their negative outlook or watch status. This decline in the regulatory environment is primarily due to adverse developments relating to a nuclear project abandoned by SCE&G in 2017. On February 1, 2018, the South Carolina House of Representatives overwhelmingly approved a bill that, if enacted, would temporarily repeal certain rates SCE&G collects related to financing costs of the abandoned nuclear project. As a result, on February 5, 2018, one agency downgraded its ratings for SCANA and SCE&G, and attributed the downgrade to the action taken by the House of Representatives and the politically charged environment that is expected to weigh heavily on any decisions South Carolina regulators and legislators related to SCE&G's electric rates. PSNC Energy’s ratings were also negatively affected because of the impact on SCANA. With this recent downgrade, the issuer ratings and the senior unsecured debt ratings for SCANA are considered below investment grade by two credit agencies, and the issuer ratings for PSNC Energy are considered to be at the threshold for investment grade by one credit agency while its senior secured debt ratings remain above investment grade. All of the ratings for SCANA and PSNC Energy are either under review for possible downgrade or have a negative or evolving outlook.

Any actions taken by or anticipated to be taken by South Carolina regulators or legislators that are viewed as adverse, any deterioration of the rated companies’ commonly monitored financial credit metrics or any additional adverse developments with respect to SCE&G’s nuclear project could further negatively affect SCANA’s and PSNC Energy’s debt ratings. If these rating agencies were to further lower any of these ratings, borrowing costs on new issuances of long-term debt and commercial paper would increase, which could adversely impact financial results or limit or eliminate refinancing opportunities, and the potential pool of investors and funding sources could decrease. In addition, further ratings downgrades may result in lower collateral thresholds being applied to PSNC Energy’s commodity derivatives, or the removal of such thresholds altogether. This action would have the effect of requiring PSNC Energy to post additional

collateral for commodity derivative instruments with unfavorable fair values. Ratings downgrades may also result in prepayments and demands from vendors for letters of credit, cash deposits, or other forms of credit support under certain gas supply and other agreements, and further ratings downgrades could result in requirements for additional deposits or the provision of additional credit support in order to conduct business under these agreements.

4. INCOME TAXES

Components of income tax expense are as follows:

Thousands of dollars	2017	2016
Current taxes:		
Federal	$ (18,337)	$ (14,285)
State	428	485
Total current taxes	(17,909)	(13,800)
Deferred taxes, net:		
Federal	56,615	43,626
State	2,581	2,642
Total deferred taxes	59,196	46,268
Total income tax expense	$ 41,287	$ 32,468

The difference between actual income tax expense and the amount calculated from the application of the statutory 35% federal income tax rate to pre-tax income is reconciled as follows:

Thousands of dollars	2017	2016
Net income	$ 72,448	$ 56,819
Income tax expense	41,287	32,468
Total pre-tax income	$ 113,735	$ 89,287
Income taxes on above at statutory federal income tax rate	$ 39,807	$ 31,250
Increases (decreases) attributed to:		
State income taxes (less federal income tax effect)	1,956	2,032
Allowance for equity funds	(2,949)	(1,156)
Remeasurement of deferred taxes upon enactment of Tax Act	2,212	—
Other differences, net	2,473	342
Total income tax expense	$ 43,499	$ 32,468

The tax effects of significant temporary differences comprising the Company's net deferred tax liability are as follows:

Thousands of dollars	2017	2016
Deferred tax assets:		
Nondeductible accruals	$ 19,515	$ 29,974
Asset retirement obligation	9,040	13,157
Net operating loss	984	—
Deferred compensation	790	—
Other	1,219	1,551
Total deferred tax assets	31,548	44,682
Deferred tax liabilities:		
Property, plant and equipment	174,104	287,797
Deferred employee benefit plan costs	7,334	12,333
Prepayments	286	523
Regulatory asset - asset retirement obligation	5,591	8,146
Regulatory asset - pipeline integrity management cost	8,418	9,841
Distribution integrity management program cost	1,699	956
Other	9,862	16,821
Total deferred tax liabilities	207,294	336,417
Net deferred tax liability	$ 175,746	$ 291,735

In December 2017, the Tax Act was enacted, resulting in the remeasurement of all federal deferred income tax assets and liabilities to reflect a 21% statutory tax rate. Due to the regulated nature of the Company's operations, this remeasurement is primarily reflected in excess deferred income tax balances within regulatory liabilities. In connection with this remeasurement, however, the Company recorded lower net income of approximately $2.2 million in its statements of income for the year ended December 31, 2017. Upon the eventual filing of the Company's 2017 consolidated income tax return, adjustments to deferred income taxes and deferred income taxes may be recorded; however, these adjustments are not expected to have a material impact on the Company's financial position, results of operations or cash flows.

The State of North Carolina lowered its corporate income tax rate from 6.0% to 5.0% in 2015, 4% in 2016, 3% in 2017 and 2.5% effective January 1, 2019. In connection with these changes in tax rates, related state deferred tax amounts were re-measured, with the change in their balances being credited to a regulatory liability. The changes in income tax rates did not and are not expected to have a material impact on the Company's financial position, results of operations, or cash flows.

The Company is included in the consolidated federal income tax return of SCANA and files various applicable state and local income tax returns. The IRS has completed examinations of SCANA's federal returns through 2004, and SCANA's federal returns through 2009 are closed for additional assessment. The IRS is currently examining SCANA's open federal returns through 2016 as a result of research and experimentation related claims attributable to another SCANA subsidiary. With few exceptions, the Company is no longer subject to state and local income tax examinations by tax authorities for years before 2010.

The Company had no uncertain tax positions, and recorded no associated interest income, interest expense or penalties, for any period presented.

5. DERIVATIVE FINANCIAL INSTRUMENTS

PSNC Energy recognizes all derivative instruments as either assets or liabilities in the statement of financial position and measures those instruments at fair value. PSNC Energy recognizes changes in the fair value of derivative instruments either in earnings, as a component of other comprehensive income (loss), or within regulatory assets or regulatory liabilities, depending upon the intended use of the derivative and the resulting designation.

Policies and procedures and risk limits are established to control the level of market, credit, liquidity and operational and administrative risks assumed by PSNC Energy. The Board of Directors of SCANA, PSNC Energy's parent, has delegated to a Risk Management Committee the authority to set risk limits, establish policies and procedures for risk management and measurement, and oversee and review the risk management process and infrastructure. The Risk Management Committee, which is comprised of certain officers, including PSNC Energy's Risk Management Officer and SCANA's senior officers, apprises the Audit Committee of the Board of Directors with regard to the management of risk and brings to their attention significant areas of concern. Written policies define the physical and financial transactions that are approved, as well as the authorization requirements and limits for transactions.

PSNC Energy hedges natural gas purchasing activities using over-the-counter options and swaps and New York Mercantile Exchange (NYMEX) futures and options. PSNC Energy's tariffs also include a provision for the recovery of actual gas costs incurred, including any costs for hedging. PSNC Energy records premiums, transaction fees, margin requirements and any realized gains or losses from its hedging program in deferred accounts as a regulatory asset or liability for the over- or under-recovery of gas costs. These derivative financial instruments are not designated as hedges for accounting purposes.

Quantitative Disclosures Related to Derivatives

PSNC Energy was party to natural gas derivative contracts for 6,430,000 Million British Thermal Units (MMBTU) at December 31, 2017 and 4,510,000 MMBTU at December 31, 2016, respectively.

The fair value of commodity derivatives, none of which were designated as hedging instruments, totaled $0.8 million at December 31, 2017 and $2.6 million at December 31, 2016. Such amounts are reflected on the balance sheet within Prepayments and other and offset to Customer deposits and customer prepayments. PSNC Energy did not have any other derivatives or other financial instruments in the statement of financial position during any period presented.

For a discussion of interest rate swaps used by PSNC Energy's equity method investees, see consolidated Note 9.

Credit Risk Considerations

PSNC Energy limits credit risk in its commodity and interest rate derivatives activities by assessing the creditworthiness of potential counterparties before entering into transactions with them and continuing to evaluate their creditworthiness on an ongoing basis. In this regard, PSNC Energy uses credit ratings provided by credit rating agencies and current market-based qualitative and quantitative data, as well as financial statements, to assess the financial health of counterparties on an ongoing basis. PSNC Energy uses standardized master agreements which generally include collateral requirements. These master agreements permit the netting of cash flows associated with a single counterparty. Cash, letters of credit and parental/affiliate guarantees may be obtained as security from counterparties in order to mitigate credit risk. The collateral agreements require a counterparty to post cash or letters of credit in the event an exposure exceeds the established threshold. The threshold represents an unsecured credit limit which may be supported by a parental/affiliate guaranty, as determined in accordance with PSNC Energy's credit policies and due diligence. In addition, collateral agreements allow for the termination and liquidation of all positions in the event of a failure or inability to post collateral.

PSNC Energy had no derivative instruments in a liability position for any period presented. In addition, PSNC Energy did not have derivative instruments with underlying contingent features which, if triggered, would have permitted PSNC Energy to request collateral from its counterparties for any period presented.

6. FAIR VALUE MEASUREMENTS, INCLUDING DERIVATIVES

A fair value measurement using unadjusted quoted prices in active markets for identical assets or liabilities is considered to be Level 1. A fair value measurement using observable inputs other than those for Level 1, including quoted prices for similar (not identical) assets or liabilities or inputs that are derived from observable market data by correlation or other means is considered to be Level 2. A Level 3 fair value measurement is one using unobservable inputs, including situations where there is little, if any, market activity for the asset or liability.

PSNC Energy uses unadjusted NYMEX prices to determine fair value for commodity derivative assets and liabilities, and considers such measures of fair value to be Level 1 for exchange traded instruments and Level 2 for over-the-counter instruments.

Fair value asset measurements were $0.8 million at December 31, 2017 and $2.6 million at December 31, 2016. These measurements were considered Level 1 and were included within Prepayments and other in the consolidated balance sheet. There were no fair value liability measurements.

There were no Level 3 fair value measurements for either period presented, and there were no transfers of fair value amounts into or out of Levels 1, 2, or 3 during any period presented.

Financial instruments for which the carrying amount may not equal estimated fair value at December 31, 2017 and December 31, 2016 were as follows:

	As of December 31, 2017		As of December 31, 2016	
Thousands of dollars	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Long-term debt	$598,700	$705,135	$449,024	$511,182

Fair values of long-term debt instruments are based on net present value calculations using independently sourced market data that incorporate a developed discount rate using similarly rated long-term debt, along with benchmark interest rates. As such, the aggregate fair values presented above are considered to be Level 2. Early settlement of long-term debt may not be possible or may not be considered prudent.

Carrying values of short-term borrowings approximate their fair values, which are based on quoted prices from dealers in the commercial paper market. These fair values are considered to be Level 2.

7. EMPLOYEE BENEFIT PLANS

Pension and Other Postretirement Benefit Plans

PSNC Energy participates in SCANA's noncontributory defined benefit pension plan, which covers substantially all regular, full-time employees hired before January 1, 2014. SCANA's policy has been to fund the plan as permitted by applicable federal income tax regulations, as determined by an independent actuary.

SCANA's pension plan provides benefits under a cash balance formula for employees hired before January 1, 2000 who elected that option and for all eligible employees hired subsequently. Under the cash balance formula, benefits accumulate as a result of compensation credits and interest credits. Employees hired before January 1, 2000 who elected to remain under the final average pay formula earn benefits based on years of credited service and the employee's average annual base earnings received during the last three years of employment. Benefits under the cash balance formula and the final average pay formula will continue to accrue through December 31, 2023, after which date no benefits will be accrued except that participants under the cash balance formula will continue to earn interest credits.

In addition to pension benefits, PSNC Energy participates in SCANA's unfunded postretirement health care and life insurance programs which provide benefits to certain active and retired employees. Retirees hired before January 1, 2011 share in a portion of their medical care cost, while employees hired subsequently are responsible for the full costs of

retiree medical benefits elected by them. The costs of postretirement benefits other than pensions are accrued during the years the employees render the services necessary to be eligible for these benefits.

The same benefit formula applies to all SCANA subsidiaries participating in the parent sponsored plans and, with regard to the pension plan, there are no legally separate asset pools. The postretirement benefit plans are accounted for as multiple employer plans. The information presented below reflects PSNC Energy's portion of the obligations, assets, funded status, net periodic benefit costs, and other information reported for the parent sponsored plans as a whole. The tabular data presented reflects the use of various cost assignment methodologies and participation assumptions based on PSNC Energy's past and current employees and its share of plan assets.

Changes in Benefit Obligation

The measurement date used to determine pension and other postretirement benefit obligations is December 31. Data related to the changes in the projected benefit obligation for pension benefits and the accumulated benefit obligation for other postretirement benefits are presented below.

	Pension Benefits		Other Postretirement Benefits	
Thousands of dollars	**2017**	**2016**	**2017**	**2016**
Benefit obligation, January 1	$ 96,838	$ 92,286	$ 30,848	$ 28,384
Service cost	2,692	2,468	588	590
Interest cost	4,000	4,158	1,510	1,605
Plan participants' contributions	—	—	174	220
Actuarial loss	7,605	3,948	2,284	1,932
Benefits paid	(7,088)	(6,022)	(1,643)	(1,475)
Amounts funded to parent	—	—	(269)	(408)
Benefit obligation, December 31	$ 104,047	$ 96,838	$ 33,492	$ 30,848

The accumulated benefit obligation for pension benefits was $101.0 million at the end of 2017 and $93.6 million at the end of 2016. The accumulated pension benefit obligation differs from the projected pension benefit obligation above in that it reflects no assumptions about future compensation levels.

Significant assumptions used to determine the above benefit obligations are as follows:

	Pension Benefits		Other Postretirement Benefits	
	2017	**2016**	**2017**	**2016**
Annual discount rate used to determine benefit obligation	3.71%	4.22%	3.74%	4.30%
Assumed annual rate of future salary increases for projected benefit obligation	3.00%	3.00%	3.00%	3.00%

A 7.0% annual rate of increase in the per capita cost of covered health care benefits was assumed for 2017. The rate was assumed to decrease gradually to 5.0% for 2023 and to remain at that level thereafter.

A one percent increase in the assumed health care cost trend rate would increase the postretirement benefit obligation approximately $0.2 million at December 31, 2017 and $0.1 million at December 31, 2016. A one percent decrease in the assumed health care cost trend rate would decrease the postretirement benefit obligation approximately $0.2 million at December 31, 2017 and $0.1 million at December 31, 2016.

Funded Status

Thousands of Dollars	Pension Benefits		Other Postretirement Benefits	
December 31,	2017	2016	2017	2016
Fair value of plan assets	$ 57,382	$ 48,623	$ —	$ —
Benefit obligation	104,047	96,838	33,492	30,848
Funded status	$ (46,665)	$ (48,215)	$ (33,492)	$ (30,848)

Amounts recognized on the consolidated balance sheets consist of:

Thousands of Dollars	Pension Benefits		Other Postretirement Benefits	
December 31,	2017	2016	2017	2016
Current liability	—	—	$ (2,054)	$ (1,679)
Noncurrent liability	$ (46,665)	$ (48,215)	(31,438)	(29,169)

Amounts recognized in accumulated other comprehensive loss (a component of common equity) were as follows:

Thousands of Dollars	Pension Benefits		Other Postretirement Benefits	
December 31,	2017	2016	2017	2016
Net actuarial loss	$ 1,090	$ 1,222	$ 344	$ 241
Prior service cost	6	13	—	—
Total	$ 1,096	$ 1,235	$ 344	$ 241

Amounts recognized in regulatory assets were as follows:

Thousands of Dollars	Pension Benefits		Other Postretirement Benefits	
December 31,	2017	2016	2017	2016
Net actuarial loss	$ 23,400	$ 27,332	$ 7,389	$ 5,401
Prior service cost	136	294	—	3
Total	$ 23,536	$ 27,626	$ 7,389	$ 5,404

Changes in Fair Value of Plan Assets

	Pension Benefits	
Thousands of dollars	2017	2016
Fair value of plan assets, January 1	$ 48,623	$ 48,137
Actual return on plan assets	15,847	6,629
Benefits paid	(7,088)	(6,143)
Fair value of plan assets, December 31	$ 57,382	$ 48,623

Investment Policies and Strategies

The assets of the pension plan are invested in accordance with the objectives of (1) fully funding the obligations of the pension plan, (2) overseeing the plan's investments in an asset-liability framework that considers the funding surplus (or deficit) between assets and liabilities, and overall risk associated with assets as compared to liabilities, and (3) maintaining sufficient liquidity to meet benefit payment obligations on a timely basis. The pension plan is closed to new entrants effective January 1, 2014, and benefit accruals will cease effective January 1, 2024. During 2013, in connection with the amendments to the plan, SCANA adopted a dynamic investment strategy for the management of the pension plan assets. The strategy will lead to a reduction in equities and an increase in long duration fixed income allocations over time with the intention of reducing volatility of funded status and pension costs.

The pension plan operates with several risk and control procedures, including ongoing reviews of liabilities, investment objectives, levels of diversification, investment managers and performance expectations. The total portfolio is constructed and maintained to provide prudent diversification with regard to the concentration of holdings in individual issues, corporations, or industries.

Transactions involving certain types of investments are prohibited. These include, except where utilized by a hedge fund manager, any form of private equity; commodities or commodity contracts (except for unleveraged stock or bond index futures and currency futures and options); ownership of real estate in any form other than publicly traded securities; short sales, warrants or margin transactions, or any leveraged investments; and natural resource properties. Investments made for the purpose of engaging in speculative trading are also prohibited.

The pension plan asset allocation at December 31, 2017 and 2016 and the target allocation for 2018 are as follows:

	Percentage of Plan Assets		
	Target Allocation	At December 31,	
Asset Category	**2018**	**2017**	**2016**
Equity Securities	58%	58%	57%
Fixed Income	33%	31%	32%
Hedge Funds	9%	11%	11%

For 2018, the expected long-term rate of return on assets will be 7.0%. In developing the expected long-term rate of return assumptions, management evaluates the pension plan's historical cumulative actual returns over several periods, considers the expected active returns across various asset classes and assumes an asset allocation is achieved. Management regularly reviews such allocations and periodically rebalances the portfolio when considered appropriate. Additional rebalancing may occur subject to funded status improvements as part of the dynamic investment policy described previously.

Fair Value Measurements

Assets held by the pension plan are measured at fair value as described below. Assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. At December 31, 2017 and 2016, fair value measurements, and the level within the fair value hierarchy in which the measurements fall, were as follows:

Thousands of dollars	**2017**	**2016**
Investments with fair value measure at Level 2:		
Mutual funds	$ 8,091	$ 7,654
Short-term investment vehicles	1,170	976
US Treasury securities	1,032	1,122
Corporate debt securities	6,166	5,016
Municipals	1,128	873
Total assets in the fair value hierarchy	$ 17,587	$ 15,641
Investments at net asset value:		
Common collective trust	$ 33,603	$ 27,723
Joint venture interests	6,192	5,259
Total investments at fair value	$ 57,382	$ 48,623

At December 31, 2017, assets with fair value measurements classified as Level 1 were insignificant. There were no transfers of fair value amounts into or out of Levels 1, 2 or 3 during 2017 or 2016.

Mutual funds held by the plan are open-ended mutual funds registered with the Securities and Exchange Commission. The price of the mutual funds' shares is based on its Net Asset Value (NAV), which is determined by dividing the total value of portfolio investments, less any liabilities, by the total number of shares outstanding. For purposes of calculating NAV, portfolio securities and other assets for which market quotes are readily available are valued at market value. Short-term investment vehicles are funds that invest in short-term fixed income instruments and are valued using observable prices of the underlying fund assets based on trade data for identical or similar securities. US Treasury securities are valued using quoted market prices or based on models using observable inputs from market sources such as external prices or spreads or benchmarked thereto. Corporate debt securities and municipals are valued based on recently executed transactions, using quoted market prices, or based on models using observable inputs from market sources such as external prices or spreads or benchmarked thereto. Common collective trust assets and limited partnerships are valued at NAV, which has been determined based on the unit values of the trust funds. Unit values are determined by the organization sponsoring such trust funds by dividing the trust funds' net assets at fair value by the units outstanding at each valuation date. Joint venture interests assets are invested in a hedge fund of funds partnership that invests directly in multiple hedge fund strategies that are not traded on exchanges and not traded on a daily basis. The valuation of such multi-strategy hedge fund of funds is estimated based on the NAV of the underlying hedge fund strategies using consistent valuation guidelines that account for variations that may influence their fair value.

Expected Cash Flows

The total benefits expected to be paid from the pension plan or from the Company's assets for the other postretirement benefits plan (net of participant contributions), respectively, are as follows:

Expected Benefit Payments

Thousands of dollars	**Pension Benefits**	**Other Postretirement Benefits**
2018	$ 66,888	$ 2,092
2019	64,621	2,220
2020	63,894	2,335
2021	66,493	2,433
2022	71,986	2,501
2023-2027	302,976	13,247

Pension Plan Contributions

The pension trust is adequately funded under current regulations. No contributions have been required since 1997, and as a result of closing the plan to new entrants and freezing benefit accruals in the future, PSNC does not anticipate making significant contributions to the pension plan for the foreseeable future.

Net Periodic Benefit Cost

PSNC Energy records net periodic benefit cost utilizing beginning of the year assumptions. Disclosures required for these plans are set forth in the following tables.

Components of Net Periodic Benefit Cost

	Pension Benefits		**Other Postretirement Benefits**	
Thousands of dollars	**2017**	**2016**	**2017**	**2016**
Service cost	$ 2,692	$ 2,468	$ 588	$ 590
Interest cost	4,000	4,158	1,510	1,605
Expected return on assets	(5,853)	(5,901)	n/a	n/a
Prior service cost amortization	175	418	3	42
Amortization of actuarial losses	1,745	1,563	133	64
Net periodic benefit cost	$ 2,759	$ 2,706	$ 2,234	$ 2,301

Other changes in plan assets and benefit obligations recognized in OCI (net of tax) were as follows:

	Pension Benefits		Other Postretirement Benefits	
Thousands of dollars	**2017**	**2016**	**2017**	**2016**
Current year actuarial (gain) loss	$ (59)	$ 167	$ 109	$ 84
Amortization of actuarial losses	(73)	(65)	(6)	(3)
Amortization of prior service cost	(7)	(17)	—	(2)
Total recognized in OCI	$ (139)	$ 85	$ 103	$ 79

Other changes in plan assets and benefit obligations recognized in regulatory assets were as follows:

	Pension Benefits		Other Postretirement Benefits	
Thousands of dollars	**2017**	**2016**	**2017**	**2016**
Current year actuarial (gain) loss	$ (2,298)	$ 3,136	$ 2,114	$ 1,798
Amortization of actuarial losses	(1,634)	(1,490)	(126)	(59)
Amortization of prior service cost	(158)	(401)	(3)	(38)
Total recognized in regulatory assets	$ (4,090)	$ 1,245	$ 1,985	$ 1,701

Significant Assumptions Used in Determining Net Periodic Benefit Cost

	Pension Benefits		Other Postretirement Benefits	
	2017	**2016**	**2017**	**2016**
Discount rate	4.22%	4.68%	4.30%	4.78%
Expected return on plan assets	7.25%	7.50%	n/a	n/a
Rate of compensation increase	3.00%	3.00%	3.00%	3.00%
Health care cost trend rate	n/a	n/a	6.60%	7.00%
Ultimate health care cost trend rate	n/a	n/a	5.00%	5.00%
Year achieved	n/a	n/a	2021	2021

The actuarial loss and prior service cost to be amortized from accumulated other comprehensive loss into net periodic benefit cost in 2018 are as follows:

Thousands of Dollars	**Pension Benefits**	**Other Postretirement Benefits**
Actuarial loss	$ 57	$ 14
Prior service cost	3	—
Total	$ 60	$ 14

The estimated amounts to be amortized from regulatory assets into net periodic benefit cost in 2018 are as follows:

Thousands of Dollars	**Pension Benefits**	**Other Postretirement Benefits**
Actuarial loss	$ 1,230	$ 305
Prior service cost	54	—
Total	$ 1,284	$ 305

Other postretirement benefit costs are subject to annual per capita limits pursuant to the plan's design. As a result, the effect of a one-percent increase or decrease in the assumed health care cost trend rate on total service and interest cost is not significant.

401(k) Retirement Savings Plan

PSNC Energy participates in a SCANA-sponsored defined contribution plan in which eligible employees may defer up to 75% of eligible earnings subject to certain limits and may diversify their investments. Employee deferrals are fully vested and nonforfeitable at all times. PSNC Energy provides 100% matching contributions up to 6% of an employee's eligible earnings. Total matching contributions made to the plan were $3.4 million in each of 2017 and 2016.

8. COMMITMENTS AND CONTINGENCIES

The Company is subject to various claims and litigation incidental to its business operations which management anticipates will be resolved without material adverse impact on the Company's results of operations, cash flows or financial condition.

Operating Lease Commitments

PSNC Energy is obligated under various operating leases for office space, furniture and equipment. Leases expire at various dates through 2022. Rent expense totaled approximately $0.5 million for each of the years 2017 and 2016. Future minimum rental payments under such leases are as follows:

	Thousands of dollars
2018	$ 486
2019	404
2020	279
2021	138
2022	45
Thereafter	—
Total	$ 1,352

Asset Retirement Obligations

The Company recognizes a liability for the present value of an ARO when incurred if the liability can be reasonably estimated. Uncertainty about the timing or method of settlement of a conditional ARO is factored into the measurement of the liability when sufficient information exists, but such uncertainty is not a basis upon which to avoid liability recognition.

The legal obligations associated with the retirement of long-lived tangible assets that result from their acquisition, construction, development and normal operation relate primarily to the Company's transmission and distribution properties held by its regulated utility. All of the amounts recorded are based upon estimates which are subject to varying degrees of precision, particularly since such payments will be made many years in the future.

A reconciliation of the beginning and ending aggregate carrying amount of AROs is as follows:

Thousands of dollars	2017	2016
Beginning balance	$ 35,607	$ 31,833
Liabilities incurred	—	—
Liabilities settled	—	(218)
Accretion expense	1,464	1,456
Revisions in estimated cash flows	1,610	2,536
Ending balance	$ 38,681	$ 35,607

In 2017 and 2016, revisions in estimated cash flows relate primarily to increased gas utility plant.

9. AFFILIATED TRANSACTIONS

PSNC Energy owns, through its wholly owned subsidiaries, 17% of Pine Needle LNG Company, L.L.C. (Pine Needle), an LNG storage facility in North Carolina, and 33.2% of Cardinal Pipeline Company, L.L.C. (Cardinal), an intrastate natural gas pipeline. PSNC Energy accounts for each of these investments using the equity method. These equity method investees recorded losses in 2017 in connection with their adoption of the Tax Act. PSNC Energy's portion of these losses totaled approximately $6.9 million.

The Company records as cost of gas the storage and transportation costs charged by its equity method investees. These costs totaled $10.1 million and $12.0 million in 2017 and 2016, respectively. The Company owed these investees $0.8 million at December 31, 2017 and $1.0 million at December 31, 2016. The Company received cash distributions representing earnings on invested capital from these investees of $2.8 million during 2017 and $3.7 million during 2016.

Pine Needle and Cardinal use interest rate swaps designated as cash flow hedges to manage interest rate risk on variable rate debt instruments by converting them synthetically to a fixed rate. The Company's share of the effective portion of changes in the fair value of these interest rate swaps are recorded in AOCI in the Company's consolidated balance sheets.

PSNC Energy had sales to an affiliate for natural gas and transportation services of $1.8 million during 2017 and $1.7 million during 2016. Purchases of natural gas from an affiliate were insignificant during 2017 and 2016.

SCANA Services, Inc., on behalf of itself and its parent company, provides the following services to PSNC Energy at direct or allocated cost: gas services, information systems services, telecommunications services, customer services, marketing and sales, human resources, corporate compliance, purchasing, financial services, risk management, public affairs, legal services, investor relations, gas supply and capacity management, strategic planning, general administrative services, and retirement benefits. Costs for these services totaled $56.4 million in 2017 and $67.7 million in 2016. In addition, SCANA Services, Inc., processes and pays invoices for PSNC Energy and is reimbursed. PSNC Energy's payables to SCANA Services, Inc., were $7.3 million at December 31, 2017 and $9.2 million at December 31, 2016.

Money pool transactions with an affiliate are described in consolidated Note 3.

10. SUBSEQUENT EVENT

On January 2, 2018, SCANA, Sedona Corp. and Dominion Energy, Inc. (Dominion Energy) entered into a merger agreement pursuant to which Sedona Corp. (a wholly-owned subsidiary of Dominion Energy) agreed to merge into SCANA in a stock-for-stock transaction in which SCANA shareholders would receive 0.6690 of a share of Dominion Energy common stock for each share of SCANA common stock. The completion of the merger is subject to a variety of closing conditions, including the receipt of approvals from SCANA's shareholders and is also subject to consents and approvals or findings from governmental entities, including the NCUC, which may impose conditions that could have an adverse effect on SCANA or could cause either SCANA or Dominion Energy to abandon the merger. See also Note 2 and Note 3.