

AGL RESOURCES INC
Form 10-Q
October 30, 2008

Glossary of Terms

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark

One)

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

For the Quarterly Period Ended September 30, 2008

OR

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

For the transition period from to

Commission File Number 1-14174

AGL RESOURCES INC.

(Exact name of registrant as specified in its charter)

Georgia

(State or other jurisdiction of incorporation or
organization)

58-2210952

(I.R.S. Employer Identification No.)

Ten Peachtree Place NE, Atlanta, Georgia 30309
(Address and zip code of principal executive offices)

404-584-4000

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting
company)

Smaller reporting company

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

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

Class	Outstanding as of October 22, 2008
Common Stock, \$5.00 Par Value	76,780,439

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GLOSSARY OF KEY TERMS

AFUDC	Allowance for funds used during construction, which has been authorized by applicable state regulatory agencies to record the cost of debt and equity funds as part of the cost of construction projects
AGL Capital	AGL Capital Corporation
AGL Networks	AGL Networks, LLC
Atlanta Gas Light	Atlanta Gas Light Company
Bcf	Billion cubic feet
Chattanooga Gas	Chattanooga Gas Company
Credit Facility	Credit agreements supporting our commercial paper program
EBIT	Earnings before interest and taxes, a non-GAAP measure that includes operating income, other income, minority interest in SouthStar's earnings and gain on sales of assets and excludes interest and income tax expense; as an indicator of our operating performance, EBIT should not be considered an alternative to, or more meaningful than, operating income or net income as determined in accordance with GAAP
EITF	Emerging Issues Task Force
ERC	Environmental remediation costs associated with our distribution operations segment which are recoverable through rates mechanisms
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
FIN	FASB Interpretation Number
Fitch	Fitch Ratings
Florida Public Service Commission	Florida Public Service Commission
FSP	FASB Staff Position
GAAP	Accounting principles generally accepted in the United States of America
Georgia Public Service Commission	Georgia Public Service Commission
GNG	Georgia Natural Gas, the name under which SouthStar does business in Georgia
Golden Triangle Storage	Golden Triangle Storage, Inc.
Heating Degree Days	A measure of the effects of weather on our businesses, calculated when the average daily actual temperatures are less than a baseline temperature of 65 degrees Fahrenheit.
Heating Season	The period from November to March when natural gas usage and operating revenues are generally higher because more customers are connected to our distribution systems when weather is colder
Jefferson Island	Jefferson Island Storage & Hub, LLC
LOCOM	Lower of weighted average cost or current market price
Maryland Public Service Commission	Maryland Public Service Commission
Marketers	Marketers selling retail natural gas in Georgia and certificated by the Georgia Commission
MMBtu	NYMEX equivalent contract units of 10,000 million British thermal units
Moody's	Moody's Investors Service
New Jersey Commission	New Jersey Board of Public Utilities
NYMEX	New York Mercantile Exchange, Inc.
OCI	Other comprehensive income
Operating margin	

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A non-GAAP measure of income, calculated as revenues minus cost of gas, that excludes operation and maintenance expense, depreciation and amortization, taxes other than income taxes, and the gain or loss on the sale of our assets; these items are included in our calculation of operating income as reflected in our statements of consolidated income. Operating margin should not be considered an alternative to, or more meaningful than operating income or net income as determined in accordance with GAAP

OTC	Over-the-counter
Piedmont	Piedmont Natural Gas
Pivotal Utility	Pivotal Utility Holdings, Inc., doing business as Elizabethtown Gas, Elkton Gas and Florida City Gas
PGA	Purchased gas adjustment
PP&E	Property, plant and equipment
PRP	Pipeline replacement program for Atlanta Gas Light
S&P	Standard & Poor's Ratings Services
SEC	Securities and Exchange Commission
Sequent	Sequent Energy Management, L.P.
SFAS	Statement of Financial Accounting Standards
SouthStar	SouthStar Energy Services LLC
VaR	Value at risk is defined as the maximum potential loss in portfolio value over a specified time period that is not expected to be exceeded within a given degree of probability
Virginia Natural Gas	Virginia Natural Gas, Inc.
V i r g i n i a Commission	Virginia State Corporation Commission
WACOG	Weighted average cost of gas
WNA	Weather normalization adjustment

REFERENCED ACCOUNTING STANDARDS

FSP FIN 39-1	FASB Staff Position 39-1 "Amendment of FIN 39"
FIN 46 & FIN 46R	FIN 46, "Consolidation of Variable Interest Entities"
FIN 48	FIN 48, "Accounting for Uncertainty in Income Taxes, an interpretation of SFAS Statement No. 109"
FSP EITF 03-6-1	FSP EITF 03-6-1, "Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities"
FSP EITF 06-3	FSP EITF 06-3, "How Taxes Collected from Customers and Remitted to Governmental Authorities Should be Presented in the Income Statement (That Is, Gross versus Net Presentation)"
FSP FAS 133-1	FSP No. FAS 133-1, "Disclosures about Credit Derivatives and Certain Guarantees: An Amendment of FASB Statement No. 133"
FSP FAS 157-3	FSP No. FAS 157-3, "Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active"
SFAS 71	SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation"
SFAS 133	SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities"
SFAS 141	SFAS No. 141, "Business Combinations"
SFAS 157	SFAS No. 157, "Fair Value Measurements"
SFAS 160	SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements"
SFAS 161	SFAS No. 161, "Disclosure about Derivative Instruments and Hedging Activities, an amendment of SFAS 133"

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PART 1 – Financial Information

Item 1. Financial Statements

AGL RESOURCES INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

In millions, except share data	September 30, 2008	As of December 31, 2007	September 30, 2007
Current assets			
Cash and cash equivalents	\$ 11	\$ 19	\$ 14
Energy marketing receivables	535	598	363
Inventories	811	551	654
Receivables (less allowance for uncollectible accounts of \$17 at Sept. 30, 2008, \$14 at Dec. 31, 2007 and \$15 at Sept. 30, 2007)	189	391	143
Energy marketing and risk management assets	172	69	90
Unrecovered PRP costs – current portion	40	31	27
Unrecovered ERC – current portion	20	23	24
Other current assets	162	115	100
Total current assets	1,940	1,797	1,415
Property, plant and equipment			
Property, plant and equipment	5,377	5,177	5,142
Less accumulated depreciation	1,651	1,611	1,610
Property, plant and equipment-net	3,726	3,566	3,532
Deferred debits and other assets			
Goodwill	418	420	420
Unrecovered PRP costs	202	254	261
Unrecovered ERC	124	135	132
Other	94	86	71
Total deferred debits and other assets	838	895	884
Total assets	\$ 6,504	\$ 6,258	\$ 5,831
Current liabilities			
Short-term debt	\$ 769	\$ 580	\$ 576
Energy marketing trade payables	568	578	383
Accounts payable - trade	181	172	131
Accrued expenses	83	87	82
Accrued PRP costs – current portion	43	55	47
Customer deposits	39	35	39
Energy marketing and risk management liabilities – current portion	34	16	9
Deferred purchased gas adjustment	14	28	15
	16	10	11

Accrued environmental remediation liabilities – current portion			
Other current liabilities	75	73	73
Total current liabilities	1,822	1,634	1,366
Accumulated deferred income taxes	625	566	527
Long-term liabilities and other deferred credits (excluding long-term debt)			
Accumulated removal costs	176	169	168
Accrued PRP costs	152	190	204
Accrued environmental remediation liabilities	89	97	88
Accrued pension obligations	43	43	83
Accrued postretirement benefit costs	19	24	25
Other long-term liabilities and other deferred credits	150	152	158
Total long-term liabilities and other deferred credits (excluding long-term debt)	629	675	726
Commitments and contingencies (Note 6)			
Minority interest	29	47	41
Capitalization			
Long-term debt	1,675	1,675	1,548
Common shareholders' equity, \$5 par value; 750,000,000 shares authorized	1,724	1,661	1,623
Total capitalization	3,399	3,336	3,171
Total liabilities and capitalization	\$ 6,504	\$ 6,258	\$ 5,831

See Notes to Condensed Consolidated Financial Statements (Unaudited).

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AGL RESOURCES INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED)

	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
In millions, except per share amounts				
Operating revenues	\$ 539	\$ 369	\$ 1,995	\$ 1,809
Operating expenses				
Cost of gas	261	159	1,193	987
Operation and maintenance	104	107	337	334
Depreciation and amortization	38	37	112	108
Taxes other than income taxes	10	11	33	31
Total operating expenses	413	314	1,675	1,460
Operating income	126	55	320	349
Other income	2	-	6	1
Minority interest	5	-	(12)	(24)
Interest expense, net	(29)	(34)	(85)	(92)
Earnings before income taxes	104	21	229	234
Income tax expense	39	8	86	89
Net income	\$ 65	\$ 13	\$ 143	\$ 145
Per common share data				
Basic earnings per common share	\$ 0.85	\$ 0.17	\$ 1.87	\$ 1.88
Diluted earnings per common share	\$ 0.85	\$ 0.17	\$ 1.87	\$ 1.87
Cash dividends declared per common share	\$ 0.42	\$ 0.41	\$ 1.26	\$ 1.23
Weighted-average number of common shares outstanding				
Basic	76.4	77.0	76.2	77.4
Diluted	76.6	77.4	76.5	77.8

See notes to Condensed Consolidated Financial Statements (Unaudited).

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AGL RESOURCES INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMMON SHAREHOLDERS' EQUITY
(UNAUDITED)

In millions, except per share amount	Common stock		Premium on common stock	Earnings reinvested	Other comprehensive loss	Shares held in treasury and trust	Total
	Shares	Amount					
Balance as of December 31, 2007	76.4	\$ 390	\$ 667	\$ 680	\$ (13)	\$ (63)	\$ 1,661
Comprehensive income:							
Net income	-	-	-	143	-	-	143
Net realized gains from hedging activities (net of tax of \$-)	-	-	-	-	(1)	-	(1)
Total comprehensive income							142
Dividends on common stock (\$1.26 per share)	-	-	-	(96)	-	3	(93)
Issuance of treasury shares	0.4	-	(1)	(4)	-	12	7
Stock-based compensation expense (net of tax of \$1)	-	-	7	-	-	-	7
Balance as of September 30, 2008	76.8	\$ 390	\$ 673	\$ 723	\$ (14)	\$ (48)	\$ 1,724

See Notes to Condensed Consolidated Financial Statements (Unaudited).

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AGL RESOURCES INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (UNAUDITED)

In millions	Nine months ended September 30,	
	2008	2007
Cash flows from operating activities		
Net income	\$ 143	\$ 145
Adjustments to reconcile net income to net cash flow provided by operating activities		
Depreciation and amortization	112	108
Change in energy marketing and risk management assets and liabilities	(86)	27
Minority interest	12	24
Deferred income taxes	66	8
Changes in certain assets and liabilities		
Gas, unbilled and other receivables	202	232
Energy marketing receivables and energy marketing trade payables, net	53	15
Inventories	(260)	(57)
Gas and trade payables	9	(82)
Other – net	(79)	(34)
Net cash flow provided by operating activities	172	386
Cash flows from investing activities		
Property, plant and equipment expenditures	(254)	(193)
Other	-	2
Net cash flow used in investing activities	(254)	(191)
Cash flows from financing activities		
Net payments and borrowings of short-term debt	189	49
Issuance of variable rate gas facility revenue bonds	161	-
Payments of long-term debt	(161)	(86)
Dividends paid on common shares	(93)	(92)
Distribution to minority interest	(30)	(23)
Issuance of treasury shares	7	13
Purchase of treasury shares	-	(57)

Other	1	(2)
Net cash flow provided by (used in) financing activities	74	(198)
Net decrease in cash and cash equivalents	(8)	(3)
Cash and cash equivalents at beginning of period	19	17
Cash and cash equivalents at end of period	\$ 11	\$ 14
Cash paid during the period for		
Interest	\$ 88	\$ 92
Income taxes	\$ 27	\$ 89

See Notes to Condensed Consolidated Financial Statements (Unaudited).

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AGL RESOURCES INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note 1 - Accounting Policies and Methods of Application

General

AGL Resources Inc. is an energy services holding company that conducts substantially all its operations through its subsidiaries. Unless the context requires otherwise, references to “we,” “us,” “our,” or “the company” mean consolidated AGL Resources Inc. and its subsidiaries (AGL Resources).

The year-end condensed balance sheet data was derived from our audited financial statements, but does not include all disclosures required by GAAP. We have prepared the accompanying unaudited condensed consolidated financial statements under the rules of the SEC. Under such rules and regulations, we have condensed or omitted certain information and notes normally included in financial statements prepared in conformity with GAAP. However, the condensed consolidated financial statements reflect all adjustments of a normal recurring nature that are, in the opinion of management, necessary for a fair presentation of our financial results for the interim periods. For a glossary of key terms and referenced accounting standards, see page 3. You should read these condensed consolidated financial statements in conjunction with our consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2007, filed with the SEC on February 7, 2008.

Due to the seasonal nature of our business, our results of operations for the three and nine months ended September 30, 2008 and 2007, and our financial condition as of December 31, 2007, and September 30, 2008 and 2007, are not necessarily indicative of the results of operations and financial condition to be expected as of or for any other period.

Basis of Presentation

Our condensed consolidated financial statements include our accounts, the accounts of our majority-owned and controlled subsidiaries and the accounts of variable interest entities for which we are the primary beneficiary. This means that our accounts are combined with our subsidiaries’ accounts. We have eliminated any intercompany profits and transactions in consolidation; however, we have not eliminated intercompany profits when such amounts are probable of recovery under the affiliates’ rate regulation process. Certain amounts from prior periods have been reclassified and revised to conform to the current period presentation.

We currently own a noncontrolling 70% financial interest in SouthStar and Piedmont owns the remaining 30%. Our 70% interest is noncontrolling because all significant management decisions require approval by both owners. We record the earnings allocated to Piedmont as a minority interest in our condensed consolidated statements of income and we record Piedmont’s portion of SouthStar’s capital as a minority interest in our condensed consolidated balance sheets.

We are the primary beneficiary of SouthStar’s activities and have determined that SouthStar is a variable interest entity as defined by FIN 46, which was revised in December 2003, FIN 46R. We determined that SouthStar is a variable interest entity because our equal voting rights with Piedmont are not proportional to our contractual obligation to absorb 75% of any losses or residual returns from SouthStar, except those losses and returns related to customers in Ohio and Florida. Earnings related to SouthStar’s customers in Ohio and Florida are allocated 70% to us and 30% to Piedmont. In addition, SouthStar obtains substantially all its transportation capacity for delivery of natural gas through our wholly owned subsidiary, Atlanta Gas Light.

Use of Accounting Estimates

The preparation of our financial statements in conformity with GAAP requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and the related disclosures of contingent assets and liabilities. We based our estimates on historical experience and various other assumptions that we believe to be reasonable under the circumstances, and we evaluate our estimates on an ongoing basis. Each of our estimates involves complex situations requiring a high degree of judgment either in the application and interpretation of existing literature or in the development of estimates that impact our financial statements. The most significant estimates include our PRP accruals, environmental liability accruals, allowance for uncollectible accounts and other contingencies, pension and postretirement obligations, derivative and hedging activities, unbilled revenues and provision for income taxes. Our actual results could differ from our estimates, and such differences could be material.

Inventories

For our distribution operations segment, we record natural gas stored underground at WACOG. For Sequent and SouthStar, we account for natural gas inventory at the lower of WACOG or market price.

Sequent and SouthStar evaluate the average cost of their natural gas inventories against market prices to determine whether any declines in market prices below the WACOG are other than temporary. For any declines considered to be other than temporary, we record adjustments to reduce the weighted average cost of the natural gas inventory to market price. SouthStar recorded LOCOM adjustments of \$18 million in the three and nine months ended September 30, 2008 and did not record LOCOM adjustments in 2007. Sequent recorded LOCOM adjustments of \$34 million in the three and nine months ended September 30, 2008 and \$1 million and \$4 million for the three and nine months ended September 30, 2007, respectively.

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Stock-Based Compensation

In the first nine months of 2008, we issued grants of approximately 258,000 stock options and 207,000 restricted stock units, which will result in the recognition of approximately \$2 million of stock-based compensation expense in 2008. No material share awards have been granted to employees whose compensation is subject to capitalization. We use the Black-Scholes pricing model to determine the fair value of the options granted. On an annual basis, we evaluate the assumptions and estimates used to calculate our stock-based compensation expense.

There have been no significant changes to our stock-based compensation, as described in Note 4 to our Consolidated Financial Statements in Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2007.

Comprehensive Income

Our comprehensive income includes net income plus OCI, which includes other gains and losses affecting shareholders' equity that GAAP excludes from net income. Such items consist primarily of gains and losses on certain derivatives designated as cash flow hedges and unfunded or over funded pension and postretirement obligations. The following table illustrates our OCI activity.

In millions	Three months ended September 30,	
	2008	2007
Cash flow hedges:		
Net derivative unrealized gains (losses) arising during the period (net of taxes of \$- in 2008 and \$1 in 2007)	\$ (1)	\$ 2
Less reclassification of realized losses included in income (net of taxes of \$- in 2008 and \$1 in 2007)	1	1
Total	\$ -	\$ 3

In millions	Nine months ended September 30,	
	2008	2007
Cash flow hedges:		
Net derivative unrealized gains arising during the period (net of taxes of \$2 in 2008 and \$1 in 2007)	\$ 3	\$ 2
Less reclassification of realized gains included in income (net of taxes of \$3 in 2008 and \$3 in 2007)	(4)	(5)
Pension adjustments (net of taxes of \$- in 2007)	-	1
Total	\$ (1)	\$ (2)

Earnings per Common Share

We compute basic earnings per common share by dividing our income available to common shareholders by the weighted-average number of common shares outstanding daily. Diluted earnings per common share reflect the potential reduction in earnings per common share that could occur when potentially dilutive common shares are added to common shares outstanding.

We derive our potentially dilutive common shares by calculating the number of shares issuable under restricted stock, restricted stock units and stock options. The future issuance of shares underlying the restricted stock and restricted share units depends on the satisfaction of certain performance criteria. The future issuance of shares underlying the outstanding stock options depends upon whether the exercise prices of the stock options are less than the average market price of the common shares for the respective periods. The following table shows the calculation of our diluted shares, assuming restricted stock and restricted stock units currently awarded under the plan ultimately vest and stock

options currently exercisable at prices below the average market prices are exercised.

In millions	Three months ended September 30,	
	2008	2007
Denominator for basic earnings per share (1)	76.4	77.0
Assumed exercise of restricted stock, restricted stock units and stock options	0.2	0.4
Denominator for diluted earnings per share (1) Daily weighted-average shares outstanding.	76.6	77.4

In millions	Nine months ended September 30,	
	2008	2007
Denominator for basic earnings per share (1)	76.2	77.4
Assumed exercise of restricted stock, restricted stock units and stock options	0.3	0.4
Denominator for diluted earnings per share (1) Daily weighted-average shares outstanding.	76.5	77.8

The following table contains the weighted average shares attributable to outstanding stock options that were excluded from the computation of diluted earnings per share because their effect would have been anti-dilutive, as the exercise prices were greater than the average market price:

In millions	September 30,	
	2008	2007 (1)
Three months ended	2.1	0.1
Nine months ended	1.6	0.0

(1) 0.0 values represent amounts less than 0.1 million.

The increase in the number of shares that were excluded from the computation is the result of a significant decline in the market value of our common shares at September 30, 2008 as compared to September 30, 2007.

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Income Taxes

We adopted FIN 48 on January 1, 2007, and as of September 30, 2008, December 31, 2007 or September 30, 2007, we did not have a liability for unrecognized tax benefits.

We do not collect income taxes from our customers on behalf of governmental authorities. We do collect and remit state and local taxes and record these amounts within our condensed consolidated balance sheets. Therefore, EITF No. 06-3 does not apply to us.

There have been no significant changes to our income taxes as described in Note 8 to our Consolidated Financial Statements in Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2007.

Regulatory Assets and Liabilities

We have recorded regulatory assets and liabilities in our condensed consolidated balance sheets in accordance with SFAS 71. Our regulatory assets and liabilities, and associated liabilities for our unrecovered PRP costs, unrecovered ERC and the associated assets and liabilities for our Elizabethtown Gas hedging program, are summarized in the following table.

	Sept. 30 2008	Dec. 31 2007	Sept. 30 2007
In millions			
Regulatory assets			
Unrecovered PRP costs			