NEW JERSEY RESOURCES CORP
Form 10-Q
August 04, 2010

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

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2010

OR

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

FOR THE TRANSITION PERIOD FROM TO

Commission file number 001-8359

NEW JERSEY RESOURCES CORPORATION
(Exact name of registrant as specified in its charter)

New Jersey (State or other jurisdiction of incorporation or organization)	22-2376465 (I.R.S. Employer Identification Number)
1415 Wyckoff Road, Wall, New Jersey 07719 (Address of principal executive offices)	732-938-1480 (Registrant's telephone number, including area code)

Securities registered pursuant to Section 12 (b) of the Act:

Common Stock - $2.50 Par Value (Title of each class)	New York Stock Exchange (Name of each exchange on which registered)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes: x No: o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated, or a smaller reporting company. See definition of “large accelerated filer”, “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer: x Accelerated filer: o Non-accelerated filer: o Smaller reporting company: o
(Do not check if a smaller
reporting company)

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

Yes: o No: x

The number of shares outstanding of $2.50 par value Common Stock as of August y, 2010, was yy,yyy,yyy.

New Jersey Resources Corporation

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Part I

INFORMATION CONCERNING FORWARD-LOOKING STATEMENTS

Certain statements contained in this report, including, without limitation, statements as to management expectations and beliefs presented in Part I, Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations," Part I, Item 3. "Quantitative and Qualitative Disclosures about Market Risk," Part II, Item I. "Legal Proceedings" and in the notes to the financial statements are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements can also be identified by the use of forward-looking terminology such as "may," "intend," "expect," "believe" or "continue" or comparable terminology and a made based upon management's current expectations and beliefs as of this date concerning future developments and their potential effect upon New Jersey Resources Corporation (NJR or the Company). There can be no assurance that future developments will be in accordance with management's expectations or that the effect of future developments on the Company will be those anticipated by management.

The Company cautions readers that the assumptions that form the basis for forward-looking statements regarding customer growth, customer usage, financial condition, results of operations, cash flows, capital requirements, market risk and other matters for fiscal 2010 and thereafter include many factors that are beyond the Company's ability to control or estimate precisely, such as estimates of future market conditions, the behavior of other market participants and changes in the debt and equity capital markets. The factors that could cause actual results to differ materially from NJR's expectations include, but are not limited to, those discussed in Risk Factors in Item 1A of NJR's 2009 Annual Report on Form 10-K and Part II, Item 1A of this Form 10-Q, as well as the following:

- weather and economic conditions;
- NJR's dependence on operating subsidiaries;
- demographic changes in the New Jersey Natural Gas (NJNG) service territory;
- the rate of NJNG customer growth;
- volatility of natural gas and other commodity prices and their impact on customer usage, NJR Energy Services' (NJRES) operations and on the Company's risk management efforts;
- changes in rating agency requirements and/or credit ratings and their effect on availability and cost of capital to the Company;
- the impact of volatility in the credit markets that would result in the increased cost and/or limit the availability of credit at NJR to fund and support physical gas inventory purchases and other working capital needs at NJRES, and all other non-regulated subsidiaries, as well as negatively affect cost and access to the commercial paper market and other short-term financing markets by NJNG to allow it to fund its commodity purchases, capital expenditures and meet its short-term obligations as they come due;
- the ability to comply with debt covenants;
- continued failures in the market for auction rate securities;
- the impact to the asset values and resulting higher costs and funding obligations of NJR's pension and postemployment benefit plans as a result of downturns in the financial markets, and impacts associated with the Patient Protection and Affordable Care Act;
- the ability to maintain effective internal controls;
- accounting effects and other risks associated with hedging activities and use of derivatives contracts;
- commercial and wholesale credit risks, including the availability of creditworthy customers and counterparties and liquidity in the wholesale energy trading market;

- Ÿthe ability to obtain governmental approvals and/or financing for the construction, development and operation of certain non-regulated energy investments;
- Ÿrisks associated with the management of the Company's joint ventures and partnerships;
- Ÿrisks associated with our investments in solar energy projects, including the availability of regulatory and tax incentives;
- Ÿthe level and rate at which costs and expenses are incurred and the extent to which they are allowed to be recovered from customers through the regulatory process in connection with constructing, operating and maintaining NJNG's natural gas transmission and distribution system;
- Ÿdependence on third-party storage and transportation facilities for natural gas supply;
- Ÿoperating risks incidental to handling, storing, transporting and providing customers with natural gas;
- Ÿaccess to adequate supplies of natural gas;
- Ÿthe regulatory and pricing policies of federal and state regulatory agencies;
- Ÿthe costs of compliance with present and future environmental laws, including potential climate change-related legislation;
- Ÿthe ultimate outcome of pending regulatory proceedings;
- Ÿthe disallowance of recovery of environmental-related expenditures and other regulatory changes; and
- Ÿenvironmental-related and other litigation and other uncertainties.

While the Company periodically reassesses material trends and uncertainties affecting the Company's results of operations and financial condition in connection with its preparation of management's discussion and analysis of results of operations and financial condition contained in its Quarterly and Annual Reports, the Company does not, by including this statement, assume any obligation to review or revise any particular forward-looking statement referenced herein in light of future events.

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ITEM 1. FINANCIAL STATEMENTS

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

	Three Months Ended June 30,		Nine Months Ended June 30,	
(Thousands, except per share data)	2010	2009	2010	2009
OPERATING REVENUES				
Utility	$105,130	$148,826	$ 794,311	$ 958,995
Nonutility	374,764	292,226	1,213,475	1,220,877
Total operating revenues	479,894	441,052	2,007,786	2,179,872
OPERATING EXPENSES				
Gas purchases:				
Utility	47,665	87,169	478,719	631,712
Nonutility	393,126	313,318	1,114,842	1,227,783
Operation and maintenance	37,077	38,436	110,386	112,209
Regulatory rider expenses	6,160	6,280	41,017	40,585
Depreciation and amortization	8,136	7,880	23,936	22,749
Energy and other taxes	6,516	11,739	50,275	67,353
Total operating expenses	498,680	464,822	1,819,175	2,102,391
OPERATING (LOSS) INCOME	(18,786)	(23,770)	188,611	77,481
Other income	1,311	1,179	3,458	3,095
Interest expense, net of capitalized interest	5,238	5,187	15,946	15,953
(LOSS) INCOME BEFORE INCOME TAXES AND EQUITY IN EARNINGS OF AFFILIATES	(22,713)	(27,778)	176,123	64,623
Income tax (benefit) provision	(11,368)	(12,146)	64,819	21,296
Equity in earnings of affiliates, net of tax	1,168	1,477	4,638	2,778
NET (LOSS) INCOME	$ (10,177)	$ (14,155)	$ 115,942	$ 46,105
(LOSSES) EARNINGS PER COMMON SHARE				
BASIC	$(0.25)	$(0.34)	$2.80	$1.09
DILUTED	$(0.25)	$(0.34)	$2.78	$1.08
DIVIDENDS PER COMMON SHARE	$0.34	$0.31	$1.02	$0.93
WEIGHTED AVERAGE SHARES OUTSTANDING				
BASIC	41,239	42,049	41,424	42,175
DILUTED	41,239	42,049	41,703	42,547

See Notes to Condensed Unaudited Consolidated Financial Statements

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ITEM 1. FINANCIAL STATEMENTS (Continued)

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Nine Months Ended June 30,	
(Thousands)	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$115,942	$ 46,105
Adjustments to reconcile net income to cash flows from operating activities:		
Unrealized loss on derivative instruments and related transactions	6,186	65,160
Depreciation and amortization	24,628	23,417
Allowance for equity used during construction	(1,474)	(233)
Allowance for bad debt expense	2,277	5,015
Deferred income taxes	69,329	12,732
Manufactured gas plant remediation costs	(2,925)	(12,280)
Equity in earnings of affiliates, net of distributions	(2,261)	3,858
Cost of removal – asset retirement obligations	(676)	(508)
Contributions to postemployment benefit plans	(7,866)	(1,768)
Changes in:		
Components of working capital	(54,205)	243,048
Other noncurrent assets	9,891	(23,611)
Other noncurrent liabilities	(2,902)	(10,251)
Cash flows from operating activities	155,944	350,684
CASH FLOWS USED IN INVESTING ACTIVITIES		
Expenditures for:		
Utility plant	(49,696)	(51,169)
Real estate properties and other	(460)	(356)
Cost of removal	(6,252)	(4,014)
Investments in equity investees	(4,300)	(41,343)
Release from restricted cash construction fund	—	4,200
Cash flows used in investing activities	(60,708)	(92,682)
CASH FLOWS USED IN FINANCING ACTIVITIES		
Proceeds from issuance of common stock	6,414	13,327
Tax benefit from stock options exercised	(96)	993
Proceeds from sale-leaseback transaction	4,925	6,268
Payments of long-term debt	(4,683)	(58,860)
Purchases of treasury stock	(28,069)	(17,757)
Payments of common stock dividends	(39,160)	(37,977)
Net proceeds (payments) of short-term debt	20,900	(129,600)
Cash flows used in financing activities	(39,769)	(223,606)
Change in cash and temporary investments	55,467	34,396
Cash and temporary investments at beginning of period	36,186	42,626
Cash and temporary investments at end of period	$ 91,653	$ 77,022
CHANGES IN COMPONENTS OF WORKING CAPITAL		
Receivables	$(82,253)	$ 97,642

Inventories	18,222	260,883
Recovery of gas costs	(77,529)	58,836
Gas purchases payable	90,976	(144,528)
Prepaid and accrued taxes	(14,093)	37,792
Accounts payable and other	330	2,271
Restricted broker margin accounts	24,172	(27,814)
Customers' credit balances and deposits	(17,137)	(43,162)
Other current assets	3,107	1,128
Total	$(54,205)	$243,048
SUPPLEMENTAL DISCLOSURES OF CASH FLOWS INFORMATION		
Cash paid for:		
Interest (net of amounts capitalized)	$10,426	$13,498
Income taxes	$23,811	$12,685

See Notes to Condensed Unaudited Consolidated Financial Statements

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New Jersey Resources Corporation
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ITEM 1. FINANCIAL STATEMENTS (Continued)

CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

ASSETS

(Thousands)	June 30, 2010	September 30, 2009
PROPERTY, PLANT AND EQUIPMENT		
Utility plant, at cost	$1,488,585	$1,438,945
Real estate properties and other, at cost	30,400	30,195
	1,518,985	1,469,140
Accumulated depreciation and amortization	(417,714)	(404,701)
Property, plant and equipment, net	1,101,271	1,064,439
CURRENT ASSETS		
Cash and temporary investments	91,653	36,186
Customer accounts receivable		
Billed	179,251	101,945
Unbilled revenues	8,333	8,616
Allowance for doubtful accounts	(3,110)	(6,064)
Regulatory assets	49,306	5,878
Gas in storage, at average cost	277,366	297,464
Materials and supplies, at average cost	7,902	6,026
Prepaid state taxes	50,383	37,886
Derivatives, at fair value	86,554	131,070
Restricted broker margin account	5,453	26,250
Deferred taxes	—	20,801
Other	14,992	18,131
Total current assets	768,083	684,189
NONCURRENT ASSETS		
Investments in equity investees	168,682	160,508
Regulatory assets	388,253	391,025
Derivatives, at fair value	8,929	9,536
Other	10,256	11,333
Total noncurrent assets	576,120	572,402
Total assets	$2,445,474	$2,321,030

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New Jersey Resources Corporation
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ITEM 1. FINANCIAL STATEMENTS (Continued)

CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

CAPITALIZATION AND LIABILITIES

(Thousands)	June 30, 2010	September 30, 2009
CAPITALIZATION		
Common stock equity	$ 741,160	$ 689,726
Long-term debt	434,927	455,492
Total capitalization	1,176,087	1,145,218
CURRENT LIABILITIES		
Current maturities of long-term debt	27,320	6,510
Short-term debt	164,300	143,400
Gas purchases payable	221,088	130,112
Accounts payable and other	45,768	44,448
Dividends payable	14,008	13,026
Deferred and accrued taxes	1,879	3,475
Regulatory liabilities	—	36,203
New Jersey clean energy program	12,402	10,920
Derivatives, at fair value	65,244	94,853
Restricted broker margin account	3,375	—
Customers’ credit balances and deposits	56,080	73,218
Total current liabilities	611,464	556,165
NONCURRENT LIABILITIES		
Deferred income taxes	292,121	243,593
Deferred investment tax credits	6,629	6,870
Deferred revenue	7,342	8,203
Derivatives, at fair value	4,177	6,250
Manufactured gas plant remediation	146,700	146,700
Postemployment employee benefit liability	91,141	89,035
Regulatory liabilities	58,726	56,450
New Jersey clean energy program	19,393	28,449
Asset retirement obligation	25,594	25,097
Other	6,100	9,000
Total noncurrent liabilities	657,923	619,647
Commitments and contingent liabilities (Note 13)		
Total capitalization and liabilities	$2,445,474	$2,321,030

See Notes to Unaudited Condensed Consolidated Financial Statements

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ITEM 1. FINANCIAL STATEMENTS (Continued)

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

	Three Months Ended June 30,		Nine Months Ended June 30,	
(Thousands)	2010	2009	2010	2009
Net (loss) income	$(10,177)	$(14,155)	$115,942	$46,105
Unrealized gain (loss) on available for sale securities, net of tax of $(85), $10, $(698) and $74, respectively (1)	131	(14)	1,010	(106)
Net unrealized (loss) on derivatives, net of tax of $76, $16, $119 and $50, respectively	(120)	(23)	(182)	(71)
Other comprehensive income (loss)	11	(37)	828	(177)
Comprehensive (loss) income	$(10,166)	$(14,192)	$116,770	$45,928

(1) Available for sale securities are included in Investments in equity investees in the Unaudited Condensed Consolidated Balance Sheets.

See Notes to Unaudited Condensed Consolidated Financial Statements

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. NATURE OF THE BUSINESS

NJR provides regulated gas distribution services and certain non-regulated businesses primarily through the following subsidiaries:

New Jersey Natural Gas Company (NJNG) provides natural gas utility service in central and northern New Jersey and is subject to rate regulation by the New Jersey Board of Public Utilities (BPU). NJNG comprises the Natural Gas Distribution segment;

NJR Energy Services Company (NJRES) comprises the Energy Services segment and is the Company's principal non-utility subsidiary that maintains and transacts around a portfolio of natural gas storage and transportation positions and provides wholesale energy and energy management services;

NJR Energy Holdings Corporation (NJREH) primarily invests in energy-related ventures through its subsidiaries, NJNR Pipeline Company (Pipeline), which holds the Company's 5.53 percent ownership interest in Iroquois Gas and Transmission System, L.P. (Iroquois) and NJR Steckman Ridge Storage Company, which holds the Company's 50 percent combined interest in Steckman Ridge GP, LLC and Steckman Ridge, LP (collectively, Steckman Ridge), a natural gas storage facility that began commercial operation in April 2009. Effective October 1, 2009, Iroquois and Steckman Ridge comprise the Midstream Assets segment;

NJR Retail Holdings Corporation (Retail Holdings) has two principal subsidiaries, NJR Home Services Company (NJRHS) and Commercial Realty & Resources Corporation (CR&R). Retail Holdings, NJR Energy Corporation (NJR Energy) and NJR Clean Energy Ventures (NJRCEV) are included in Retail and Other operations.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accompanying Unaudited Condensed Consolidated Financial Statements have been prepared by New Jersey Resources Corporation (NJR or the Company) in accordance with the rules and regulations of the Securities and Exchange Commission (SEC). The September 30, 2009 Balance Sheet data is derived from the audited financial statements of the Company. These Unaudited Condensed Consolidated Financial Statements should be read in conjunction with the financial statements and the notes thereto included in NJR's 2009 Annual Report on Form 10-K.

The Unaudited Condensed Consolidated Financial Statements include the accounts of NJR and its subsidiaries. In the opinion of management, the accompanying Unaudited Condensed Consolidated Financial Statements reflect all adjustments necessary, for a fair presentation of the results of the interim periods presented. These adjustments are of a normal and recurring nature. Because of the seasonal nature of NJR's utility and wholesale energy services operations, in addition to other factors, the financial results for the interim periods presented are not indicative of the results that are to be expected for the fiscal year ended September 30, 2010.

Intercompany transactions and accounts have been eliminated.

Change in Reportable Segments

Effective October 1, 2009, NJR established Midstream Assets as a new reportable segment to reflect the way it currently views and manages growth opportunities associated with investments in natural gas transportation and storage facilities. Consequently, the results of operations, assets and other financial information for Iroquois and Steckman Ridge, previously included in Retail and Other operations, are now reported as components of the Midstream Assets segment. As required, prior year information for both Midstream Assets and Retail and Other operations has been restated throughout this report to be consistent with current year presentation (see Note 14. Business Segment and Other Operations Data and Item 2. Management Discussion and Analysis of Financial Condition and Results of Operations).

Gas in Storage

The following table summarizes Gas in storage by company as of:

	June 30, 2010		September 30, 2009	
($ in thousands)	Assets	Bcf	Assets	Bcf
NJNG	$100,947	14.4	$175,201	21.9
NJRES	176,419	40.0	122,263	36.3
Total	$277,366	54.4	$297,464	58.2

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Continued)

Gas in storage decreased during the nine months ended June 30, 2010, due primarily to a 34.2 percent decrease in NJNG's inventory volumes due to timing of summer injections, offset by an increase in the average cost of gas at NJRES.

Customer Accounts Receivable

Customer accounts receivable include outstanding billings from the following subsidiaries as of:

(Thousands)	June 30, 2010		September 30, 2009	
NJNG (1)	$ 11,315	6%	$ 21,239	21%
NJRES	157,578	88	73,451	72
NJRHS and other	10,358	6	7,255	7
Total	$179,251	100%	$101,945	100%

(1) Does not include Unbilled revenues of $8.3 million and $8.6 million as of June 30, 2010 and September 30, 2009, respectively.

Accounts receivable increased during the nine months ended June 30, 2010, due primarily to the impact of higher commodity prices on NJRES' receivables.

Capitalized Financing Costs and Deferred Interest

Included in the Unaudited Condensed Consolidated Balance Sheets are capitalized amounts associated with the debt and equity components of NJNG's Allowance for funds used during construction, (AFUDC), which are recorded in utility plant, as well as capitalized interest recorded in investments in equity investees. Corresponding amounts recognized in interest expense and other income, as appropriate, in the Unaudited Condensed Consolidated Statements of Operations are as follows:

	Three Months Ended June 30,		Nine Months Ended June 30,	
(Thousands)	2010	2009	2010	2009
AFUDC:				
Debt	$262	$169	$ 662	$599
Equity	$557	$233	$1,474	$233
Weighted average rate	7.76%	5.38%	7.34%	3.57%
Investments in equity investees:				
Capitalized interest	$ —	$214	$ —	$1,884
Weighted average interest rates	—%	4.95%	—%	5.15%
Total capitalized costs	$819	$616	$2,136	$2,716
Net weighted average rate	7.76%	5.17%	7.34%	4.36%

NJNG’s base rates include the ability for NJNG to recover the cost of debt and equity associated with AFUDC and construction work in progress (CWIP). Due to a reduction in NJNG's commercial paper borrowings relative to its CWIP, NJNG's capitalized costs included an equity portion associated with its AFUDC as noted above.

During the three and nine months ended June 30, 2009, NJR capitalized interest costs associated with its development and construction of the Steckman Ridge natural gas storage facility. The facility became operational during the third quarter of fiscal 2009, therefore NJR is no longer capitalizing any costs related to Steckman Ridge (see Note 6. Investments in Equity Investees).

Pursuant to a BPU order, NJNG is permitted to recover carrying costs on uncollected balances related to Societal Benefits Clause (SBC) program costs (see Note 3. Regulation). Accordingly, other income includes interest related to these SBC program costs in the amount of $374,000 and $482,000 for the three months ended June 30, 2010 and 2009, respectively and $1.3 million and $1.5 million for the nine months ended June 30, 2010 and 2009, respectively.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Recent Updates to the Accounting Standards Codification (ASC)

Topic 715, Compensation—Retirement Benefits:

On December 30, 2008, the FASB issued guidance that requires additional disclosures surrounding postretirement benefit plans to provide users of financial statements information related to a company's plan assets, investment policies and strategies and significant concentrations of risk. Disclosures will include information related to the fair value of plan assets, including inputs and valuation techniques that are used to measure plan assets and the effect of Level 3 measurements on changes in plan assets. The guidance is effective for fiscal years ending after December 15, 2009. As it is a disclosure only standard, it will have no impact on the Company's statement of financial position, results of operations or cash flows.

Topic 810, Consolidation:

In June 2009, the FASB issued guidance requiring qualitative evaluations including an additional emphasis on identifying the party who effectively controls the entity, which will replace the quantitative assessments currently in practice, when determining whether a company has a controlling financial interest in a variable interest entity (VIE). In addition, the assessments will be required on an ongoing basis, rather than limiting the reassessments to when certain triggering events occur. Additional disclosures will provide information on a company's involvement with VIE's. The guidance is effective at the beginning of a company's annual reporting period that begins after November 15, 2009, including interim reporting periods. The Company will adopt the provisions of the statement prospectively during its first quarter of fiscal 2011 and is evaluating the effect on its financial position, results of operations and cash flows.

Topic 820, Fair Value Measurements and Disclosures:

In August 2009, the FASB issued additional guidance for measuring the fair value of liabilities and clarifies that the quoted price for the identical liability, when traded as an asset in an active market, is a Level 1 measurement, providing there are no adjustments to the quoted price. Alternatively, when no quoted price is available, the guidance affirms the use of other permitted valuation techniques. The guidance became effective for the Company on October 1, 2009. There was no impact to the Company's statement of financial position, results of operations or cash flows upon adoption.

In January 2010, the FASB issued guidance expanding the requirement to disclose information about significant transfers into and out of Level 3 to all three levels of the fair value hierarchy. In addition, it requires a description of the valuation techniques and inputs used to determine Level 2 and Level 3 fair values and provides additional guidance on determining an appropriate level of disaggregation into classes of assets and liabilities in fair value disclosures. The guidance became effective for the first annual or interim period beginning after December 15, 2009. There was no impact to the Company's statement of financial position, results of operations or cash flows upon adoption.

3. REGULATION

Base Rates

In October 2008, the BPU unanimously approved and made effective certain changes in the design of NJNG's base rates. As a result, NJNG received a revenue increase in its base rates of $32.5 million, which is inclusive of an approximate $13 million impact of a change to the Conservation Incentive Program (CIP) baseline usage rate. Other changes included an allowed rate of return of 7.76 percent that incorporates a return on equity component of 10.3 percent and a reduction to NJNG's depreciation expense component.

Conservation Incentive Program (CIP)

The CIP allows NJNG to recover utility gross margin variations related to both weather and customer usage. Recovery of such utility gross margin variations (filed for annually and recovered in the year following the end of the CIP usage year) is subject to additional conditions, including an earnings test and an evaluation of Basic Gas Supply Service (BGSS) related savings.

As of June 30, 2010, under the CIP, NJNG has accrued $13.7 million to be recovered from residential and commercial customers, which includes $9 million related to the weather component of the CIP and $4.7 million related to the usage component of the CIP.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following are NJNG's BPU filings and results during fiscal 2009 and 2010 related to CIP:

- October 2008 – The BPU provisionally approved, effective October 3, 2008, NJNG's CIP petition filed in May 2008 requesting an additional $6.8 million and modification to its CIP recovery rates. The additional amount brought the total recovery requested to $22.4 million and included amounts accrued and estimated through September 30, 2008.

- April 2009 – NJNG submitted a proposal to extend its CIP mechanism, as currently structured, until October 1, 2010. The extension was requested due to the continuing nature of energy efficiency programs at the state and federal levels in concert with the issuance of the economic stimulus programs. As a result of no action being taken by the BPU as of September 30, 2009, the CIP remained in effect for an additional year or until a final order was issued by the BPU.

- June 2009 – The BPU issued their final order approving NJNG's recovery of $6.8 million of CIP rates for fiscal 2008. In addition, NJNG filed its annual BGSS and CIP filing (2010 BGSS/CIP filing) for recoverable CIP amounts for fiscal 2009, requesting approval to modify its CIP recovery rates effective October 1, 2009, resulting in total annual recovery requested for fiscal 2009 of $6.9 million, representing amounts accrued and estimated through September 30, 2009. NJNG also included a request to reduce the WNC rate to facilitate recovery of its remaining balance in fiscal 2010. The rates included in the filing were provisionally approved on September 16, 2009.

- December 2009 – NJNG submitted a petition requesting approval from the BPU for an extension of its CIP mechanism, as currently structured, through September 30, 2013. On January 20, 2010, the BPU approved an extension to NJNG's CIP through September 30, 2013.

  In addition, NJNG and NJRES entered into an asset management agreement that began in January 2010 and ends in March 2013. Under the terms of this agreement, NJNG released certain transportation and storage contracts to NJRES for the entire term of the agreement. NJNG also sold approximately 1 Bcf of natural gas in storage at cost to NJRES. In return, NJNG will have the option to purchase index priced gas from NJRES at NJNG's city gate and other delivery locations to maintain operational reliability. These capacity release payments provide BGSS savings pursuant to the terms of the CIP as approved in the January 20, 2010, BPU Board Order, and reduces costs to NJNG's BGSS customers.

- June 2010 – The BPU issued their final order approving NJNG's recovery of $6.9 million of CIP rates for fiscal year 2009. In addition, NJNG filed its annual BGSS and CIP filing (2011 BGSS/CIP/WNC filing) for recoverable CIP amounts for fiscal 2010, requesting approval to modify its CIP recovery rates effective October 1, 2010, resulting in total annual recovery requested for fiscal 2010 of $12.1 million, an increase of $5.2 million. The request represents recovery of amounts accrued and estimated through September 30, 2010. The request results in an increase of 0.7 percent for the average residential heating customer, which is offset by a BGSS decrease of 3.5 percent as discussed below. NJNG also included a request to reduce the Weather Normalization Clause (WNC) rate to facilitate recovery of its remaining balance in fiscal 2011.

Basic Gas Supply Service (BGSS)

BGSS is a BPU-approved rate mechanism designed to allow for the recovery of natural gas commodity costs. NJNG occasionally adjusts its periodic BGSS rates for its residential and small commercial customers to reflect increases or decreases in the cost of natural gas sold to customers.

The following are NJNG's BGSS filings during fiscal 2009 and 2010 related to its requested rate adjustments and refunds to its residential and small commercial customers:

ŸDecember 2008 – NJNG provided notice that it would implement a $30 million BGSS-related rate credit that would lower residential and small commercial sales customers' bills in January and February 2009. This rate credit was due primarily to a decline in wholesale commodity costs subsequent to the October 2008 BGSS price change. On February 20, 2009, NJNG provided notice to the BPU that its BGSS-related rate credit would be extended through March 31, 2009, to reduce BGSS charges by an additional $15 million.

ŸJune 2009 – NJNG proposed a decrease of 17.6 percent for the average residential heating customer in its 2010 BGSS/CIP filing of which 15.7 percent was due to the reduction in commodity costs based on the continuing decline in the wholesale natural gas market. The balance of the rate change was related to changes to the CIP rate, as discussed above, and a minor reduction to the rate related to collecting the remaining balance under the WNC. In September 2009, the BPU approved on a provisional basis a stipulation in that case which included a decrease of approximately 19 percent to the average residential heating customer of which 17.2 percent was due to the reduction to the BGSS price and the balance of rate change was related to the CIP and WNC rates as discussed above.

ŸOctober 2009 – NJNG provided refunds of approximately $37.4 million to residential and small commercial customers due to the decline in the wholesale price of natural gas.

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- ŸJanuary 2010 – NJNG notified the BPU that bill credits would be provided to residential and small commercial customers, based on individual customer usage, in February 2010 and March 2010. NJNG provided credits of approximately $35.3 million.

- ŸMarch 2010 – NJNG notified the BPU that it would extend the BGSS bill credit for residential and small business customers through April 30, 2010. NJNG provided credits of approximately $15.2 million.

- ŸMay 2010 – NJNG provided refunds of approximately $22.5 million to residential and small commercial customers due to the decline in the wholesale price of natural gas.

- ŸJune 2010 – The BPU approved the June 2009 provisional BGSS rate reduction of 17.2 percent on a final basis. In addition, NJNG filed its annual BGSS and CIP filing (2011 BGSS/CIP/WNC filing) requesting a decrease of 2.8 percent for the average residential heating customer of which 3.5 percent was due to the reduction in commodity costs. The balance of the rate change of 0.7 percent is related to changes to the CIP rate, as previously discussed.

Other Incentive Programs

NJNG is eligible to receive financial incentives for reducing BGSS costs through a series of utility gross margin-sharing programs that include Off-System Sales, Capacity Release, Storage Incentive and Financial Risk Management (FRM) programs. In October 2008, the BPU approved the extension of the incentive programs through October 31, 2011, along with an increase to certain annual cost and volume limitations.

Societal Benefits Clause (SBC)

The SBC is comprised of three primary riders that allow NJNG to recover costs associated with the following programs:

Universal Service Fund (USF), which is a permanent statewide program for all natural gas and electric utilities for the benefit of income-eligible customers, Manufactured Gas Plant (MGP) Remediation, and the New Jersey Clean Energy Program (NJCEP), which is a statewide program designed to promote energy efficiency and renewable energy that all state utilities are required to fund. Recovery of SBC program costs is subject to BPU approval based on annual filings that include an updated report of expenditures incurred each year.

The following is a summary of regulatory actions related to SBC:

- ŸOctober 2008 - The BPU released a final Order in the NJCEP, updating state utilities' funding obligations for the period from January 1, 2009, to December 31, 2012. As a result, NJNG recorded an obligation and a corresponding regulatory asset at a present value of $44.3 million in the Unaudited Condensed Consolidated Balance Sheets. As of June 30, 2010, NJNG had a $31.8 million obligation remaining.

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January 2009 - NJNG filed an application (January 2009 SBC filing) regarding its SBC to increase its MGP factor and its NJCEP factor while maintaining its effective rate on USF. This filing, if approved, will result in an overall increase of approximately 0.48 percent per month for an average residential bill.

ŸJune 2009 – Natural gas utilities in the State of New Jersey collectively filed with the BPU to decrease the statewide USF rate, which was approved by the BPU on a provisional basis, effective October 12, 2009. The USF change decreased the average monthly bill of a residential heating customer by 0.6 percent.

In addition, the BPU approved NJNG's February 2008 SBC filing, which included recovery of MGP remediation expenditures incurred through June 30, 2007, resulting in an expected total annual recovery of $17.7 million.

ŸMarch 2010 - NJNG, BPU Staff and Rate Counsel executed a Settlement for the January 2009 SBC filing to allow for an increase in the MGP and NJCEP factors, while maintaining the current statewide USF factor. The new MGP factor recovers MGP incurred costs through September 30, 2008, resulting in an expected total annual recovery of approximately $20 million. The Stipulation was approved by the BPU in a Final Decision and Order on April 28, 2010.

ŸJune 2010 – NJNG filed an application (June 2010 SBC filing) regarding its SBC to maintain the current MGP factor approved in April 2010 and to maintain the current NJCEP. In addition, natural gas utilities in the State of New Jersey collectively filed with the BPU to increase the statewide USF rate to be effective October 1, 2010. If approved, the USF change would result in an overall increase to the average monthly bill of a residential heating customer by 0.03 percent.

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