

NATIONAL FUEL GAS CO
Form 10-Q
May 04, 2012
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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 March 31, 2012

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 1-3880

NATIONAL FUEL GAS COMPANY

(Exact name of registrant as specified in its charter)

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New Jersey
(State or other jurisdiction of
incorporation or organization)

13-1086010
(I.R.S. Employer
Identification No.)

6363 Main Street
Williamsville, New York
(Address of principal executive offices)

14221
(Zip Code)

(716) 857-7000

(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 and (2) has been subject to such filing requirements for the past 90

days. YES NO

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 NO

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

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer (Do not check if a smaller reporting company)

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 NO

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

Common stock, \$1 par value, outstanding at April 30, 2012: 83,216,016 shares.

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GLOSSARY OF TERMS

Frequently used abbreviations, acronyms, or terms used in this report:

National Fuel Gas Companies

Company	The Registrant, the Registrant and its subsidiaries or the Registrant's subsidiaries as appropriate in the context of the disclosure
Distribution Corporation	National Fuel Gas Distribution Corporation
Empire	Empire Pipeline, Inc.
ESNE	Energy Systems North East, LLC
Horizon	Horizon Energy Development, Inc.
Horizon B.V.	Horizon Energy Development B.V.
Horizon LFG	Horizon LFG, Inc.
Horizon Power	Horizon Power, Inc.
Midstream Corporation	National Fuel Gas Midstream Corporation
Model City	Model City Energy, LLC
National Fuel	National Fuel Gas Company
NFR	National Fuel Resources, Inc.
Registrant	National Fuel Gas Company
Seneca	Seneca Resources Corporation
Seneca Energy	Seneca Energy II, LLC
Supply Corporation	National Fuel Gas Supply Corporation

Regulatory Agencies

EPA	United States Environmental Protection Agency
FASB	Financial Accounting Standards Board
FERC	Federal Energy Regulatory Commission
IASB	International Accounting Standards Board
NYDEC	New York State Department of Environmental Conservation
NYPSC	State of New York Public Service Commission
PaPUC	Pennsylvania Public Utility Commission
PHMSA	Pipeline and Hazardous Materials Safety Administration
SEC	Securities and Exchange Commission

Other

2011 Form 10-K	The Company's Annual Report on Form 10-K for the year ended September 30, 2011
Bbl	Barrel (of oil)
Bcf	Billion cubic feet (of natural gas)
Bcfe (or Mcfe) represents Bcf (or Mcf) Equivalent	The total heat value (Btu) of natural gas and oil expressed as a volume of natural gas. The Company uses a conversion formula of 1 barrel of oil = 6 Mcf of natural gas.
Btu	British thermal unit; the amount of heat needed to raise the temperature of one pound of water one degree Fahrenheit.
Capital expenditure	Represents additions to property, plant, and equipment, or the amount of money a company spends to buy capital assets or upgrade its existing capital assets.
Degree day	A measure of the coldness of the weather experienced, based on the extent to which the daily average temperature falls below a reference temperature, usually 65 degrees Fahrenheit.
Derivative	A financial instrument or other contract, the terms of which include an underlying variable (a price, interest rate, index rate, exchange rate, or other variable) and a notional amount (number of units, barrels, cubic feet, etc.). The terms also permit for the instrument or contract to be settled net and no initial net investment is required to enter into the financial instrument or contract. Examples include futures contracts, options, no cost collars and swaps.

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Development costs	Costs incurred to obtain access to proved oil and gas reserves and to provide facilities for extracting, treating, gathering and storing the oil and gas.
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act.
Dth	Decatherm; one Dth of natural gas has a heating value of 1,000,000 British thermal units, approximately equal to the heating value of 1 Mcf of natural gas.
Exchange Act	Securities Exchange Act of 1934, as amended
Expenditures for long-lived assets	Includes capital expenditures, stock acquisitions and/or investments in partnerships.
Exploration costs	Costs incurred in identifying areas that may warrant examination, as well as costs incurred in examining specific areas, including drilling exploratory wells.
Firm transportation and/or storage	The transportation and/or storage service that a supplier of such service is obligated by contract to provide and for which the customer is obligated to pay whether or not the service is utilized.
GAAP	Accounting principles generally accepted in the United States of America
Goodwill	An intangible asset representing the difference between the fair value of a company and the price at which a company is purchased.
Hedging	A method of minimizing the impact of price, interest rate, and/or foreign currency exchange rate changes, often times through the use of derivative financial instruments.
Hub	Location where pipelines intersect enabling the trading, transportation, storage, exchange, lending and borrowing of natural gas.
Interruptible transportation and/or storage	The transportation and/or storage service that, in accordance with contractual arrangements, can be interrupted by the supplier of such service, and for which the customer does not pay unless utilized.
LIBOR	London Interbank Offered Rate
LIFO	Last-in, first-out
Marcellus Shale	A Middle Devonian-age geological shale formation that is present nearly a mile or more below the surface in the Appalachian region of the United States, including much of Pennsylvania and southern New York.
Mbbl	Thousand barrels (of oil)
Mcf	Thousand cubic feet (of natural gas)
MD&A	Management's Discussion and Analysis of Financial Condition and Results of Operations
MDth	Thousand decatherms (of natural gas)
MMBtu	Million British thermal units
MMcf	Million cubic feet (of natural gas)
NGA	The Natural Gas Act of 1938, as amended; the federal law regulating interstate natural gas pipeline and storage companies, among other things, codified beginning at 15 U.S.C. Section 717.
NYMEX	New York Mercantile Exchange. An exchange which maintains a futures market for crude oil and natural gas.
Open Season	A bidding procedure used by pipelines to allocate firm transportation or storage capacity among prospective shippers, in which all bids submitted during a defined time period are evaluated as if they had been submitted simultaneously.
PCB	Polychlorinated Biphenyl
Precedent Agreement	An agreement between a pipeline company and a potential customer to sign a service agreement after specified events (called "conditions precedent") happen, usually within a specified time.
Proved developed reserves	Reserves that can be expected to be recovered through existing wells with existing equipment and operating methods.

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Proved undeveloped (PUD) reserves	Reserves that are expected to be recovered from new wells on undrilled acreage, or from existing wells where a relatively major expenditure is required to make these reserves productive.
Reserves	The unproduced but recoverable oil and/or gas in place in a formation which has been proven by production.
Restructuring	Generally referring to partial deregulation of the pipeline and/or utility industry by statutory or regulatory process. Restructuring of federally regulated natural gas pipelines resulted in the separation (or unbundling) of gas commodity service from transportation service for wholesale and large-volume retail markets. State restructuring programs attempt to extend the same process to retail mass markets.
Revenue decoupling mechanism	A rate mechanism which adjusts customer rates to render a utility financially indifferent to throughput decreases resulting from conservation.
S&P	Standard & Poor's Rating Service
SAR	Stock appreciation right
Service agreement	The binding agreement by which the pipeline company agrees to provide service and the shipper agrees to pay for the service.
Stock acquisitions	Investments in corporations.
Unbundled service	A service that has been separated from other services, with rates charged that reflect only the cost of the separated service.
VEBA	Voluntary Employees' Beneficiary Association
WNC	Weather normalization clause; a clause in utility rates which adjusts customer rates to allow a utility to recover its normal operating costs calculated at normal temperatures. If temperatures during the measured period are warmer than normal, customer rates are adjusted upward in order to recover projected operating costs. If temperatures during the measured period are colder than normal, customer rates are adjusted downward so that only the projected operating costs will be recovered.

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The Company has nothing to report under this item.

Reference to "the Company" in this report means the Registrant or the Registrant and its subsidiaries collectively, as appropriate in the context of the disclosure. All references to a certain year in this report are to the Company's fiscal year ended September 30 of that year, unless otherwise noted.

This Form 10-Q contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934. Forward-looking statements should be read with the cautionary statements and important factors included in this Form 10-Q at Item 2 - MD&A, under the heading "Safe Harbor for Forward-Looking Statements." Forward-looking statements are all statements other than statements of historical fact, including, without limitation, statements regarding future prospects, plans, objectives, goals, projections, estimates of oil and gas quantities, strategies, future events or performance and underlying assumptions, capital structure, anticipated capital expenditures, completion of construction and other projects, projections for pension and other post-retirement benefit obligations, impacts of the adoption of new accounting rules, and possible outcomes of litigation or regulatory proceedings, as well as statements that are identified by the use of the words "anticipates," "estimates," "expects," "forecasts," "intends," "plans," "predicts," "projects," "believes," "seeks," "will," "may," and similar expressions.

Table of Contents**Part I. Financial Information****Item 1. Financial Statements****National Fuel Gas Company****Consolidated Statements of Income and Earnings****Reinvested in the Business****(Unaudited)**

(Thousands of Dollars, Except Per Common Share Amounts)	Three Months Ended March 31,	
	2012	2011
INCOME		
Operating Revenues	\$ 552,309	\$ 660,881
Operating Expenses		
Purchased Gas	208,537	306,595
Operation and Maintenance	118,047	116,721
Property, Franchise and Other Taxes	30,477	23,798
Depreciation, Depletion and Amortization	63,151	60,011
	420,212	507,125
Operating Income	132,097	153,756
Other Income (Expense):		
Gain on Sale of Unconsolidated Subsidiaries		50,879
Interest Income	192	68
Other Income	1,654	2,424
Interest Expense on Long-Term Debt	(20,425)	(17,926)
Other Interest Expense	(1,253)	(1,454)
Income Before Income Taxes	112,265	187,747
Income Tax Expense	44,873	72,136
Net Income Available for Common Stock	67,392	115,611
EARNINGS REINVESTED IN THE BUSINESS		
Balance at January 1	1,237,242	1,093,398
	1,304,634	1,209,009
Dividends on Common Stock (2012 - \$0.355 per share; 2011 - \$0.345 per share)	(29,527)	(28,478)
Balance at March 31	\$ 1,275,107	\$ 1,180,531
Earnings Per Common Share:		
Basic:		
Net Income Available for Common Stock	\$ 0.81	\$ 1.40

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Diluted:			
Net Income Available for Common Stock		\$ 0.81	\$ 1.38
Weighted Average Common Shares Outstanding:			
Used in Basic Calculation		83,107,884	82,400,851
Used in Diluted Calculation		83,678,261	83,673,977

See Notes to Condensed Consolidated Financial Statements

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Table of ContentsNational Fuel Gas CompanyConsolidated Statements of Income and EarningsReinvested in the Business(Unaudited)

(Thousands of Dollars, Except Per Common Share Amounts)	Six Months Ended March 31,	
	2012	2011
INCOME		
Operating Revenues	\$ 984,732	\$ 1,111,829
Operating Expenses		
Purchased Gas	340,730	469,633
Operation and Maintenance	218,106	214,171
Property, Franchise and Other Taxes	49,707	43,534
Depreciation, Depletion and Amortization	125,698	113,324
	734,241	840,662
Operating Income	250,491	271,167
Other Income (Expense):		
Gain on Sale of Unconsolidated Subsidiaries		50,879
Interest Income	1,297	951
Other Income	2,990	2,317
Interest Expense on Long-Term Debt	(39,066)	(38,118)
Other Interest Expense	(2,023)	(2,855)
Income Before Income Taxes	213,689	284,341
Income Tax Expense	85,598	110,187
Net Income Available for Common Stock	128,091	174,154
EARNINGS REINVESTED IN THE BUSINESS		
Balance at October 1	1,206,022	1,063,262
	1,334,113	1,237,416
Dividends on Common Stock (2012 - \$0.71 per share; 2011 - \$0.69 per share)	(59,006)	(56,885)
Balance at March 31	\$ 1,275,107	\$ 1,180,531
Earnings Per Common Share:		
Basic:		
Net Income Available for Common Stock	\$ 1.54	\$ 2.12
Diluted:		
Net Income Available for Common Stock	\$ 1.53	\$ 2.08
Weighted Average Common Shares Outstanding:		

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Used in Basic Calculation	82,988,750	82,311,162
Used in Diluted Calculation	83,712,681	83,561,775

See Notes to Condensed Consolidated Financial Statements

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Table of ContentsNational Fuel Gas CompanyConsolidated Balance Sheets(Unaudited)

(Thousands of Dollars)	March 31, 2012	September 30, 2011
ASSETS		
Property, Plant and Equipment	\$ 6,180,827	\$ 5,646,918
Less - Accumulated Depreciation, Depletion and Amortization	1,750,636	1,646,394
	4,430,191	4,000,524
Current Assets		
Cash and Temporary Cash Investments	192,243	80,428
Hedging Collateral Deposits	18,872	19,701
Receivables Net of Allowance for Uncollectible Accounts of \$43,124 and \$31,039, Respectively	168,757	131,885
Unbilled Utility Revenue	31,318	17,284
Gas Stored Underground	16,195	54,325
Materials and Supplies - at average cost	28,395	27,932
Other Current Assets	40,354	38,334
Deferred Income Taxes	20,281	15,423
	516,415	385,312
Other Assets		
Recoverable Future Taxes	146,561	144,377
Unamortized Debt Expense	14,552	10,571
Other Regulatory Assets	504,399	510,986
Deferred Charges	7,993	5,552
Other Investments	85,555	79,365
Goodwill	5,476	5,476
Fair Value of Derivative Financial Instruments	121,760	76,085
Other	2,594	2,836
	888,890	835,248
Total Assets	\$ 5,835,496	\$ 5,221,084

See Notes to Condensed Consolidated Financial Statements

Table of ContentsNational Fuel Gas CompanyConsolidated Balance Sheets(Unaudited)

(Thousands of Dollars)	March 31, 2012	September 30, 2011
CAPITALIZATION AND LIABILITIES		
Capitalization:		
Comprehensive Shareholders Equity		
Common Stock, \$1 Par Value		
Authorized - 200,000,000 Shares; Issued And Outstanding 83,173,850 Shares and 82,812,677 Shares, Respectively	\$ 83,174	\$ 82,813
Paid in Capital	660,495	650,749
Earnings Reinvested in the Business	1,275,107	1,206,022
Total Common Shareholders Equity Before Items of Other Comprehensive Loss	2,018,776	1,939,584
Accumulated Other Comprehensive Loss	(51,889)	(47,699)
Total Comprehensive Shareholders Equity	1,966,887	1,891,885
Long-Term Debt, Net of Current Portion	1,149,000	899,000
Total Capitalization	3,115,887	2,790,885
Current and Accrued Liabilities		
Notes Payable to Banks and Commercial Paper	20,000	40,000
Current Portion of Long-Term Debt	250,000	150,000
Accounts Payable	98,053	126,709
Amounts Payable to Customers	17,327	15,519
Dividends Payable	29,527	29,399
Interest Payable on Long-Term Debt	29,491	25,512
Customer Advances	204	19,643
Customer Security Deposits	17,021	17,321
Other Accruals and Current Liabilities	197,952	94,787
Fair Value of Derivative Financial Instruments	66,887	9,728
	726,462	528,618
Deferred Credits		
Deferred Income Taxes	1,040,789	955,384
Taxes Refundable to Customers	65,550	65,543
Unamortized Investment Tax Credit	2,296	2,586
Cost of Removal Regulatory Liability	146,771	135,940
Other Regulatory Liabilities	37,327	31,026
Pension and Other Post-Retirement Liabilities	472,717	481,520
Asset Retirement Obligations	77,230	75,731
Other Deferred Credits	150,467	153,851
	1,993,147	1,901,581
Commitments and Contingencies		

Total Capitalization and Liabilities

\$ 5,835,496 \$ 5,221,084

See Notes to Condensed Consolidated Financial Statements

Table of ContentsNational Fuel Gas CompanyConsolidated Statements of Cash Flows(Unaudited)

(Thousands of Dollars)	Six Months Ended March 31,	
	2012	2011
OPERATING ACTIVITIES		
Net Income Available for Common Stock	\$ 128,091	\$ 174,154
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Gain on Sale of Unconsolidated Subsidiaries		(50,879)
Depreciation, Depletion and Amortization	125,698	113,324
Deferred Income Taxes	81,696	106,510
Excess Tax Benefits Associated with Stock-Based Compensation Awards	(1,076)	
Other	4,269	5,703
Change in:		
Hedging Collateral Deposits	829	(50,692)
Receivables and Unbilled Utility Revenue	(50,906)	(123,393)
Gas Stored Underground and Materials and Supplies	37,156	30,144
Prepayments and Other Current Assets	(943)	57,447
Accounts Payable	(28,656)	33,234
Amounts Payable to Customers	1,808	(12,634)
Customer Advances	(19,439)	(24,938)
Customer Security Deposits	(300)	(256)
Other Accruals and Current Liabilities	65,039	93,473
Other Assets	(48,692)	15,239
Other Liabilities	44,323	(23,214)
Net Cash Provided by Operating Activities	338,897	343,222
INVESTING ACTIVITIES		
Capital Expenditures	(499,607)	(392,338)
Net Proceeds from Sale of Unconsolidated Subsidiaries		59,365
Other	(789)	(3,097)
Net Cash Used in Investing Activities	(500,396)	(336,070)
FINANCING ACTIVITIES		
Changes in Notes Payable to Banks and Commercial Paper	(20,000)	
Excess Tax Benefits Associated with Stock-Based Compensation Awards	1,076	
Net Proceeds from Issuance of Long-Term Debt	496,085	
Reduction of Long-Term Debt	(150,000)	(200,000)
Dividends Paid on Common Stock	(58,877)	(56,723)
Net Proceeds from Issuance (Repurchase) of Common Stock	5,030	(2,833)
Net Cash Provided by (Used in) Financing Activities	273,314	(259,556)
Net Increase (Decrease) in Cash and Temporary Cash Investments	111,815	(252,404)
Cash and Temporary Cash Investments at October 1	80,428	397,171
Cash and Temporary Cash Investments at March 31	\$ 192,243	\$ 144,767

See Notes to Condensed Consolidated Financial Statements

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Table of ContentsNational Fuel Gas CompanyConsolidated Statements of Comprehensive Income(Unaudited)

(Thousands of Dollars)	Three Months Ended March 31,	
	2012	2011
Net Income Available for Common Stock	\$ 67,392	\$ 115,611
Other Comprehensive Income (Loss), Before Tax:		
Unrealized Gain on Securities Available for Sale Arising During the Period	3,116	897
Unrealized Gain (Loss) on Derivative Financial Instruments Arising During the Period	14,498	(40,844)
Reclassification Adjustment for Realized Gains on Derivative Financial Instruments in Net Income	(16,185)	(7,212)
Other Comprehensive Income (Loss), Before Tax	1,429	(47,159)
Income Tax Expense Related to Unrealized Gain on Securities Available for Sale Arising During the Period	1,161	337
Income Tax Expense (Benefit) Related to Unrealized Gain (Loss) on Derivative Financial Instruments Arising During the Period	840	(16,778)
Reclassification Adjustment for Income Tax Expense on Realized Gains from Derivative Financial Instruments in Net Income	(1,816)	(2,847)
Income Taxes - Net	185	(19,288)
Other Comprehensive Income (Loss)	1,244	(27,871)
Comprehensive Income	\$ 68,636	\$ 87,740

(Thousands of Dollars)	Six Months Ended March 31,	
	2012	2011
Net Income Available for Common Stock	\$ 128,091	\$ 174,154
Other Comprehensive Income (Loss), Before Tax:		
Foreign Currency Translation Adjustment		17
Reclassification Adjustment for Realized Foreign Currency Translation Loss in Net Income		34
Unrealized Gain on Securities Available for Sale Arising During the Period	3,828	3,438
Unrealized Gain (Loss) on Derivative Financial Instruments Arising During the Period	16,653	(67,980)
Reclassification Adjustment for Realized Gains on Derivative Financial Instruments in Net Income	(28,050)	(16,265)
Other Comprehensive Loss, Before Tax	(7,569)	(80,756)
Income Tax Expense Related to Unrealized Gain on Securities Available for Sale Arising During the Period	1,424	1,298
Income Tax Expense (Benefit) Related to Unrealized Gain (Loss) on Derivative Financial Instruments Arising During the Period	1,657	(27,946)
Reclassification Adjustment for Income Tax Expense on Realized Gains from Derivative Financial Instruments in Net Income	(6,460)	(6,572)

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Income Taxes - Net	(3,379)	(33,220)
Other Comprehensive Loss	(4,190)	(47,536)
Comprehensive Income	\$ 123,901	\$ 126,618

See Notes to Condensed Consolidated Financial Statements

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National Fuel Gas Company

Notes to Condensed Consolidated Financial Statements

(Unaudited)

Note 1 - Summary of Significant Accounting Policies

Principles of Consolidation. The Company consolidates all entities in which it has a controlling financial interest. The equity method is used to account for entities in which the Company has a non-controlling financial interest. All significant intercompany balances and transactions are eliminated.

During the quarter ended March 31, 2011, the Company sold its 50% equity method investments in Seneca Energy and Model City for \$59.4 million, resulting in a gain of \$50.9 million. Seneca Energy and Model City generate and sell electricity using methane gas obtained from landfills owned by outside parties.

The preparation of the consolidated financial statements in conformity with GAAP 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 amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.