

NEW JERSEY RESOURCES CORP  
Form 10-Q  
May 08, 2009

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

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2009

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 1-8359

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:  No:

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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, 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:  Accelerated filer:  Non-accelerated filer:  Smaller reporting company:   
(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:  No:

The number of shares outstanding of \$2.50 par value Common Stock as of May 06, 2009 was 42,139,988.

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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 made based upon management's expectations and beliefs 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 2009 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, as well as the following:

- weather and economic conditions;
- demographic changes in the New Jersey Natural Gas (NJNG) service territory;
- the rate of NJNG customer growth;
- volatility of natural gas commodity prices and its impact on customer usage, cash flow, 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;
- continued volatility or seizure of the credit markets that would result in the decreased availability and access to 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 access to the commercial paper market and other short-term financing markets at NJNG to allow it to fund its commodity purchases and meet its short-term obligations as they come due;
- the impact to the asset values and funding obligations of NJR's pension and postemployment benefit plans as a result of declines in the financial markets;
- increases in borrowing costs associated with variable-rate debt;
- commercial and wholesale credit risks, including creditworthiness of customers and counterparties;
- the ability to obtain governmental approvals and/or financing for the construction, development and operation of certain non-regulated energy investments;
- risks associated with the management of the Company's joint ventures and partnerships;
- the impact of governmental regulation (including the regulation of rates);

- conversion activity and other marketing efforts;
- actual energy usage of NJNG's customers;
- the pace of deregulation of retail gas markets;
- access to adequate supplies of natural gas;
- the regulatory and pricing policies of federal and state regulatory agencies;
- the ultimate outcome of pending regulatory proceedings, including the possible expiration of the Conservation Incentive Program (CIP);
- changes due to legislation at the federal and state level;
- the availability of an adequate number of appropriate counterparties in the wholesale energy trading market;
- sufficient liquidity in the wholesale energy trading market and continued access to the capital markets;
- the disallowance of recovery of environmental-related expenditures and other regulatory changes;
- environmental-related and other litigation and other uncertainties;
- the effects and impacts of inflation on NJR and its subsidiaries operations;
- change in accounting pronouncements issued by the appropriate standard setting bodies; and
- terrorist attacks or threatened attacks on energy facilities or unrelated energy companies.

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 INCOME (Unaudited)

(Thousands, except per share data)	Three Months Ended March 31,		Six Months Ended March 31,	
	2009	2008	2009	2008
<b>OPERATING REVENUES</b>	\$937,516	\$1,177,545	\$1,738,820	\$1,988,683
<b>OPERATING EXPENSES</b>				
Gas purchases	782,130	1,065,925	1,480,275	1,750,619
Operation and maintenance	37,365	34,605	73,773	66,784
Regulatory rider expenses	20,744	17,789	34,305	29,954
Depreciation and amortization	7,508	9,517	14,869	18,920
Energy and other taxes	31,981	29,374	55,614	47,534
Total operating expenses	879,728	1,157,210	1,658,836	1,913,811
<b>OPERATING INCOME</b>	57,788	20,335	79,984	74,872
Other income	1,058	1,540	1,916	3,068
Interest expense, net	4,219	6,692	10,766	14,502
<b>INCOME BEFORE INCOME TAXES AND EQUITY IN EARNINGS OF AFFILIATES</b>	54,627	15,183	71,134	63,438
Income tax provision	19,897	3,394	25,142	21,888
Equity in earnings of affiliates, net of tax	787	746	1,301	1,170
<b>NET INCOME</b>	\$ 35,517	\$ 12,535	\$ 47,293	\$ 42,720
<b>EARNINGS PER COMMON SHARE</b>				
<b>BASIC</b>	\$0.84	\$0.30	\$1.12	\$1.02
<b>DILUTED</b>	\$0.83	\$0.30	\$1.11	\$1.02
<b>DIVIDENDS PER COMMON SHARE</b>	\$0.31	\$0.28	\$0.62	\$0.55
<b>WEIGHTED AVERAGE SHARES OUTSTANDING</b>				
<b>BASIC</b>	42,305	41,840	42,238	41,758
<b>DILUTED</b>	42,693	42,099	42,598	42,018

See Notes to Condensed Unaudited Consolidated Financial Statements





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Part I

## ITEM 1. FINANCIAL STATEMENTS (Continued)

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Six Months Ended March 31,	
(Thousands)	2009	2008
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 47,293	\$ 42,720
Adjustments to reconcile net income to cash flows from operating activities:		
Unrealized loss on derivative instruments	45,008	72,051
Depreciation and amortization	15,303	19,070
Allowance for funds (equity) used during construction	—	(755)
Allowance for bad debt expense	3,801	2,544
Deferred income taxes	(22,428)	(2,942)
Manufactured gas plant remediation costs	(9,851)	(7,958)
Equity in earnings from investments, net of distributions	(1,301)	766
Cost of removal – asset retirement obligations	(463)	(355)
Contributions to employee benefit plans	(563)	(381)
Changes in:		
Components of working capital	284,371	27,852
Other noncurrent assets	(17,426)	14,543
Other noncurrent liabilities	2,126	565
Cash flows from operating activities	345,870	167,720
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Expenditures for:		
Utility plant	(37,802)	(29,385)
Real estate properties and other	(240)	(588)
Cost of removal	(3,583)	(3,641)
Investments in equity investees	(28,525)	(5,259)
Withdrawal from restricted cash construction fund	4,200	—
Cash flows used in investing activities	(65,950)	(38,873)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from issuance of common stock	6,959	9,915
Tax benefit from stock options exercised	993	568
Proceeds from sale-leaseback transaction	6,268	7,485
Payments of long-term debt	(57,594)	(2,310)
Purchases of treasury stock	(3,291)	(11,040)
Payments of common stock dividends	(24,384)	(21,734)
Net (payments) proceeds from short-term debt	(168,200)	(107,579)
Cash flows used in financing activities	(239,249)	(124,695)
Change in cash and temporary investments	40,671	4,152

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Cash and temporary investments at beginning of period	42,626	5,140
Cash and temporary investments at end of period	\$ 83,297	\$ 9,292
<b>CHANGES IN COMPONENTS OF WORKING CAPITAL</b>		
Receivables	\$ (25,651)	\$(264,803)
Inventories	415,082	193,659
Recovery of gas costs	41,865	1,352
Gas purchases payable	(150,386)	116,692
Prepaid and accrued taxes, net	115,528	83,474
Accounts payable and other	(3,140)	(24,322)
Restricted broker margin accounts	(65,546)	(72,426)
Customers' credit balances and deposits	(49,203)	(7,062)
Other current assets	5,822	1,288
Total	\$284,371	\$ 27,852
<b>SUPPLEMENTAL DISCLOSURES OF CASH FLOWS INFORMATION</b>		
Cash paid for:		
Interest (net of amounts capitalized)	\$12,277	\$14,302
Income taxes	\$ 9,227	\$21,977

See Notes to Condensed Unaudited Consolidated Financial Statements

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## ITEM 1. FINANCIAL STATEMENTS (Continued)

## CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

## ASSETS

(Thousands)	March 31, 2009	September 30, 2008
<b>PROPERTY, PLANT AND EQUIPMENT</b>		
Utility plant, at cost	\$1,402,392	\$1,366,237
Real estate properties and other, at cost	30,047	29,808
	1,432,439	1,396,045
Accumulated depreciation and amortization	(393,912)	(378,759)
Property, plant and equipment, net	1,038,527	1,017,286
<b>CURRENT ASSETS</b>		
Cash and temporary investments	83,297	42,626
Customer accounts receivable		
Billed	208,827	227,132
Unbilled revenues	50,492	9,417
Allowance for doubtful accounts	(5,501)	(4,580)
Regulatory assets	7,795	51,376
Gas in storage, at average cost	63,523	478,549
Materials and supplies, at average cost	5,054	5,110
Prepaid state taxes	—	37,271
Derivatives, at fair value	242,814	208,703
Restricted broker margin accounts	104,497	41,277
Other	22,424	12,785
Total current assets	783,222	1,109,666
<b>NONCURRENT ASSETS</b>		
Investments in equity investees and other	148,739	115,981
Regulatory assets	411,211	340,670
Derivatives, at fair value	22,891	24,497
Restricted cash construction fund	—	4,200
Other	12,001	13,092
Total noncurrent assets	594,842	498,440
Total assets	\$2,416,591	\$2,625,392

See Notes to Unaudited Condensed Consolidated Financial Statements



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## ITEM 1. FINANCIAL STATEMENTS (Continued)

## CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

## CAPITALIZATION AND LIABILITIES

(Thousands)	March 31, 2009	September 30, 2008
<b>CAPITALIZATION</b>		
Common stock equity	\$ 757,291	\$ 726,958
Long-term debt	458,998	455,117
Total capitalization	1,216,289	1,182,075
<b>CURRENT LIABILITIES</b>		
Current maturities of long-term debt	5,934	60,119
Short-term debt	10,000	178,200
Gas purchases payable	165,130	315,516
Accounts payable and other	48,009	61,735
Dividends payable	13,101	11,776
Deferred and accrued taxes	77,616	24,720
Regulatory liabilities	13,871	—
New Jersey clean energy program	9,777	3,056
Derivatives, at fair value	285,255	146,320
Restricted broker margin accounts	26,746	29,072
Customers' credit balances and deposits	14,254	63,455
Total current liabilities	669,693	893,969
<b>NONCURRENT LIABILITIES</b>		
Deferred income taxes	202,860	239,703
Deferred investment tax credits	7,031	7,192
Deferred revenue	8,729	9,090
Derivatives, at fair value	13,038	25,016
Manufactured gas plant remediation	120,230	120,730
Postemployment employee benefit liability	55,096	52,272
Regulatory liabilities	58,587	63,419
New Jersey clean energy program	31,062	—
Asset retirement obligation	24,695	24,416
Other	9,281	7,510
Total noncurrent liabilities	530,609	549,348
Commitments and contingent liabilities (Note 13)		
Total capitalization and liabilities	\$2,416,591	\$2,625,392

See Notes to Unaudited Condensed Consolidated Financial Statements

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## ITEM 1. FINANCIAL STATEMENTS (Continued)

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

(Thousands)	Three Months Ended		Six Months Ended	
	March 31,		March 31,	
	2009	2008	2009	2008
Net income	\$35,517	\$12,535	\$47,293	\$42,720
Other comprehensive income				
Unrealized (loss) gain on investments in equity investees, net of tax of \$444, \$90, \$64 and \$(28), respectively	(637)	(129)	(92)	41
Net unrealized (loss) on derivatives, net of tax of \$15, \$34, \$34 and \$59, respectively	(22)	(10)	(48)	(52)
Other comprehensive income	(659)	(139)	(140)	(11)
Comprehensive income	\$34,858	\$12,396	\$47,153	\$42,709

See Notes to Unaudited Condensed Consolidated Financial Statements





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## NOTES TO CONDENSED UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

## 1. GENERAL

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, 2008 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 2008 Annual Report on Form 10-K.

The unaudited condensed consolidated financial statements include the accounts of NJR and its subsidiaries, New Jersey Natural Gas Company (NJNG), NJR Energy Services Company (NJRES), NJR Retail Holdings Corporation (Retail Holdings), NJR Energy Investment Corporation (NJREI) and NJR Service Company (NJR Service). Intercompany transactions and accounts have been eliminated. NJREI's primary subsidiaries are NJR Energy Corporation (NJR Energy) and NJR Steckman Ridge Storage Company. NJR Energy invests primarily in energy-related ventures through its subsidiary, NJNR Pipeline Company (Pipeline), which holds the Company's 5.53 percent ownership interest in Iroquois Gas and Transmission System, L.P. (Iroquois). NJR Steckman Ridge Storage Company 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 was acquired and is being developed with a partner in Pennsylvania. Retail Holdings' two principal subsidiaries are NJR Home Services Company (NJRHS) and Commercial Realty & Resources Corporation (CR&R).

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, 2009.

## Customer Accounts Receivable

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

(Thousands)	March 31, 2009		September 30, 2008	
NJNG	\$ 94,007	45%	\$ 21,398	9%
NJRES	107,155	51	198,902	88
NJRHS and other	7,665	4	6,832	3
Total	\$208,827	100%	\$227,132	100%

Accounts receivable related to estimated unbilled revenues and allowance for doubtful accounts are associated with NJNG only.

## Gas in Storage

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

(\$ in thousands)	March 31, 2009		September 30, 2008	
	Assets	Bcf	Assets	Bcf

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NJNG	\$19,391	1.9	\$189,828	22.1
NJRES	44,132	13.1	288,721	27.6
Total	\$63,523	15.0	\$478,549	49.7

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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New Accounting Standards

Recently Adopted

Effective October 1, 2008 NJR adopted Statement of Financial Accounting Standards (SFAS) No. 157, Fair Value Measurements (SFAS 157) for its financial assets and liabilities, with the exception of its pension assets. On October, 1, 2009, in accordance with SFAS 157-2, NJR will prospectively apply the provisions of SFAS 157 to its non-financial assets and liabilities that are not measured at least annually. In addition, the provisions of SFAS 157 will be applied to NJR's annual pension disclosures in accordance with FASB Staff Position (FSP) No. FAS 132(R)-1 (FSP 132(R)-1), Employers' disclosures about Pensions and Other Postretirement Benefits, beginning in fiscal 2010.

SFAS 157 defines fair value as the amount that would be exchanged to sell an asset or transfer a liability in an orderly transaction between market participants, and establishes a fair value hierarchy of market and unobservable data that is used to develop pricing assumptions. The adoption of SFAS 157 did not have a material impact on NJR's financial position or results of operations. See Note 4, Fair Value Measurements, for more information on the adoption of SFAS 157, as well as the required disclosures.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities, (SFAS 161). SFAS 161 requires enhanced qualitative and quantitative disclosures on the objectives and accounting for derivatives and related hedging activities, as well as their impacts on the financial statements. NJR adopted SFAS 161 effective January 1, 2009. As SFAS 161 provisions only require additional disclosures, there was no impact to NJR's statement of financial position and results of operations upon adoption. See Note 3 Derivative Instruments for a description of NJR's derivative activities, including the additional disclosures required by SFAS 161.

On April 10, 2007, the FASB issued FASB Staff Position No. FIN 39-1 (FSP FIN 39-1), Amendment of FASB Interpretation No. 39. FSP FIN 39-1 provides additional guidance for parties that are subject to master netting arrangements. Specifically, for transactions that are executed with the same counterparty, it permits companies to offset the fair values of amounts recognized for derivatives as well as the related fair value amounts of cash collateral receivables or payables, when certain conditions apply. FSP FIN 39-1 became effective for fiscal years beginning after November 15, 2007. As NJR's policy has been to present its derivative positions and any receivables or payables with the same counterparty on a gross basis, FSP FIN 39-1 had no impact on its statement of financial position and results of operations.

Other Recently Issued Standards

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS 159). SFAS 159 permits entities to elect to measure eligible items at fair value as an alternative to hedge accounting and to mitigate volatility in earnings. A company can either elect the fair value option according to a pre-existing policy, when the asset or liability is first recognized or when it enters into an eligible firm commitment. Changes in the fair value of assets and liabilities that the company chooses to apply the fair value option to, are reported in earnings at each reporting date. SFAS 159 also provides guidance on disclosures that are intended to provide comparability to other companies' assets and liabilities that have different measurement attributes and to other companies with similar financial assets and liabilities. SFAS 159 became effective for NJR as of October 1, 2008; however, since the Company did not elect the fair value option for any items, the provisions of SFAS 159 do not impact our results of operations or financial condition.

On December 4, 2007, the FASB issued SFAS No. 160, Non-controlling Interests in Consolidated Financial Statements (SFAS 160). SFAS 160 is an amendment of Accounting Research Bulletin (ARB) No. 51 and was issued to improve the relevance, comparability and transparency of the financial information that a reporting entity provides in its consolidated financial statements. This Statement applies to all entities that prepare consolidated financial statements, except not-for-profit organizations, but will affect only those entities that have an outstanding non-controlling interest in one or more subsidiaries. SFAS 160 clarifies that a non-controlling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements and that a parent company must recognize a gain or loss in net income when a subsidiary is deconsolidated. SFAS 160 is effective for fiscal years beginning after December 15, 2008, and early adoption is prohibited. The Company has concluded that this statement will have no impact on its statement of financial position or results of operations.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Continued)

On December 30, 2008, the FASB issued FSP 132(R)-1, which requires additional disclosures surrounding postretirement benefit plan assets. Specifically, the objective of FSP 132(R)-1 is to provide users of financial statements information related to a company's plan assets, investment policies and strategies and significant concentrations of risk. In addition, certain disclosure provisions from FAS 157 will be applied, including those related to inputs and valuation techniques that are used to measure plan assets and the effect of level three measurements on changes in plan assets. FSP 132(R)-1 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 or results of operations.

On April 9, 2009 the FASB issued FSP No. FAS 107-1 and APB 28-1, Interim Disclosures about Fair Values of Financial Instruments, which amends SFAS 107, Disclosures about Fair Values of Financial Instruments, and requires that companies also disclose the fair value of financial instruments during interim reporting similar to those that are currently provided annually. FSP No. FAS 107-1 and APB 28-1 is effective for interim reporting periods ending after June 15, 2009 and it will have no impact on the Company's statement of financial position or results of operations.

## 2. REGULATION

### October Base Rate Order

As a result of increases in NJNG's operation, maintenance and capital costs, on November 20, 2007, NJNG petitioned the New Jersey Board of Public Utilities (BPU) to increase base rates for delivery service by approximately \$58.4 million, which included a return on NJNG's equity component of 11.375 percent. This request was consistent with NJNG's objectives of providing safe and reliable service to its customers and earning a market-based return on its regulated investments.

On October 3, 2008, the BPU unanimously approved and made effective the settlement of NJNG's base rate case. 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, received an allowed return on equity component of 10.3 percent, reduced its depreciation expense component from 3.0 percent to 2.34 percent and reduced its annual depreciation expense by \$1.6 million as a result of the amortization of previously recovered asset retirement obligations.

### 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 one 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.

In May 2008, NJNG filed its Petition for the Annual Review of its CIP for recoverable CIP amounts for fiscal 2008, requesting an additional \$6.8 million and approval to modify its CIP recovery rates effective October 1, 2008. The additional amount brought the total recovery requested to \$22.4 million. The total recovery requested includes amounts accrued and estimated through September 30, 2008. On October 3, 2008, the BPU approved the CIP petition on a provisional basis, effective the date of the Board Order. As of March 31, 2009, NJNG has \$7.6 million accrued in Regulatory Assets in the Unaudited Condensed Consolidated Balance Sheets. On April 1, 2009, NJNG filed a petition with the BPU requesting an extension of its CIP for an additional year through 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. If accepted by the BPU, the CIP would remain in effect for an additional year or until a final Board Order is issued by the BPU.

In conjunction with the CIP, NJNG incurs costs related to its obligation to fund programs that promote customer conservation efforts during the three-year term of the CIP pilot program. As of March 31, 2009, NJNG had a remaining liability of \$305,000 related to these programs.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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Basic Gas Supply Service

BGSS is a BPU approved rate mechanism designed to allow for the recovery of natural gas commodity costs. As necessary, NJNG 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.

In May 2008, NJNG filed for an increase to the periodic BGSS factor to be effective October 1, 2008, that would have increased an average residential heating customer's bill by approximately 18 percent due to an increase in the price of wholesale natural gas. Subsequent to the filing, wholesale natural gas prices moderated, and on September 22, 2008, NJNG, the Staff of the BPU and the Department of the Public Advocate, Division of Rate Counsel (Rate Counsel) signed an agreement for an increase to the periodic BGSS factor that would increase an average residential heating customer's bill by approximately 8.9 percent. On October 3, 2008, the BPU approved the BGSS increase on a provisional basis, effective the date of the Board Order.

On December 17, 2008, NJNG provided notice that it would implement a \$30 million BGSS-related temporary rate credit that would lower residential and small commercial sales customers' bills in January and February 2009. This temporary rate credit was due primarily to a decline in wholesale commodity costs subsequent to the October 2008 BGSS price change. NJNG also extended and increased the per therm temporary rate credit to lower customer bills by an additional \$15 million through March 31, 2009 due to continuing lower wholesale natural gas costs.

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 2007, the BPU reduced the sharing percentage of the margin generated by the FRM program retained by NJNG from 20 percent to 15 percent effective November 1, 2007. In October 2008, the Board's base rate order provided for the extension of the incentive programs through October 31, 2011, along with an expansion of the storage incentive and FRM programs.

Societal Benefits Clause (SBC) and Weather Normalization Clause (WNC)

The SBC is comprised of three primary components: a Universal Service Fund rider (USF), a Manufactured Gas Plant (MGP) Remediation Adjustment (RA), and the New Jersey Clean Energy Program (NJCEP). In February 2008, NJNG filed an application regarding its SBC proposing no change to the rates previously approved in October 2007 (February 2008 SBC filing). On January 27, 2009, NJNG filed an application regarding its SBC to increase its RA factor and its NJCEP factor while maintaining its effective rate on USF (January 2009 SBC filing). The January 2009 SBC filing is subject to BPU staff and Rate Counsel review and must be approved by the BPU prior to implementing the new SBC rates.

USF

Through the USF, eligible customers receive a credit toward their utility bill. The credits applied to eligible customers are recovered through the USF rider in the SBC. NJNG recovers carrying costs on deferred USF balances.

In June 2008, the natural gas utilities in the State of New Jersey collectively filed with the BPU to increase the statewide USF recovery rate effective October 1, 2008. In the BPU's October 21, 2008 Order, the USF increase was

approved on a provisional basis, effective October 24, 2008, and it also approved interest on USF deferred balances at the Treasury Constant Maturity 2-year rate, plus 60 basis points, net of tax, with the rate changing on a monthly basis. NJNG believes the increase has a negligible impact on customers.

#### MGP

In October 2007, the BPU approved \$14.7 million in eligible costs to be recovered annually for MGP remediation expenditures incurred through June 30, 2006. The February 2008 SBC filing included MGP remediation expenditures incurred through June 30, 2007, resulting in an expected annual recovery of \$17.7 million. The January 2009 SBC filing included MGP remediation expenditures incurred through June 30, 2008 resulting in an expected annual recovery of \$20.7 million.



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NJCEP

In October 2008, the BPU released a final Order, updating state utilities' funding obligations for NJCEP for the period from January 1, 2009 to December 31, 2012. NJNG's share of the total funding requirement of \$1.2 billion is \$50.8 million. Accordingly, NJNG recorded the initial obligation and a corresponding regulatory asset at a present value of \$44.3 in the Unaudited Condensed Consolidated Balance Sheets. NJNG's annual obligation gradually increases from \$10.3 million in fiscal 2009 to \$15.9 million in fiscal 2012. As of March 31, 2009, NJNG had a \$40.8 million obligation remaining.

The January 2009 SBC filing included an increase to the NJCEP factor. The proposed factor is expected to recover \$12.9 million annually.

WNC

As of March 31, 2009, NJNG has a \$243,000 unrecovered balance related to gross margin variations incurred during the fiscal 2006 winter period. On October 3, 2008, the BPU provisionally approved a decrease to NJNG's WNC rate, effective the date of the Board Order, to fully recover its remaining WNC balance.

Economic Stimulus

On January 20, 2009, NJNG filed two petitions with the BPU seeking approval to implement programs designed to both stimulate the state and local economy through infrastructure investments and encourage energy efficiency. The Accelerated Infrastructure Program (AIP) would allow NJNG to accelerate \$70.8 million of 14 previously planned infrastructure projects, maintaining safe and reliable service to NJNG's customers while creating opportunity for approximately 75 to 100 new jobs. The AIP would be funded through an annual adjustment to customers' base rates. The second filing, for an Energy Efficiency (EE) Program and associated cost recovery mechanism, requests BPU approval to implement various programs to encourage energy efficiency for residential and commercial customers. NJNG proposed to recover the EE costs of approximately \$22.9 million over a 4-year period through a clause mechanism similar to the SBC. Both programs include the recovery of NJNG's overall weighted average cost of capital.

On April 16, 2009, the BPU approved NJNG's AIP allowing NJNG to commence construction on its 14 infrastructure projects. NJNG will make a filing for the recovery of infrastructure program investment costs in June 2010 to be effective October 1, 2010. The filing will allow the recovery of costs of the AIP construction activities for the period ending August 31, 2010, including the recovery of NJNG's overall weighted average cost of capital.

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## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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## Regulatory Assets &amp; Liabilities

The Company had the following regulatory assets, all related to NJNG, on the Unaudited Condensed Consolidated Balance Sheets:

(Thousands)	March 31, 2009	September 30, 2008	Recovery Period
Regulatory assets—current			
Underrecovered gas costs	\$ —	\$ 27,994	Less than one year (1)
WNC	243	919	Less than one year (2)
CIP	7,552	22,463	Less than one year (3)
Total current	\$ 7,795	\$ 51,376	
Regulatory assets—noncurrent			
Remediation costs (Notes 2 and 13)			
Expended, net of recoveries	\$ 84,826	\$ 92,164	(4)
Liability for future expenditures	120,230	120,730	(5)
CIP	88	2,397	(6)
Deferred income and other taxes	12,574	12,726	Various (7)
Derivatives (Note 3)	99,055	49,610	(8)
Postemployment benefit costs (Note 10)			
SBC/Clean Energy	52,397	52,519	(9)
Total noncurrent	\$411,211	\$340,670	
(1)	Recoverable, subject to BPU approval, through BGSS, without interest.		
(2)	Recoverable as a result of BPU approval in October 2008, without interest. This balance reflects the net results from winter period of fiscal 2006. No new WNC activity has been recorded since October 1, 2006 due to the existence of the CIP.		
(3)	Recoverable or refundable, subject to BPU annual approval, without interest. Balance, as of March 31, 2009, includes approximately \$3.0 million relating to the weather component of the calculation and approximately \$4.6 million relating to the customer usage component of the calculation. Recovery from customers is designed to be one year from date of rate approval by the BPU.		
(4)	Recoverable, subject to BPU approval, with interest over rolling 7-year periods.		
(5)	Estimated future expenditures. Recovery will be requested when actual expenditures are incurred (see Note 13. Commitments and Contingent Liabilities – Legal Proceedings).		
(6)	Recoverable or refundable, subject to BPU annual approval, without interest. Balance, as of March 31, 2009, includes approximately \$88,000 relating to the customer usage component of the calculation.		
(7)	Recoverable without interest, subject to BPU approval.		
(8)	Recoverable, subject to BPU approval, through BGSS, without interest.		
(9)	Recoverable or refundable, subject to BPU approval, without interest. Includes unrecognized service costs recorded in accordance with SFAS No. 158, Employers' Accounting for Defined Benefit Pension and Other Postemployment Plans that NJNG has determined are recoverable in base rates charged to customers (see Note 10. Employee Benefit Plans).		
(10)	Recoverable with interest, subject to BPU approval.		

If there are any changes in regulatory positions that indicate the recovery of regulatory assets is not probable, the related cost would be charged to income in the period of such determination.

The Company had the following regulatory liabilities, all related to NJNG, on the Unaudited Condensed Consolidated Balance Sheets:

(Thousands)	March 31, 2009	September 30, 2008
Regulatory liabilities—current		
Overrecovered gas costs (1)	\$13,871	—
Total current	\$13,871	—
Regulatory liabilities—noncurrent		
Cost of removal obligation (2)	\$58,587	\$63,419
Total noncurrent	\$58,587	\$63,419

(1) Refundable, subject to BPU approval, through BGSS with interest.

(2) NJNG accrues and collects for cost of removal in rates. This liability represents collections in excess of actual expenditures. Approximately \$21.6 million, including accretion of \$742,000 for the six months ended March 31, 2009, of regulatory assets relating to asset retirement obligations have been netted against the cost of removal obligation as of March 31, 2009 (see Note 11. Asset Retirement Obligations).

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## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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## 3. DERIVATIVE INSTRUMENTS

The Company and its subsidiaries are subject to commodity price risk due to fluctuations in the market price of natural gas. To manage this risk, the Company and its subsidiaries enter into a variety of derivative instruments including, but not limited to, futures contracts, physical forward contracts, financial options, and swaps to economically hedge the commodity price risk associated with its existing and anticipated commitments to purchase and sell natural gas. These contracts generally qualify as derivatives in accordance with SFAS 133, Accounting for Derivative Instruments and Hedging Activities. As a result, in accordance with the provisions of SFAS 133 all of the financial and certain of the Company's physical derivative instruments are recorded at fair value in the Unaudited Condensed Consolidated Balance Sheets. The Company chooses not to designate its derivatives as hedging instruments pursuant to SFAS 133, and therefore changes in the fair value of the derivative instruments are recorded as a component of Gas purchases or Operating revenues, for NJRES and NJR Energy, respectively, in the Unaudited Condensed Consolidated Statements of Income as unrealized gains or losses. Changes in fair value of NJNG's derivative instruments are recorded as a component of Regulatory assets or liabilities in the Unaudited Condensed Consolidated Balance Sheets, as these amounts will be recovered through future BGSS amounts as an increase or reduction to the cost of natural gas in NJNG's tariff.

Effective October 1, 2007, the Company elected to discontinue the use of the "normal purchase normal sales" (normal) scope exception of SFAS 133 for all new physical commodity contracts entered into on or after October 1, 2007 by NJRES. For these contracts, the changes in fair value are included currently in earnings. Also, effective October 1, 2008, due to changes in the Company's ability to assert physical delivery, the Company is no longer applying normal treatment to physical commodity contracts executed prior to October 1, 2007. Therefore, all NJRES physical commodity contracts are derivatives and are accounted for at fair value in the Unaudited Condensed Consolidated Balance Sheets, with changes in fair value included as a component of operating revenue or gas purchases, as appropriate, in the Unaudited Condensed Consolidated Statements of Income. The Company continues to apply the normal scope exception for all physical commodity contracts at NJNG and NJR Energy, and as a result the profit or loss on these contracts is not recorded until physical delivery occurs.

As described in Note 1, General, NJR adopted the provisions of SFAS 161, which requires enhanced disclosures surrounding derivative activities. The additional quantitative and qualitative disclosures are included throughout this note. For a more detailed discussion of the Company's fair value policies and level disclosures please see Note 4, Fair Value Measurements.

The following table reflects the fair value of NJR's derivative assets and liabilities recognized in its Unaudited Condensed Consolidated Balance Sheets as of March 31, 2009:

(Thousands)	Balance Sheet Location	Fair Value	
		Asset Derivatives	Liability Derivatives
Derivatives not designated as hedging instruments under SFAS 133:			
NJNG:			
Financial derivative commodity contracts	Derivatives - Current	\$ 12,229	\$108,207
	Derivatives - Noncurrent	—	3,078

NJRES:			
Physical forward commodity contracts	Derivatives - Current	18,848	16,071
	Derivatives - Noncurrent	6,631	31
Financial derivative commodity contracts	Derivatives - Current	210,557	160,402
	Derivatives - Noncurrent	14,309	9,697
NJR Energy:			
Financial derivative commodity contracts	Derivatives - Current	1,180	575
	Derivatives - Noncurrent	1,951	232
Total fair value of derivatives		\$265,705	\$298,293

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## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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As discussed above, the Company no longer applies the normal scope exception at NJRES and chooses not to apply the hedge accounting provisions of SFAS 133 to any of NJR and subsidiaries' derivatives. As a result, any unrealized gains (losses) related to NJRES' open financial and physical commodity contracts and NJR Energy's financial derivatives are recognized in the Unaudited Condensed Consolidated Statements of Income as a component of Operating revenue or Gas purchases, as appropriate. NJRES' utilizes financial derivatives to hedge the margin associated with the purchase of physical gas for injection into storage and the subsequent sale of physical gas at a later date. The gains (losses) on these financial transactions are recognized upon settlement in Gas purchases. The gains (losses) on the financial transactions that are economic hedges of the cost of the purchased gas are recognized prior to the gains (losses) on the physical transaction that is recognized when the natural gas is sold. Therefore, mismatches between the timing of recognizing realized gains or losses on the financial derivative instruments and the timing of the actual sale of the natural gas that is being economically hedged creates volatility in the results of NJRES, although the Company's intended economic results relating to the entire transaction are unaffected.

Gains (losses) at NJRES and NJR Energy included as a component of Gas purchases and Operating revenues, as noted below, for the three months ended March 31, 2009 are as follows:

(Thousands)	Location of Gain or (Loss) Recognized in Income on Derivative	Amount of Gain or (Loss) Recognized in Income on Derivative
Derivatives not designated as hedging instruments under SFAS 133:		
NJRES:		
Physical commodity contracts	Operating revenues	\$ 8,039
Physical commodity contracts	Gas purchases	(570)
Financial derivatives	Gas purchases	32,157
Subtotal NJRES		39,626
NJR Energy:		
Financial derivatives	Operating revenues	(10,010)
Total NJRES and NJR Energy unrealized and realized gains		\$29,616

NJNG's financial derivatives are part of its regulated risk management activities that serve to mitigate BGSS costs passed on to its customers. As these transactions are entered into pursuant to and recoverable through regulatory riders, any changes in the value of NJNG's financial derivatives are deferred in Regulatory Assets or Liabilities and there is no impact to earnings.

As of March 31, 2009, NJNG, NJRES and NJR Energy had the following outstanding long (short) derivatives:

		Volume (Bcf)
NJNG	Futures	16.8
	Swaps	(0.3)
	Options	10.4
NJRES	Futures	(6.7)
	Swaps	(39.5)

	Options	3.6
	Physical	65.8
NJR Energy	Swaps	3.8

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Generally, exchange-traded contracts require posted collateral, referred to as margin, usually in the form of cash. The amount of margin required is comprised of a fixed initial amount based on the contract and a variable amount based on market price movements from the initial trade price. The Company maintains broker margin accounts for NJNG and NJRES. The balances are as follows:

(Thousands)	Balance Sheet Location	March 31, 2009	September 30, 2008
NJNG broker margin deposit	Broker margin - Current Assets	\$104,497	\$ 41,277
NJRES broker margin (liability)	Broker margin - Current Liabilities	\$ (26,746)	\$(29,072)

## Wholesale Credit Risk

NJNG, NJRES and NJR Energy are exposed to credit risk as a result of their wholesale marketing activities. NJR monitors and manages the credit risk of its wholesale marketing operations through credit policies and procedures that management believes reduce overall credit risk. These policies include a review and evaluation of current and prospective counterparties' financial statements and/or credit ratings, daily monitoring of counterparties' credit limits and exposure, daily communication with traders regarding credit status and the use of credit mitigation measures, such as collateral requirements and netting agreements. Examples of collateral include letters of credit and cash received for either prepayment or margin deposit. Collateral may be requested due to NJR's election not to extend credit or because exposure exceeds defined thresholds. Most of NJR's wholesale marketing contracts contain standard netting provisions. These contracts include those governed by the International Swaps and Derivatives Association (ISDA) and the North American Energy Standards Board (NAESB). The netting provisions refer to payment netting, whereby receivables and payables with the same counterparty are offset and the resulting net amount is paid to the party to which it is due.

As a result of the inherent volatility in the prices of natural gas commodities and derivatives, the market value of contractual positions with individual counterparties could exceed established credit limits or collateral provided by those counterparties. If a counterparty failed to perform the obligations under its contract (for example, failed to deliver or pay for natural gas), then the Company could sustain a loss.

The following is a summary of gross credit exposures grouped by investment and noninvestment grade counterparties, as of March 31, 2009. Internally-rated exposure applies to counterparties that are not rated by Standard & Poor's (S&P) or Moody's Investors Service, Inc (Moody's). In these cases, the company's or guarantor's financial statements are reviewed, and similar methodologies and ratios used by S&P and/or Moody's are applied to arrive at a substitute rating. Gross credit exposure is defined as the unrealized fair value of physical and financial derivative commodity contracts plus any outstanding receivable for the value of natural gas delivered for which payment has not yet been received. The amounts presented below have not been reduced by any collateral received or netting and exclude accounts receivable for retail natural gas sales and services.

(Thousands)	Gross Credit Exposure
Investment grade	\$163,664
Noninvestment grade	14,960
Internally rated investment grade	17,014
Internally rated noninvestment grade	1,897
Total	\$197,535



Conversely, certain of NJRES', NJNG's and NJR Energy's derivative instruments are tied to agreements containing provisions that would require cash collateral payments from the Company if certain events occur. These provisions vary based upon the terms in individual counterparty agreements and can result in cash payments if NJNG's credit rating were to fall below its current level. NJNG's credit rating, with respect to Standard and Poor's, reflects the overall corporate credit profile. Specifically, most, but not all, of these additional payments will be triggered if NJNG's debt is downgraded by the major credit agencies, regardless of investment grade status. As well, some of these agreements include threshold amounts that would result in additional collateral payments if the values of derivative liabilities were to exceed the maximum values provided for in relevant counterparty agreements. Other provisions include payment features that are not specifically tied to ratings, but are based on certain financial metrics.