AGL RESOURCES INC
Form 8-K
April 27, 2005

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

FORM 8-K

CURRENT REPORT

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

Date of Report (Date of earliest event reported): April 27, 2005

AGL RESOURCES INC.
(Exact name of registrant as specified in its charter)

Georgia	**1-14174**	**58-2210952**
(State or other jurisdiction of incorporation)	(Commission File No.)	(I.R.S. Employer Identification No.)

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

404-584-4000
(Registrant's telephone number, including area code)

Not Applicable
(Former name or former address, if changed since last report)

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

[ ] Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

[ ] Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

[ ] Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

[ ] Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 2.02 Results of Operations and Financial Condition

On April 27, 2005, AGL Resources Inc. announced its financial results for the three months ended March 31, 2005 and certain other information. A copy of AGL Resources' press release announcing such financial results and other information is attached as Exhibit 99.1 hereto and incorporated by reference herein.

The information in the preceding paragraph, as well as Exhibit 99.1 referenced therein, shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, nor shall it be deemed incorporated by reference in any filing under the Securities Act of 1933.

Item 7.01 Regulation FD Disclosure

On April 27, 2005 at 4:30 p.m. (ET) AGL Resources Inc. plans to hold its first quarter 2005 earnings conference call. The Company is filing this Form 8-K to provide selected discussion of financial results, liquidity and market risks as of March 31, 2005.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

Certain expectations and projections regarding our future performance referenced in this report, as well as in other reports and proxy statements we file with the Securities and Exchange Commission (SEC), are forward-looking statements. Officers and other key employees may also make verbal statements to analysts, investors, regulators, the media and others that are forward-looking.

Forward-looking statements involve matters that are not historical facts, such as projections of our financial performance, management's goals and strategies for our business and assumptions regarding the foregoing. Because these statements involve anticipated events or conditions, forward-looking statements often include words such as "anticipate," "assume," "believe," "can," "could," "estimate," "expect," "forecast," "indicate," "intend," "may," "plan," "predi "should," "target," "will," "would" or similar expressions. For example, in this report, we have forward-looking statements regarding our expectations for various items, including:

- revenue growth;
- operating income growth;
- cash flows from operations;
- operating expense growth;
- capital expenditures;
- our business strategies and goals;
- our potential for growth and profitability;
- our ability to integrate our recent and future acquisitions;
- trends in our business and industries, and
- developments in accounting standards

Do not unduly rely on forward-looking statements. They represent our expectations about the future and are not guarantees. Our expectations are based on currently available competitive, financial and economic data along with our operating plans. While we believe that our expectations are reasonable in view of the currently available information, our expectations are subject to future events, risks and uncertainties, and there are several factors - many beyond our control - that could cause results to differ significantly from our expectations. We caution readers that, in addition to the important factors described elsewhere in this report, the factors set forth in our 2004 Annual Report on Form 10-K filed with the SEC on February 15, 2005 under Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" under the caption "Risk Factors," among others, could cause our business, results of operations or financial condition in 2005 and thereafter to differ significantly from those expressed in any forward-looking statements. There also may be other factors not described in this report that could cause results to

differ significantly from our expectations.

Forward-looking statements are only as of the date they are made, and we do not undertake any obligation to update these statements to reflect subsequent changes.

Overview

We are a Fortune 1000 energy services holding company whose principal business is the distribution of natural gas in six states - Florida, Georgia, Maryland, New Jersey, Tennessee and Virginia. Our six utilities serve more than 2.3 million end-use customers, making us the largest distributor of natural gas in the Southeast and mid-Atlantic regions of the United States, based on customer count. We also are involved in various related businesses, including retail natural gas marketing to end-use customers in Georgia; natural gas asset management and related logistics activities for our own utilities as well as for other non-affiliated companies; natural gas storage arbitrage and related activities; operation of high-deliverability underground natural gas storage assets; and construction and operation of telecommunications conduit and fiber infrastructure within select metropolitan areas. We manage these businesses through four operating segments - distribution operations, retail energy operations, wholesale services and energy investments - and a non-operating corporate segment.

The distribution operations segment is the largest component of our business and is comprehensively regulated by regulatory agencies in six states. These agencies approve rates designed to provide us the opportunity to generate revenues; to recover the cost of natural gas delivered to our customers and our fixed and variable costs such as depreciation, interest, maintenance and overhead costs; and to earn a reasonable return for our shareholders. With the exception of Atlanta Gas Light Company (Atlanta Gas Light), our largest utility franchise, the earnings of our regulated utilities are weather-sensitive to varying degrees. Although various regulatory mechanisms provide a reasonable opportunity to recover our fixed costs regardless of volumes sold, the effect of weather manifests itself in terms of higher earnings during periods of colder weather and lower earnings with warmer weather. Our retail energy operations segment, which includes SouthStar Energy Services LLC (SouthStar), also is weather sensitive, and uses a variety of hedging strategies to mitigate potential weather impacts. Our utilities and SouthStar face competition in the residential and commercial customer markets based on customer preferences for natural gas compared with other energy products, as well as the price of those products relative to that of natural gas.

We derived approximately 96% of our earnings before interest and taxes (EBIT) during the three months ended March 31, 2005 from our regulated natural gas distribution business and from the sale of natural gas to end-use customers in Georgia by SouthStar. This statistic is significant because it represents the portion of our earnings that results directly from the underlying business of supplying natural gas to retail customers. Although SouthStar is not subject to the same regulatory framework as our utilities, it is an integral part of the retail framework for providing gas service to end-use customers in the state of Georgia. For more information regarding our measurement of EBIT and the items it excludes from operating income and net income, see “Results of Operations - AGL Resources.”

The remaining 4% of our EBIT was principally derived from businesses that are complementary to our natural gas distribution business. We engage in natural gas asset management and operation of high deliverability natural gas underground storage as subordinate activities to our utility franchises. These businesses allow us to be opportunistic in capturing incremental value at the wholesale level, provide us with deepened business insight about natural gas market dynamics and facilitate our ability, in the case of asset management, to provide transparency to regulators as to how that value can be captured to benefit our utility customers through sharing arrangements. Given the volatile and changing nature of the natural gas resource base in North America and globally, we believe that participation in these related businesses strengthens our business vitality.

Industry Dynamics and Competition The natural gas industry continues to face a number of challenges, most of which relate to the supply of, and demand for, natural gas across the United States. A confluence of factors - including higher peak demands across all customer classes; incremental demand for natural gas to fuel the production of electricity, declining continental supply, particularly in the Gulf of Mexico region, and sustained higher pricing levels relative to historical averages - have created a mismatch between demand and declining supply.

These factors continue to challenge our industry to unlock new sources of natural gas supply to serve the North American market. Liquefied natural gas (LNG) continues to grow in importance as an incremental supply source to meet the expected growth in demand for natural gas. Expansion of existing LNG terminals and construction of new facilities both point toward rapid import expansions throughout the rest of this decade. In addition to expansion of LNG supplies, access to previously restricted areas for natural gas drilling also will be critical in meeting future supply needs. The challenge is magnified by the time lags and capital expenditures required to bring new LNG facilities and new drilling rigs online and by the absence of a comprehensive national energy policy designed to facilitate the construction and expansion process.

The natural gas industry also continues to face significant competition from the electric utilities serving the residential and small commercial markets as the potential replacement of natural gas appliances with electric appliances becomes more prevalent. The primary competitive factors are the price of energy and the comfort of natural gas heating compared to electric heating and other energy sources. The increase in wholesale natural gas prices over the last several years has resulted in increases in the costs of natural gas billed to our customers and has affected, to some extent, our ability to retain customers, which remains one of our greater challenges in our southernmost utilities in 2005 and future years.

Integration of NUI Corporation We have made significant progress in integrating the assets and operations of NUI Corporation (NUI), which we acquired on November 30, 2004, into our business operations. In the first quarter of 2005, we consolidated a number of NUI's business technology platforms into our enterprise-wide systems, including the accounting, payroll, human resources and supply chain functions. We also consolidated the call center operation that previously served the NUI utilities into our centralized call center. The combination of system integrations and the application of our best-practice operational model in managing the NUI assets already has resulted in improvements in the metrics we use to measure our business results. Such metrics include the productivity of our field personnel, the speed of our response to customers, personal and system safety and system reliability.

Internal Controls Section 404 of the Sarbanes-Oxley Act of 2002 (SOX 404) and related rules of the SEC require management of public companies to assess the effectiveness of the company's internal controls over financial reporting as of the end of each fiscal year. In our 2004 Annual Report on Form 10-K filed with the SEC on February 15, 2005 we noted that, for 2004, the scope of our assessment of our internal controls over financial reporting included all our consolidated entities except those falling under NUI, which we acquired on November 30, 2004, and Jefferson Island Storage & Hub, LLC (Jefferson Island), which we acquired on October 1, 2004. In accordance with the SEC's published guidance, we excluded these entities from our assessment as they were acquired late in the year, and it was not possible to conduct our assessment between the date of acquisition and the end of the year. SEC rules require that we complete our assessment of the internal control over financial reporting of these entities within one year from the date of acquisition.

We have initiated our efforts to assess the systems of internal control related to NUI's and Jefferson Island's businesses to comply with the SEC's requirements under both Sections 302 and 404 of the Sarbanes-Oxley Act. During the first quarter of 2005, we converted and integrated substantially all of NUI's accounting systems and internal control processes into our corporate accounting systems and internal control processes. As part of this process, we are addressing and resolving the material deficiencies in internal controls for the NUI business identified by NUI's external and internal auditors during audits performed in fiscal years 2003 and 2004, as more fully described in our 2004 Annual Report on Form 10-K. While the conversion of financial systems is a key step toward remediation of the control deficiencies, we still are in the process of documenting the internal control process for the NUI business and we continue to remediate known deficiencies in internal controls.

Results of Operations

AGL Resources We acquired Jefferson Island and NUI in the fourth quarter of 2004. As a result, these acquired operations are included in our results of operations for the three months ended March 31, 2005 but are not included for

the same period in 2004.

Beginning in 2005, we added an additional segment, Retail Energy Operations, which consists of the operations of SouthStar, our retail gas marketing subsidiary that conducts business primarily in Georgia. We added this segment due to our application of accounting guidance in SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information," ("FAS 131") in consideration of the impact of the NUI and Jefferson Island acquisitions and it is consistent with our desire to provide transparency and visibility to SouthStar on a standalone basis. Separating SouthStar into its own segment also provides additional visibility to the remaining businesses in the Energy Investments segment, principally Jefferson Island and Pivotal Propane of Virginia, Inc. (Pivotal Propane), which are more closely related in structure and operation. Additionally, we have restated the segment information for the three months ended March 31, 2004 in accordance with the guidance set forth in FAS 131.

Revenues We generate nearly all our operating revenues through the sale, distribution and storage of natural gas. We include in our consolidated revenues an estimate of revenues from natural gas distributed, but not yet billed, to residential and commercial customers from the latest meter reading date to the end of the reporting period. We record these estimated revenues as unbilled revenues on our consolidated balance sheet.

A significant portion of our operations is subject to variability associated with changes in commodity prices and seasonal fluctuations. During the heating season, primarily from November through March, natural gas usage and operating revenues are higher since generally more customers will be connected to our distribution systems and natural gas usage is higher in periods of colder weather than in periods of warmer weather. Commodity prices tend to be higher in colder months as well. Our non-utility businesses principally use physical and financial arrangements to economically hedge the risks associated with seasonal fluctuations and changing commodity prices. Certain hedging and trading activities may require cash deposits to satisfy margin requirements. In addition, because these economic hedges do not generally qualify for hedge accounting treatment, our reported earnings for the wholesale services and retail energy operations segments reflect changes in the fair value of certain derivatives and these values may change significantly from period to period.

Operating margin and EBIT We evaluate the performance of our operating segments using the measures of operating margin and EBIT. We believe operating margin is a better indicator than revenues for the contribution resulting from customer growth in our distribution operations and retail energy operations segments since the cost of gas can vary significantly and is generally passed directly to our customers. We also consider operating margin to be a better indicator in our wholesale services and energy investments segments since it is a direct measure of gross profit before overhead costs. Management believes EBIT is useful to investors as a measurement of our operating segments' performance because it can be used to evaluate the effectiveness of our businesses from an operational perspective, exclusive of the costs to finance those activities and exclusive of income taxes, neither of which affects the efficiency of the underlying operations.

Our operating margin and EBIT are not measures that are considered to be calculated in accordance with GAAP. You should not consider operating margin or EBIT an alternative to, or a more meaningful indicator of, our operating performance than operating income or net income as determined in accordance with GAAP. In addition, our operating margin or EBIT measures may not be comparable to a similarly titled measure of another company. The following are reconciliations of our operating margin and EBIT to operating income and net income, together with other consolidated financial information for the three months ended March 31, 2005 and 2004.

	Three months ended March 31,		
In millions	**2005**	**2004**	**2005 vs. 2004**
Operating revenues	$ 912	$ 651	40%
Cost of gas	572	393	46
Operating margin	340	258	32
Operating expenses	159	125	27
Operating income	181	133	36
Other income	1	1	-
Minority interest	(13)	(11)	(18)
EBIT	169	123	37
Interest expense	(26)	(16)	(63)
Earnings before income taxes	143	107	34
Income taxes	(55)	(41)	(34)
Net income	$ 88	$ 66	33%
Basic earnings per common share	$ 1.15	$ 1.02	13%
Fully diluted earnings per common share	$ 1.14	$ 1.00	14%
Weighted average number of common shares outstanding			

Basic	76.9	64.6	19%
Fully diluted	77.6	65.5	19%

Segment information Operating revenues, operating margin and EBIT information for each of our segments are contained in the following table for the three months ended March 31, 2005 and 2004:

2005 (*in millions*)	**Operating revenues**	**Operating margin**	**EBIT**
Distribution operations	$ 634	$ 253	$ 123
Retail energy operations	314	66	40
Wholesale services	11	11	4
Energy investments	12	9	5
Corporate (1)	(59)	1	(3)
Consolidated	$ 912	$ 340	$ 169
2004			
Distribution operations	$ 389	$ 180	$ 82
Retail energy operations	307	57	33
Wholesale services	20	20	12
Energy investments	1	1	1
Corporate (1)	(66)	-	(5)
Consolidated	$ 651	$ 258	$ 123

(1) Includes intercompany eliminations

First quarter 2005 compared to first quarter 2004

Operating Margin $73 million of the $82 million increase in operating margin resulted from distribution operations, of which approximately $70 million resulted from the acquisition of NUI. The remaining $12 million primarily reflects increased contributions from retail energy operations in the amount of $9 million, increased contributions of $8 million in the energy investments segment, and an increase of $1 million in the corporate segment, offset by a $9 million decrease in wholesale services.

Operating Expenses Operating expenses increased by $34 million, of which $32 million was from our distribution operations where $37 million was as a result of the NUI acquisition. The higher expenses from NUI were offset by $2 million of lower expenses at Virginia Natural Gas Company and $1 million of lower expenses related to favorable bad debt expense compared to last year. Wholesale services’ operating expenses were $1 million less than in 2004 because of costs related to Sequent’s Energy Trading and Risk Management system in the first quarter of 2004. Our energy investments expenses increased $4 million due primarily to the Jefferson Island acquisition. Operating expenses for the retail energy operations segment were essentially flat year-over-year.

Interest Expense Interest expense increased by $10 million from last year’s first quarter, primarily as a result of NUI and Jefferson Island acquisition debt ($8 million) and higher short-term interest rates ($2 million) as shown in the following table:

	Three months ended March 31,		
Dollars in millions	**2005**	**2004**	**2005 vs. 2004**
Average debt outstanding (1)	$ 1,820	$ 1,214	$ 606
Average rate	5.7%	5.3%	0.4%

(1) Daily average of all outstanding debt.

If, for the three months ended March 31, 2005, market interest rates on our variable rate debt had been 100 basis points higher, representing a 6.1% interest rate rather than our actual 5.1% interest rate, our year-to-date pretax interest expense would have increased by $4 million.

Income Taxes Income taxes increased by $14 million, primarily as a result of the higher pre-tax income for the first quarter of 2005.

Shares Outstanding Weighted average shares outstanding increased 12.3 million during the first quarter 2005, primarily as a result of our 11-million share equity offering completed in November 2004.

Distribution Operations

Distribution operations includes our natural gas local distribution utility companies, which construct, manage and maintain natural gas pipelines and distribution facilities and serve 2.3 million end-use customers. Our distribution utilities include:

- *Atlanta Gas Light*
- *Elizabethtown Gas*
- *Virginia Natural Gas Company, Inc. (Virginia Natural Gas)*
- *Florida City Gas (Florida Gas)*
- *Chattanooga Gas Company (Chattanooga Gas)*
- *Elkton Gas*

Each utility operates subject to regulations provided by the state regulatory agencies in its service territories with respect to rates charged to our customers, maintenance of accounting records and various other service and safety matters. Rates charged to our customers vary according to customer class (residential, commercial or industrial) and rate jurisdiction. Rates are set at levels that should generally allow for the recovery of all prudently incurred costs, including a return on rate base sufficient to pay interest on debt and provide a reasonable return on common equity. Rate base consists generally of the original cost of utility plant in service, working capital, inventories and certain other assets; less accumulated depreciation on utility plant in service, net deferred income tax liabilities and certain other deductions. We continuously monitor the performance of our utilities to determine whether rates need to be adjusted through the regulatory process.

Updates The following is a summary of significant developments with regard to our distribution operations segment that have occurred since we filed our 2004 Annual Report on Form 10-K on February 15, 2005.

On October 15, 2004, Atlanta Gas Light filed a request for a $26 million rate increase from the Georgia Public Service Commission (Georgia Commission) which would continue its performance-based rate plan (PBR) and included a return on equity (ROE) band of 10.2% to 12.2% with an 11.2% midpoint. This filing was required by the PBR implemented for AGLC in 2001. On February 25, 2005, the Georgia Commission Adversary Staff and intervening parties filed rebuttal testimony. Adversary Staff put forth a case calling for a $55.6 million base rate reduction predicated on a 9.0% ROE.

In March 2005, the Virginia State Corporation Commission staff issued a report alleging that Virginia Natural Gas' rates were excessive and that its rates should be adjusted to produce a $15 million reduction in revenue. The staff also filed a motion requesting that Virginia Natural Gas' rates be declared interim and subject to refund. On April 11, 2005, Virginia Natural Gas responded to the staff's report and motion and contested the allegations in the report and objected to the motion filed by the staff. Virginia Natural Gas also notified the Virginia State Corporation Commission that it would file a general rate case before December 31, 2005. As of April 27, 2005, the Virginia Commission has taken no action on the staff's motions.

On April 26, 2005, Elizabethtown Gas presented the New Jersey Board of Public Utilities (NJBPU) with a proposal to accelerate the replacement of approximately 88 miles of 8" to 12" elevated pressure cast iron main. Under the proposal, approximately $42 million in estimated capital costs incurred over a three year period would be recovered through a pipeline replacement rider similar to the program in effect at Atlanta Gas Light. If the program as proposed is approved, cost recovery would occur on a one-year lag basis, with collections starting on October 1, 2006 and extending through December 31, 2009, after which time the program would be rolled into base rates.

In October 2004, the Tennessee Regulatory Authority (Tennessee Authority) denied Chattanooga Gas Company's (CGC) request for a $4 million rate increase, instead approving an increase of approximately $1 million based on a 10.2% return on equity. In November 2004, the Tennessee Authority granted Chattanooga Gas' motion for reconsideration of the rate increase and in December 2004 heard oral arguments on the issues of the appropriate capital structure and the return on equity to be used in setting Chattanooga Gas' rates. In March 2005, CGC filed additional testimony and supporting documentation at the request of the Tennessee Authority. The Tennessee Authority has yet to issue a final ruling on our request for reconsideration.

Operations On March 1, 2005, Atlanta Gas Light completed its acquisition of 250 miles of interstate pipeline in central Georgia from Southern Natural Gas (SNG), a subsidiary of El Paso Corporation, for $32 million. The acquisition will improve deliverable capacity and reliability of the storage capacity from our LNG facility in Macon to our markets in Atlanta.

Results of Operations for our distribution operations segment for the three months ended March 31, 2005 and 2004 are as follows:

In millions	Three months ended March 31, 2005	2004	2005 vs. 2004
Operating revenues	$ 634	$ 389	$ 245
Cost of gas	381	209	172
Operating margin	253	180	73
Operating expenses			
Operation and maintenance	93	71	22
Depreciation and amortization	28	21	7
Taxes other than income	9	6	3
Total operating expenses	130	98	32
Operating income	123	82	41
Other income	-	-	-
EBIT	$ 123	$ 82	$ 41
Metrics *(includes information only for 2005 for utilities acquired from NUI)*			
Average end-use customers (in thousands)	2,266	1,840	23%
Operation and maintenance expenses per customer	$ 42	$ 38	11
EBIT per customer	$ 53	$ 45	18
Throughput (in millions of dekatherms)			
Firm	106	90	18%
Interruptible	33	28	18
Total	139	118	18%
Heating degree days (1):			% Colder / (Warmer)
Florida	490	-	-%
Georgia	1,396	1,503	(7)
Maryland	2,684	-	-
New Jersey	2,755	-	-
Tennessee	1,545	1,716	(10)
Virginia	2,056	1,853	11

(1) We measure the effects of weather on our businesses using “degree days.” The measure of degree days for a given day is the difference between the average daily actual temperature and the baseline temperature of 65 degrees Fahrenheit. Heating degree days result when the average daily actual temperature is less than 65-degrees. Generally, increased heating degree days result in greater demand for gas on our distribution systems.

First quarter 2005 compared to first quarter 2004

Operating Margin The increase in operating margin of $73 million, or 41%, was primarily a result of the addition of NUI’s operations, which contributed $70 million. The remainder of the increase was the combination of higher operating margin at Atlanta Gas Light offset by lower operating margin at Virginia Natural Gas. The increase at Atlanta Gas Light was a result of higher PRP revenues, additional revenue from gas storage carrying charges billed to marketers and increased customer usage and growth. These results were offset by a reduction in operating margins at Virginia Natural Gas, resulting from lower use per heating degree day and a change in the weather normalization adjustment calculation resulting from a regulatory order.

Operating Expenses The increase in operating expenses of $32 million, or 33%, primarily was a result of the addition of NUI’s operations, which contributed $37 million. This increase was offset primarily by lower operating expenses at

Virginia Natural Gas, largely in part to lower bad debt and payroll expenses.

EBIT The increase in EBIT of $41 million was primarily from the inclusion of NUI's operations, which contributed approximately $34 million.

Retail Energy Operations

Our retail energy operations segment consists of SouthStar, a joint venture formed in 1998 by our subsidiary, Georgia Natural Gas Company, Piedmont Natural Gas and Dynegy Inc. (Dynegy). The purpose was to market natural gas and related services to retail customers on an unregulated basis, principally in Georgia. On March 11, 2003, we purchased Dynegy's 20% ownership interest.

We currently own a non-controlling 70% financial interest in SouthStar, and Piedmont owns the remaining 30%. Our 70% interest is non-controlling because all significant management decisions require approval of both owners. On March 29, 2004, we executed an amended and restated partnership agreement with Piedmont. This amended and restated partnership agreement calls for SouthStar's future earnings starting in 2004 to be allocated 75% to our subsidiary and 25% to Piedmont. In addition, we executed a services agreement which provided that AGL Services Company will provide and administer accounting, treasury, internal audit, human resources and information technology functions for SouthStar.

Results of operations for our retail energy operations segment for the three months ended March 31, 2005 and 2004 are shown in the following table.

	Three months ended March 31,					
In millions		**2005**		**2004**		**2005 vs. 2004**
Operating revenues	$	314	$	307	$	7
Cost of sales		248		250		(2)
Operating margin		66		57		9
Operating expenses						
Operation and maintenance		13		13		-
Depreciation and amortization		-		-		-
Taxes other than income		-		-		-
Total operating expenses		13		13		-
Operating income		53		44		9
Minority interest (1)		(13)		(11)		(2)
EBIT	$	40		33	$	7
Average customers (in thousands)		531		550		(4%)
Market share in Georgia		36%		37%		(3%)

(1) Minority interest adjusts our earnings to reflect our 75% share of SouthStar's earnings.

First quarter 2005 compared to first quarter 2004

Operating Margin The $9 million increase in operating margin is primarily a result of higher commodity margins in 2005, partly offset by lower sales volumes due to 7% warmer weather in 2004. These margins resulted from larger storage spreads and favorable asset management activities during the quarter.

Operating Expenses Operating expenses were virtually flat year-over-year. Bad debt expense decreased $2 million in 2005 as a result of significantly lower write-offs. However, this was substantially offset by a one-time vendor performance credit and the timing of marketing expenses in 2005.

EBIT SouthStar's EBIT contribution of $40 million in 2005 was $7 million higher than last year, reflecting higher commodity margins and favorable asset management results during the quarter.

Wholesale Services

Wholesale services consists of Sequent, our subsidiary involved in asset optimization, transportation, storage, producer and peaking services and wholesale marketing. Our asset optimization business focuses on capturing economic value from idle or underutilized natural gas assets, which are typically amassed by companies via investments in or contractual rights to natural gas transportation and storage assets. Margin is typically created in this business by participating in transactions that balance the needs of varying markets and time horizons.

Sequent provides its customers with natural gas from the major producing regions and market hubs primarily in the Eastern and Mid-Continental United States. Sequent also purchases transportation and storage capacity to meet its delivery requirements and customer obligations in the marketplace. Sequent's customers benefit from its logistics expertise and ability to deliver natural gas at prices that are advantageous relative to other alternatives available to its end-use customers.

The following is a summary of significant developments with regard to our wholesale services segment that have occurred since we filed our 2004 Annual Report on Form 10-K on February 15, 2005.

Asset Management Transactions Our asset management customers include our own utilities, nonaffiliated utilities, municipal utilities and large industrial customers. These customers must contract for transportation and storage services to meet their demands, and they typically contract for these services on a 365-day basis even though they may only need a portion of these services to meet their peak demands for a much shorter period. We enter into agreements with these customers, either through contract assignment or agency arrangement, whereby we use their rights to transportation and storage services during periods when they do not need them. We capture margin by optimizing the purchase, transportation, storage and sale of natural gas, and we typically either share profits with customers or pay them a fee for using their assets.

On April 1, 2005, in connection with the acquisition of NUI, Sequent commenced asset management responsibilities for Elizabethtown Gas, Florida Gas and Elkton Gas. The following table summarizes Sequent's asset management transactions with our affiliated utilities.

Dollars in millions	**Duration of contract (in years)**	**Expiration date**	**Frequency of payment**	**Profits shared / fees paid in 2005 (1)**