PACIFIC ENTERPRISES INC
Form 10-Q
August 07, 2008

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 June 30, 2008

Commission File Number	Name of Registrant as Specified in its Charter, Address and Telephone Number	State of Incorporation	I.R.S. Employer Identification No.
1-40	PACIFIC ENTERPRISES 101 Ash Street San Diego, California 92101 (619) 696-2020	California	94-0743670
1-1402	SOUTHERN CALIFORNIA GAS COMPANY 555 West Fifth Street Los Angeles, California 90013 (213) 244-1200	California	95-1240705

No Change
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X No

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

Large accelerated filer	[ ]	Accelerated filer	[ ]	Non-accelerated filer	[X]

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

Yes		No	X

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

Common stock outstanding:

Pacific Enterprises	Wholly owned by Sempra Energy
Southern California Gas Company	Wholly owned by Pacific Enterprises

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INFORMATION REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report contains statements that are not historical fact and constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The words "estimates," "believes," "expects," "anticipates," "plans," "intends," "may," "could," "would" and "should" or similar expressions, or discussions of strategy or of plans are intended to identify forward-looking statements. Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions. Future results may differ materially from those expressed in these forward-looking statements.

Forward-looking statements are necessarily based upon various assumptions involving judgments with respect to the future and other risks, including, among others, local, regional and national economic, competitive, political, legislative and regulatory conditions and developments; actions by the California Public Utilities Commission, the California State Legislature, the Federal Energy Regulatory Commission and other regulatory bodies in the United States; capital markets conditions, inflation rates, interest rates and exchange rates; energy and trading markets, including the timing and extent of changes in commodity prices; the availability of natural gas and liquefied natural gas; weather conditions and conservation efforts; war and terrorist attacks; business, regulatory, environmental and legal decisions and requirements; the status of deregulation of retail natural gas and electricity delivery; the timing and success of business development efforts; the resolution of litigation; and other uncertainties, all of which are difficult to predict and many of which are beyond the control of the companies. Readers are cautioned not to rely unduly on any forward-looking statements and are urged to review and consider carefully the risks, uncertainties and other factors which affect the companies' business described in this report and other reports filed by the companies from time to time with the Securities and Exchange Commission.

PART I. FINANCIAL INFORMATION
ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

PACIFIC ENTERPRISES AND SUBSIDIARIES
STATEMENTS OF CONSOLIDATED INCOME

	Three months ended		Six months ended	
	June 30,		June 30,	
(Dollars in millions)	2008	2007	2008	2007
		(unaudited)		
Operating revenues	$ 1,143	$ 981	$ 2,699	$ 2,349
Operating expenses				
Cost of natural gas	673	529	1,760	1,441
Other operating expenses	265	249	515	492
Depreciation	71	70	142	139
Franchise fees and other taxes	32	29	71	65
Total operating expenses	1,041	877	2,488	2,137
Operating income	102	104	211	212
Other expense, net	--	(1)	--	(3)
Interest income	6	13	13	25
Interest expense	(15)	(19)	(32)	(38)
Income before income taxes	93	97	192	196
Income tax expense	36	41	77	82
Net income	57	56	115	114
Preferred dividend requirements	1	1	2	2
Earnings applicable to common shares	$ 56	$ 55	$ 113	$ 112

See Notes to Condensed Consolidated Financial Statements.

PACIFIC ENTERPRISES AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(Dollars in millions)	June 30, 2008 (unaudited)	December 31, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	$ 135	$ 59
Accounts receivable - trade	510	671
Accounts receivable - other	68	22
Due from unconsolidated affiliates	204	5
Income taxes receivable	86	37
Deferred income taxes	29	33
Inventories	45	98
Other regulatory assets	27	40
Other	49	23
Total current assets	1,153	988
Other assets:		
Due from unconsolidated affiliates	459	457
Other regulatory assets	114	100
Pension plan assets in excess of benefit obligations	45	62
Sundry	38	39
Total other assets	656	658
Property, plant and equipment:		
Property, plant and equipment	8,624	8,448
Less accumulated depreciation and amortization	(3,379)	(3,292)
Property, plant and equipment, net	5,245	5,156
Total assets	$ 7,054	$ 6,802

See Notes to Condensed Consolidated Financial Statements.

PACIFIC ENTERPRISES AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(Dollars in millions)	June 30, 2008 (unaudited)	December 31, 2007
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable - trade	$ 389	$ 300
Accounts payable - other	83	130
Due to unconsolidated affiliates	83	125
Regulatory balancing accounts, net	321	183
Customer deposits	102	90
Accrued compensation and benefits	77	87
Other	242	223
Total current liabilities	1,297	1,138
Long-term debt	1,113	1,113
Deferred credits and other liabilities:		
Customer advances for construction	125	123
Pension and other postretirement benefit obligations, net of plan assets	58	58
Deferred income taxes	121	102
Deferred investment tax credits	32	33
Regulatory liabilities arising from removal obligations	1,194	1,187
Regulatory liabilities arising from pension and other postretirement benefit obligations	18	34
Asset retirement obligations	579	562
Deferred taxes refundable in rates	231	231
Preferred stock of subsidiary	20	20
Deferred credits and other	287	285
Total deferred credits and other liabilities	2,665	2,635

Commitments and contingencies (Note 6)

Shareholders equity:		
Preferred stock	80	80
Common stock (600 million shares authorized; 84 million shares outstanding; no par value)	1,462	1,462
Retained earnings	441	378
Accumulated other comprehensive income (loss)	(4)	(4)
Total shareholders' equity	1,979	1,916
Total liabilities and shareholders' equity	$ 7,054	$ 6,802

See Notes to Condensed Consolidated Financial Statements.

PACIFIC ENTERPRISES AND SUBSIDIARIES
CONDENSED STATEMENTS OF CONSOLIDATED CASH FLOWS

	Six months ended June 30,	
(Dollars in millions)	2008	2007
	(unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 115	$ 114
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	142	139
Deferred income taxes and investment tax credits	21	10
Other	1	1
Net change in other working capital components	315	408
Changes in other assets	5	6
Changes in other liabilities	(20)	(13)
Net cash provided by operating activities	579	665
CASH FLOWS FROM INVESTING ACTIVITIES		
Expenditures for property, plant and equipment	(242)	(191)
Increase in loans to affiliates, net	(59)	(105)
Other	--	(4)
Net cash used in investing activities	(301)	(300)
CASH FLOWS FROM FINANCING ACTIVITIES		
Common dividends paid	(200)	(100)
Preferred dividends paid	(2)	(2)
Net cash used in financing activities	(202)	(102)
Increase in cash and cash equivalents	76	263
Cash and cash equivalents, January 1	59	211
Cash and cash equivalents, June 30	$ 135	$ 474
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Interest payments, net of amounts capitalized	$ 31	$ 36

Income tax payments, net of refunds	$	104	$	26
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING ACTIVITY				
Decrease in accounts payable from investments in property, plant and equipment	$	(31)	$	(12)

See Notes to Condensed Consolidated Financial Statements.

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SOUTHERN CALIFORNIA GAS COMPANY AND SUBSIDIARIES
STATEMENTS OF CONSOLIDATED INCOME

	Three months ended June 30,		Six months ended June 30,	
(Dollars in millions)	2008	2007	2008	2007
	(unaudited)			
Operating revenues	$ 1,143	$ 981	$ 2,699	$ 2,349
Operating expenses				
Cost of natural gas	673	529	1,760	1,441
Other operating expenses	266	248	515	491
Depreciation	71	70	142	139
Franchise fees and other taxes	32	29	71	65
Total operating expenses	1,042	876	2,488	2,136
Operating income	101	105	211	213
Other income (expense), net	2	(2)	2	(4)
Interest income	4	8	7	14
Interest expense	(14)	(17)	(30)	(35)
Income before income taxes	93	94	190	188
Income tax expense	36	39	76	78
Net income	57	55	114	110
Preferred dividend requirements	1	1	1	1
Earnings applicable to common shares	$ 56	$ 54	$ 113	$ 109

See Notes to Condensed Consolidated Financial Statements.

SOUTHERN CALIFORNIA GAS COMPANY AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(Dollars in millions)	June 30, 2008 (unaudited)	December 31, 2007
ASSETS		
Current assets:		
Cash and cash equivalents	$ 135	$ 59
Accounts receivable - trade	510	671
Accounts receivable - other	68	22
Due from unconsolidated affiliates	198	129
Income taxes receivable	24	--
Deferred income taxes	29	33
Inventories	45	98
Other regulatory assets	27	40
Other	49	22
Total current assets	1,085	1,074
Other assets:		
Other regulatory assets	114	100
Pension plan assets in excess of benefit obligations	45	62
Sundry	15	16
Total other assets	174	178
Property, plant and equipment:		
Property, plant and equipment	8,622	8,446
Less accumulated depreciation and amortization	(3,379)	(3,292)
Property, plant and equipment, net	5,243	5,154
Total assets	$ 6,502	$ 6,406

See Notes to Condensed Consolidated Financial Statements.

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SOUTHERN CALIFORNIA GAS COMPANY AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

(Dollars in millions)	June 30, 2008 (unaudited)	December 31, 2007
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable - trade	$ 389	$ 300
Accounts payable - other	83	130
Due to unconsolidated affiliates	--	171
Income taxes payable	--	26
Regulatory balancing accounts, net	321	183
Customer deposits	102	90
Accrued compensation and benefits	77	87
Other	241	223
Total current liabilities	1,213	1,210
Long-term debt	1,113	1,113
Deferred credits and other liabilities:		
Customer advances for construction	125	123
Pension and other postretirement benefit obligations, net of plan assets	58	58
Deferred income taxes	135	117
Deferred investment tax credits	32	33
Regulatory liabilities arising from removal obligations	1,194	1,187
Regulatory liabilities arising from pension and other postretirement benefit obligations	18	34
Asset retirement obligations	579	562
Deferred taxes refundable in rates	231	231
Deferred credits and other	271	268
Total deferred credits and other liabilities	2,643	2,613

Commitments and contingencies (Note 6)

Shareholders equity:		
Preferred stock	22	22
Common stock (100 million shares authorized; 91 million shares outstanding; no par value)	866	866
Retained earnings	649	586
Accumulated other comprehensive income (loss)	(4)	(4)
Total shareholders' equity	1,533	1,470
Total liabilities and shareholders' equity	$ 6,502	$ 6,406

See Notes to Condensed Consolidated Financial Statements.

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SOUTHERN CALIFORNIA GAS COMPANY AND SUBSIDIARIES
CONDENSED STATEMENTS OF CONSOLIDATED CASH FLOWS

	Six months ended June 30,	
(Dollars in millions)	2008	2007
	(unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 114	$ 110
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	142	139
Deferred income taxes and investment tax credits	21	11
Other	1	1
Net change in other working capital components	313	401
Changes in other assets	5	6
Changes in other liabilities	(20)	(10)
Net cash provided by operating activities	576	658
CASH FLOWS FROM INVESTING ACTIVITIES		
Expenditures for property, plant and equipment	(242)	(191)
Increase in loans to affiliates, net	(57)	(105)
Other	--	2
Net cash used in investing activities	(299)	(294)
CASH FLOWS FROM FINANCING ACTIVITIES		
Common dividends paid	(200)	(100)
Preferred dividends paid	(1)	(1)
Net cash used in financing activities	(201)	(101)
Increase in cash and cash equivalents	76	263
Cash and cash equivalents, January 1	59	211
Cash and cash equivalents, June 30	$ 135	$ 474
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Interest payments, net of amounts capitalized	$ 29	$ 33

Income tax payments, net of refunds	$	104	$	26
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING ACTIVITY				
Decrease in accounts payable from investments in property, plant and equipment	$	(31)	$	(12)

See Notes to Condensed Consolidated Financial Statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. GENERAL

Principles of Consolidation

This Quarterly Report on Form 10-Q is that of Pacific Enterprises (PE) and Southern California Gas Company (SoCalGas) (collectively referred to as the company or the companies). PE s common stock is wholly owned by Sempra Energy, a California-based Fortune 500 holding company, and PE owns all of the common stock of SoCalGas. The accompanying financial statements are, in one case, the Condensed Consolidated Financial Statements of PE and its subsidiary, SoCalGas, and, in the other case, the Condensed Consolidated Financial Statements of SoCalGas and its subsidiaries, which comprise less than one percent of SoCalGas' consolidated financial position and results of operations.

Sempra Energy also indirectly owns all of the common stock of San Diego Gas & Electric Company (SDG&E). SoCalGas and SDG&E are collectively referred to as the Sempra Utilities.

Basis of Presentation

The Condensed Consolidated Financial Statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) and in accordance with the interim-period-reporting requirements of Form 10-Q. Results of operations for interim periods are not necessarily indicative of results for the entire year. In the opinion of management, the accompanying statements reflect all adjustments necessary for a fair presentation. These adjustments are only of a normal, recurring nature.

Information in this Quarterly Report should be read in conjunction with the company s Annual Report on Form 10-K for the year ended December 31, 2007 (the Annual Report) and its Quarterly Report on Form 10-Q for the quarter ended March 31, 2008.

The companies' significant accounting policies are described in Note 1 of the Notes to Consolidated Financial Statements in the Annual Report. The same accounting policies are followed for interim reporting purposes, except for the adoption of new accounting standards as discussed in Note 2.

SoCalGas accounts for the economic effects of regulation on utility operations in accordance with Statement of Financial Accounting Standards (SFAS) 71*, Accounting for the Effects of Certain Types of Regulation.*

As discussed in Note 5, beginning April 1, 2008, the SDG&E and SoCalGas core natural gas supply portfolios were combined and are managed by SoCalGas. SoCalGas will procure natural gas for SDG&E s core customers. This core gas procurement function is considered a shared service, therefore amounts related to SDG&E are not included in the income statement.

NOTE 2. NEW ACCOUNTING STANDARDS

Recently issued pronouncements that have had or may have a significant effect on the company's financial statements are described below.

SFAS 161, "Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133" (SFAS 161): SFAS 161 expands the disclosure requirements in Financial

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Accounting Standards Board (FASB) Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133). SFAS 161 requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The company is in the process of evaluating the effect of this statement on its financial statement disclosures.

FASB Staff Position (FSP) FIN 39-1, "Amendment of FASB Interpretation No. 39" (FSP FIN 39-1): FSP FIN 39-1 amends certain paragraphs of FASB Interpretation No. 39, *Offsetting of Amounts Related to Certain Contracts*, to permit a reporting entity to offset fair value amounts recognized for the right to reclaim or the obligation to return cash collateral against fair value amounts recognized for derivative instruments executed with the same counterparty under the same master netting arrangement. FSP FIN 39-1 is effective for fiscal years beginning after November 15, 2007. The company adopted FSP FIN 39-1 effective January 1, 2008. The company applied FSP FIN 39-1 as a change in accounting principle through retrospective application. Each consolidated balance sheet herein reflects the offsetting of net derivative positions with fair value amounts for cash collateral with the same counterparty when management believes a legal right of setoff exists. The adoption of FSP FIN 39-1 did not have a material impact on the company's financial statements. Additional disclosure is provided in Note 4.

NOTE 3. OTHER FINANCIAL DATA

Pension and Other Postretirement Benefits

The following tables provide the components of benefit costs:

	Pension Benefits Three months ended June 30,		Other Postretirement Benefits Three months ended June 30,	
(Dollars in millions)	2008	2007	2008	2007
Service cost	$ 10	$ 9	$ 5	$ 6
Interest cost	24	24	10	12
Expected return on assets	(25)	(25)	(11)	(10)
Amortization of:				
Prior service credit	--	--	(1)	(1)

Actuarial loss		--		1		--		1
Regulatory adjustment		(9)		(8)		1		--
Total net periodic benefit cost	$	--	$	1	$	4	$	8

	Pension Benefits Six months ended June 30,				Other Postretirement Benefits Six months ended June 30,			
(Dollars in millions)	2008		2007		2008		2007	
Service cost	$	20	$	20	$	9	$	11
Interest cost		49		48		21		23
Expected return on assets		(51)		(51)		(22)		(20)
Amortization of:								
Prior service cost (credit)		1		1		(2)		(3)
Actuarial loss		--		1		--		3
Regulatory adjustment		(18)		(18)		3		2
Total net periodic benefit cost	$	1	$	1	$	9	$	16

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The company expects to contribute $2 million to its pension plan and $19 million to its other postretirement benefit plans in 2008. For the three and six months ended June 30, 2008, the company made contributions of $4 million and $9 million to its other postretirement benefit plans, respectively, and a negligible amount of contributions to the pension plan.

Capitalized Interest

The company recorded $1 million and $2 million of capitalized interest for the three months and six months ended June 30, 2008, respectively, including primarily the debt-related portion of allowance for funds used during construction. The company recorded a negligible amount and $1 million of capitalized interest for the three months and six months ended June 30, 2007, respectively, including primarily the debt-related portion of allowance for funds used during construction.

Comprehensive Income

The following is a reconciliation of net income to comprehensive income for PE:

	Three months ended June 30,		Six months ended June 30,	
(Dollars in millions)	2008	2007	2008	2007
Net income	$ 57	$ 56	$ 115	$ 114
Financial instruments*	5	--	--	--
Comprehensive income	$ 62	$ 56	$ 115	$ 114

* Net of tax expense of $4 million for the three months ended June 30, 2008.

The following is a reconciliation of net income to comprehensive income for SoCalGas:

	Three months ended June 30,		Six months ended June 30,	
(Dollars in millions)	2008	2007	2008	2007
Net income	$ 57	$ 55	$ 114	$ 110

Financial instruments*	5	--	--	--
Comprehensive income	$ 62	$ 55	$ 114	$ 110

* Net of tax expense of $4 million for the three months ended June 30, 2008.

Other Expense, Net

Other Expense, Net consists of the following:

	Three months ended June 30,		Six months ended June 30,	
(Dollars in millions)	2008	2007	2008	2007
Regulatory interest, net	$ (1)	$ (3)	$ (2)	$ (5)
Allowance for equity funds used during construction	2	1	4	2
Sundry, net	1	--	--	(1)
Total at SoCalGas	2	(2)	2	(4)
Additional at Pacific Enterprises:				
Preferred dividends of subsidiary	(1)	(1)	(1)	(1)
Sundry, net	(1)	2	(1)	2
Total	$ --	$ (1)	$ --	$ (3)

NOTE 4. FINANCIAL INSTRUMENTS

The company periodically uses commodity derivative instruments and interest-rate swap agreements to moderate its exposure to commodity price changes and interest-rate changes and to lower its overall cost of borrowing.

Fair Value Hedges

As of June 30, 2008 and December 31, 2007, the company has a fair value hedge for a notional amount of debt totaling $150 million. The fair value hedge balance was an asset of $2 million at June 30, 2008 and December 31, 2007, respectively. The hedge expires in 2011.

Market value adjustments since inception of the hedge were recorded as an increase in fixed-price contracts and other derivatives (in noncurrent assets as Sundry or in Deferred Credits and Other) and as a corresponding increase or decrease in Long-Term Debt without affecting net income or other comprehensive income. There has been no hedge ineffectiveness on this swap.

Cash Flow Hedges

As of June 30, 2008 and December 31, 2007, the company had established a cash flow interest-rate swap hedge for a notional amount of debt totaling $183 million. The swap expires in 2038. There has been no hedge ineffectiveness on this swap.

Natural Gas Contracts

The use of derivative instruments is subject to certain limitations imposed by company policy and regulatory requirements. These instruments enable the company to estimate with greater certainty the effective prices to be received by the company and the prices to be charged to its customers. The company records realized gains or losses on derivative instruments associated with transactions for natural gas contracts in Cost of Natural Gas on the Statements of Consolidated Income. On the Consolidated Balance Sheets, the company records corresponding regulatory assets and liabilities related to unrealized gains and losses from these derivative instruments to the extent derivative gains and losses associated with these derivative instruments will be payable or recoverable in future rates.

Adoption of FSP FIN 39-1

The company adopted FSP FIN 39-1 effective January 1, 2008, which requires retrospective application. Each Consolidated Balance Sheet herein reflects the offsetting of net derivative positions with fair value amounts for cash collateral with the same counterparty when management believes a legal right of setoff exists. As of June 30, 2008 and December 31, 2007, the application of FSP FIN 39-1 had no impact on the Consolidated Balance Sheets. The fair value of cash collateral that was not offset in the Consolidated Balance Sheets as of June 30, 2008 and December 31, 2007 was $6 million and $7 million, respectively. The fair value of commodity derivative assets and liabilities as of June 30, 2008 and December 31, 2007, determined in accordance with the company's netting policy, is presented below.

Fair Value Hierarchy

The company s valuation techniques used to measure fair value and the definition of the three levels of the fair value hierarchy, as defined in SFAS 157, *Fair Value Measurements* (SFAS 157), are discussed in Note 7 of the Notes to Consolidated Financial Statements in the Annual Report.

The following tables set forth by level within the fair value hierarchy the company's financial assets and liabilities that were accounted for at fair value on a recurring basis as of June 30, 2008 and December 31, 2007. As required by SFAS 157, financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The company's assessment of the significance of a particular input to the fair value measurement requires judgment, and may affect the valuation of fair value assets and liabilities and their placement within the fair value hierarchy levels.

Recurring Fair Value Measures		At fair value as of June 30, 2008
(Dollars in millions)	Level 1	Level 2