SOUTH JERSEY INDUSTRIES INC
Form 10-K
February 28, 2013
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549
FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2012

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ____________to ______________.
Commission File Number 1-6364
SOUTH JERSEY INDUSTRIES, INC.
(Exact name of registrant as specified in its charter)

New Jersey (State of incorporation)	22-1901645 (IRS employer identification no.)
1 South Jersey Plaza, Folsom, New Jersey 08037	(609) 561-9000
(Address of principal executive offices, including zip code)	(Registrant's telephone number, including area code)

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

Common Stock - $1.25 par value per share	New York Stock Exchange
(Title of each class)	(Name of exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act: Yes x No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Act: Yes o No x

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

The aggregate market value of voting stock held by non-affiliates of the registrant as of June 30, 2012 was $1,544,272,903. As of February 15, 2013, there were 31,744,916 shares of the registrant's common stock outstanding.

Documents Incorporated by Reference:
In Part I of Form 10-K: None
In Part II of Form 10-K: None
In Part III of Form 10-K: Portions of the registrant's proxy statement filed within 120 days of the close of the registrant's fiscal year in connection with the registrant's 2013 annual meeting of shareholders are incorporated by reference into Part III of this Form 10-K.

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Forward Looking Statements

Certain statements contained in this Annual Report on form 10-K may qualify as “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements other than statements of historical fact included in this Report should be considered forward-looking statements made in good faith by South Jersey Industries (SJI or the Company) and are intended to qualify for the safe harbor from liability established by the Private Securities Litigation Reform Act of 1995. When used in this Report, or any other of the Company's documents or oral presentations, words such as “anticipate,” “believe,” “expect,” “estimate,” “forecast,” “goal,” “intend,” “objective,” “plan,” “project,” “seek,” “strategy” and similar expressions are intended to identify forward-looking statements. Such forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those expressed or implied in the statements. These risks and uncertainties include, but are not limited to the risks set forth under “Risk Factors” in Part I, Item 1A of this Annual Report on Form 10-K and elsewhere throughout this Report. These cautionary statements should not be construed by you to be exhaustive and they are made only as of the date of this Report. While the Company believes these forward-looking statements to be reasonable, there can be no assurance that they will approximate actual experience or that the expectations derived from them will be realized. Further, SJI undertakes no obligation to update or revise any of its forward-looking statements whether as a result of new information, future events or otherwise.

Available Information

The Company's Internet address is www.sjindustries.com. We make available free of charge on or through our website SJI's annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission (SEC). The SEC maintains an Internet site that contains these reports at http://www.sec.gov. Also, copies of SJI's annual report will be made available, free of charge, upon written request. The content on any web site referred to in this filing is not incorporated by reference into this filing unless expressly noted otherwise.

Units of Measurement

For Natural Gas:	
1 Bcf	= One billion cubic feet
1dt	= One decatherm
1 MMdts	= One million decatherms
dts/d	= Decatherms per day
MDWQ	= Maximum daily withdrawal quantity
For Electric:	
1 MMmwh	= One million megawatt hours
1 mwh	= One megawatt hour

PART I

Item 1. Business
Description of Business

The registrant, South Jersey Industries, Inc. (SJI), a New Jersey corporation, was formed in 1969 for the purpose of owning and holding all of the outstanding common stock of South Jersey Gas Company, a public utility, and acquiring and developing non-utility lines of business.

SJI currently provides a variety of energy related products and services primarily through the following subsidiaries:

- South Jersey Gas Company (SJG) is a regulated natural gas utility. SJG distributes natural gas in the seven southernmost counties of New Jersey.

- South Jersey Energy Company (SJE) acquires and markets natural gas and electricity to retail end users and provides total energy management services to commercial and industrial customers.

- Marina Energy LLC (Marina) develops and operates on-site energy-related projects.

- South Jersey Resources Group, LLC (SJRG) markets natural gas storage, commodity and transportation assets on a wholesale basis in the mid-Atlantic, Appalachian and southern states.

- South Jersey Energy Service Plus, LLC (SJESP) services residential and small commercial HVAC systems, provides plumbing services and services appliances under warranty via a subcontractor arrangement as well as on a time and materials basis.

- South Jersey Exploration, LLC (SJEX) owns oil, gas and mineral rights in the Marcellus Shale region of Pennsylvania.

Additional Information on the nature of our business can be found in “Management's Discussion and Analysis of Financial Condition and Results of Operations,” under Item 7 of this report.

Financial Information About Reportable Segments

Information regarding Reportable Segments is incorporated by reference to Note 8 of the consolidated financial statements included under Item 8 of this report.

Sources and Availability of Raw Materials

South Jersey Gas Company

Transportation and Storage Agreements

SJG has direct connections to the interstate pipeline systems of both Transcontinental Gas Pipe Line Company, LLC (Transco) and Columbia Gas Transmission, LLC (Columbia). During 2012, SJG purchased and had delivered approximately 33.0 million decatherms (MMdts) of natural gas for distribution to both on-system and off-system customers. Of this total, 18.8 MMdts were transported on the Transco pipeline system while 14.2 MMdts were transported on the Columbia pipeline system. Moreover, during 2012 third-party suppliers delivered 32.2 MMdts to SJG's system on behalf of end use customers behind our city gate stations. SJG also secures other long term services from one additional pipeline upstream of the Transco and Columbia systems. This upstream pipeline is owned by Dominion Transmission, Inc. (Dominion). Services provided by Dominion are utilized to deliver gas into either the Transco or Columbia systems for ultimate delivery to SJG. Services provided by all of the above-mentioned pipelines are subject to the jurisdiction of the Federal Energy Regulatory Commission (FERC). Unless otherwise indicated, our intentions are to renew or extend these service agreements before they expire.

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Transco:

Transco is SJG's largest supplier of long-term gas transmission services which includes both year-round and seasonal firm transportation (FT) service arrangements. When combined, these FT services enable SJG to purchase gas from third parties and have delivered to its city gate stations by Transco a total of 297,958 dts per day (dts/d). Of this total, 133,917 dts/d is long-haul FT (where gas can be transported from the production areas of the Southwest to the market areas of the Northeast) while 164,041 dts/d is market area FT. The terms of SJG's year-round agreements extend for various periods through 2025. The terms of its seasonal agreements vary in length with the longest extending into 2013.

Of the 297,958 dts/d of Transco services mentioned above, SJG has released a total of 39,800 dts/d of its long-haul FT and 42,998 dts/d of its market area FT service. These releases were made in association with SJG's Conservation Incentive Program (CIP) discussed further under Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations. In addition, SJG released 90,000 dts/d of market area FT service to SJRG as part of an Asset Management Agreement discussed further in this section under “Gas Supplies”.

SJG currently has six long-term gas storage service agreements with Transco that, when combined, are capable of storing approximately 5.0 MMdts. Through these agreements, SJG can inject gas into market and production area storages during periods of low demand and extract gas at a Maximum Daily Withdrawal Quantity (MDWQ) of up to 107,407 dts during periods of high demand. The longest term of these storage service agreements extends through October 2019.

Dominion:

SJG subscribes to a firm storage service from Dominion, under its Rate Schedule GSS. This storage has a MDWQ of 10,000 dts during the period between November 16 and March 31 of each winter season, with an associated total storage capacity of 423,000 dts. Gas withdrawn from Dominion GSS storage is delivered through both the Dominion and Transco (Leidy Line) pipeline systems for delivery to SJG service territory. The primary term of this agreement extends through March 31, 2015.

Columbia:

SJG subscribes to three firm transportation agreements with Columbia which provides for 54,022 dts/d of firm deliverability with 45,022 dts/d of this deliverability extending through October 31, 2019. The remaining 9,000 dts per day had a primary term of one year which extended from November 1, 2011 through October 31, 2012. The agreement was subject to pre-granted abandonment upon its termination, with SJG having the right of first refusal to extend the agreement. By way of an agreement dated July 9, 2012, this service was extended through October 31, 2013. SJG had previously released 14,714 dts/d of this amount to SJRG in conjunction with its CIP thereby reducing the combined availability of firm transportation on the Columbia system to 39,308 dts/d.

SJG also subscribes to a firm storage service with Columbia under its Rate Schedule FSS along with an associated firm transportation service under Rate Schedule SST, each of which extends through October 31, 2019. SJG has a total FSS MDWQ of 52,891 dts and a related 3,473,022 dts of storage capacity. SJG released to SJRG 19,029 dts of its FSS MDWQ along with 1,249,485 dts of its FSS storage capacity. Additionally, SJG also released to SJRG 19,029 dts/d of its Columbia SST transportation service. Both releases made by SJG were in connection with its CIP and extend through September 30, 2014.

Gas Supplies

SJG has an Asset Management Agreement (AMA) with SJRG that extends through November 30, 2013. Under this agreement SJG has released to SJRG its firm transportation rights equal to 90,000 dts/d of transportation capacity on Transco. SJRG will manage this capacity and provide SJG with up to 90,000 dts/d of firm deliverability in the summer season and up to 90,000 dts/d of interruptible deliverability in the winter season. SJRG will seek to optimize the capacity released under this AMA and will pay SJG a fee based on a sharing formula in the agreement.

During 2012, SJG entered into an AMA with a gas marketer which extends through October 31, 2013. Under this agreement SJG has released to the marketer its firm transportation rights equal to 10,000 dts/d of transportation capacity on Transco. The marketer will manage this capacity and provide SJG with up to 10,000 dts/d of firm deliverability each day through October 31, 2013. The marketer will seek to optimize the capacity released to it under this AMA and has paid SJG a one time Asset Management Fee in consideration for same.

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Also during 2012, SJG entered into an AMA with a gas marketer which extends through March 31, 2013. Under this agreement SJG has released its storage capacity and deliverability held on the Dominion pipeline system to the marketer equal to 423,000 dts of storage capacity and 10,000 dts/d of deliverability on both the Dominion and Transco Leidy Line systems. The marketer will manage this capacity and provide SJG with the right to call on up to 10,000 dts/d into Transco's Leidy Line for the period from November 1, 2012 through March 31, 2013. The marketer will seek to optimize the storage capacity released to it under this AMA and has paid SJG a one time Asset Management Fee in consideration for same.

In 2011, SJG entered into a long-term gas purchase agreement with a gas producer, the primary term of which extends through October 31, 2019. The maximum daily quantities (MDQ) available for purchase under this agreement initially starts at 6,250 dts/d and ratchets up to a MDQ of 25,000 dts/d. Gas purchased from this producer will be sourced in the Appalachian supply areas and delivered into the Columbia pipeline system for delivery to SJG.

Due to increased liquidity in the market place, all other gas supply agreements with third party suppliers are short-term agreements and SJG uses financial contracts secured through SJRG to hedge against forward price risk. Short-term agreements typically extend between one day and several months in duration.

Supplemental Gas Supplies

During 2012, SJG entered into two seasonal Liquefied Natural Gas (LNG) purchase agreements with a third party supplier. The term of the first agreement, which is being used during the 2012-2013 winter season to refill SJG's storage tank, extends through March 31, 2013, and has an associated contract quantity of 250,000 dts. The second agreement was acquired to replenish LNG in storage during the 2013 summer season. This agreement extends from April 1, 2013 through October 31, 2013 and also provides SJG with up to 250,000 dts of LNG.

SJG operates peaking facilities which can store and vaporize LNG for injection into its distribution system. SJG's LNG facility has a storage capacity equivalent to 434,300 dts of natural gas and has an installed capacity to vaporize up to 118,250 dts of LNG per day for injection into its distribution system.

Peak-Day Supply

SJG plans for a winter season peak-day demand on the basis of an average daily temperature of 2 degrees Fahrenheit (F). Gas demand on such a design day for the 2012-2013 winter season is estimated to be 476,462 dts. SJG projects that it has adequate supplies and interstate pipeline entitlements to meet its design requirements. SJG experienced its highest peak-day demand for calendar year 2012 of 389,376 dts on January 15th, while experiencing an average temperature of 21.5 degrees F that day.

Natural Gas Prices

SJG's average cost of natural gas purchased and delivered in 2012, 2011 and 2010, including demand charges, was $4.73 per dt, $6.11 per dt and $6.64 per dt, respectively.

South Jersey Energy Company

Transportation and Storage Agreements - Natural Gas

Access to gas suppliers and cost of gas are significant to the operations of SJE. No material part of the business of SJE is dependent upon a single customer or a few customers. SJE purchases delivered gas only, primarily from SJRG.

Consequently, SJE maintains no transportation or storage agreements.

Electric Supply

Due to the liquidity in the market, SJE primarily purchases delivered electric in the day-ahead and real time markets through regional transmission organizations and consequently does not own or operate any generation or transmission assets.

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South Jersey Resources Group

Transportation and Storage Agreements

National Fuel Gas Supply Corporation:

SJRG has multiple storage service agreements with National Fuel Gas Supply Corporation (National Fuel). Two contracts totaling 2,581,420 dts of capacity have evergreen rights that extend year to year. One additional contract covering 224,576 dts of storage capacity extends through March 31, 2018 while a final contract covering 150,040 dts of capacity expires March 31, 2023.

SJRG holds long term firm transportation agreements with National Fuel associated with the above-mentioned agreements. Under these agreements, National Fuel will provide SJRG with a maximum daily injection transportation quantity of 16,947 dts/d with primary receipt points from Tennessee Gas Pipeline for delivery into storage, and 25,661 dts/d of maximum daily withdrawal transportation quantity with a primary receipt point of storage and a primary delivery point of Transcontinental Gas Pipeline.

Transcontinental Gas Pipeline:

SJRG has a storage agreement with Transco for storage service at Transco's WSS facility which expires in October 2017. Under this evergreen contract, up to 24,479 dts/d may be injected and up to 46,380 dts/d may be withdrawn. Total storage capacity on the agreement is 4,406,135 dts.

SJRG also has two firm transportation agreements with Transco which expire September 30, 2013. Under these contracts, Transco will provide SJRG with receipts at various production points in Texas and Louisiana and deliveries in New Jersey totaling 19,900 dts/d. This service was released to SJRG by SJG as discussed above.

SJRG also holds a firm transportation agreement with Transco which expires March 31, 2043. Under this agreement, Transco will provide SJRG with 10,000 dts/d of deliveries to New York and receipts at Leidy, PA.

Dominion Gas Transmission:

SJRG has a firm transportation agreement with Dominion which expires October 31, 2022. Under this agreement, Dominion will provide SJRG with 5,000 dts/d of deliveries to Leidy, Pennsylvania and receipts at Lebanon, Ohio.

SJRG also has a firm transportation agreement with Dominion related to SJRG's Transco SS-1 storage. Under this contract, Dominion will provide receipts at Leidy, Pennsylvania and deliveries to storage in the amount of 17,432 dts/d. This service was released to SJRG by SJG in 2008.

Columbia Gas Transmission:

SJRG holds a firm transportation agreement with Columbia. Under this evergreen agreement, Columbia provides receipts at Leach, Kentucky and deliveries of 14,714 dts/d to New Jersey. In addition, SJRG has 10,000 dts/d of Columbia capacity from New York to Maryland expiring October 31, 2018. These services with Columbia were released to SJRG by SJG as discussed above.

SJRG holds a storage agreement with Columbia for service under Columbia's FSS rate schedule. Under this evergreen agreement, Columbia will provide SJRG with storage capacity of 1,249,485 dts. Under this agreement, 19,029 dts/d may be withdrawn from storage and 9,996 dts/d may be injected.

SJRG holds firm transportation related to the above mentioned storage agreement which provides for receipts at storage and deliveries to New Jersey of 19,029 dts/d. Under this evergreen contract, these services with Columbia were released to SJRG by SJG.

Columbia Gulf Transmission:

SJRG holds a firm transportation agreement with Columbia Gulf which expires October 31, 2019. Under this evergreen agreement, Columbia provides receipts in Louisiana with deliveries at Leach, Kentucky in the amount of 15,000 dts/d.

Tennessee Gas Transmission:

SJRG holds three firm transportation agreements with Tennessee Gas Pipeline. Two contracts, one totaling 30,000 Dth and the other totaling 28,400 Dth, have deliveries to various points in Pennsylvania and receipts in northeastern Pennsylvania and extend through October 31, 2016. The final contract is for 60,000 Dth with various deliveries and receipts in Louisiana, and extends through March 31, 2014.

Gas Supplies

SJRG has entered into several long-term natural gas supply agreements to purchase a minimum of 465,700 dts/d and up to 700,000 dts/d, depending upon production levels, for terms ranging from three to ten years at index based prices. Further, SJG released 90,000 dts/d of market area FT service to SJRG as part of an AMA agreement discussed above.

Patents and Franchises

South Jersey Gas Company

SJG holds nonexclusive franchises granted by municipalities in the seven-county area of southern New Jersey that it serves. No other natural gas public utility presently serves the territory covered by SJG's franchises. Otherwise, patents, trademarks, licenses, franchises and concessions are not material to the business of SJG.

Seasonal Aspects

South Jersey Gas Company

SJG experiences seasonal fluctuations in sales when selling natural gas for heating purposes. SJG meets this seasonal fluctuation in demand from its firm customers by buying and storing gas during the summer months, and by drawing from storage and purchasing supplemental supplies during the heating season. As a result of this seasonality, SJG's revenues and net income are significantly higher during the first and fourth quarters than during the second and third quarters of the year.

Non-Utility Companies

Among SJI's non-utility activities, wholesale and retail gas marketing have seasonal patterns similar to SJG's. Activities such as energy services and energy project development do not follow seasonal patterns. Other activities such as retail electric marketing and appliance service can have seasonal earnings patterns that are different from the utility. While growth in the earnings contributions from nonutility operations has improved SJI's second and third quarter net income levels, the first and fourth quarters remain the periods where most of SJI's revenue and net income is produced.

Working Capital Practices

Reference is made to “Liquidity and Capital Resources” included in Item 7, “Management's Discussion and Analysis of Financial Condition and Results of Operations,” of this report.

Customers

No material part of the Company's business is dependent upon a single customer or a few customers, the loss of which would have a material adverse effect on SJI performance on a consolidated basis.

Backlog

Backlog is not material to an understanding of SJI's business or that of any of its subsidiaries.

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Government Contracts

No material portion of the business of SJI or any of its subsidiaries is subject to renegotiation of profits or termination of contracts or subcontracts at the election of any government.

Competition

Information on competition for SJI and its subsidiaries can be found in Item 7, “Management's Discussion and Analysis of Financial Condition and Results of Operations,” of this report.

Research

During the last three fiscal years, neither SJI nor any of its subsidiaries engaged in research activities to any material extent.

Environmental Matters

Information on environmental matters for SJI and its subsidiaries can be found in Note 15 of the consolidated financial statements included under Item 8 of this report.

Employees

SJI and its subsidiaries had a total of approximately 700 employees as of December 31, 2012. Of that total, approximately 320 employees are unionized. The Company has collective bargaining agreements with two unions that represent these employees: the International Brotherhood of Electrical Workers (IBEW) Local 1293 and the International Association of Machinists and Aerospace Workers (IAM) Local 76. SJG employees represented by the IBEW operated under a collective bargaining agreement that was set to expire February 28, 2013, however a new collective bargaining agreement was agreed to and commences on March 1, 2013 and runs through February 28, 2017. SJESP employees represented by the IBEW operate under a collective bargaining agreement that runs through February 28, 2014. The remaining unionized employees represented by the IAM operate under a collective bargaining agreement that expires in August 2014.

Financial Information About Foreign and Domestic Operations and Export Sales

SJI has no foreign operations and export sales have not been a significant part of SJI's business.

Item 1A. Risk Factors

SJI and its subsidiaries operate in an environment that involves risks, many of which are beyond our control. SJI has identified the following risk factors that could cause SJI's operating results and financial condition to be materially adversely affected. In addition, new risks may emerge at any time, and SJI cannot predict those risks or the extent to which they may affect SJI's businesses or financial performance.

- SJI is a holding company and its assets consist primarily of investments in subsidiaries. Should SJI's subsidiaries be unable to pay dividends or make other payments to SJI for financial, regulatory, legal or other reasons, SJI's ability to pay dividends on its common stock could be limited. SJI's stock price could be adversely affected as a result.
- SJI's business activities are concentrated in southern New Jersey. Changes in the economies of southern New Jersey and surrounding regions could negatively impact the growth opportunities available to SJI and the financial condition

of customers and prospects of SJI.

- Changes in the regulatory environment or unfavorable rate regulation at its utility may have an unfavorable impact on SJI's financial performance or condition. SJI's utility business is regulated by the New Jersey Board of Public Utilities which has authority over many of the activities of the business including, but not limited to, the rates it charges to its customers, the amount and type of securities it can issue, the nature of investments it can make, the nature and quality of services it provides, safety standards and other matters. The extent to which the actions of regulatory commissions restrict or delay SJG's ability to earn a reasonable rate of return on invested capital and/or fully recover operating costs may adversely affect its results of operations, financial condition and cash flows.

- SJI may not be able to respond effectively to competition, which may negatively impact SJI's financial performance or condition. Regulatory initiatives may provide or enhance opportunities for competitors that could reduce utility income obtained from existing or prospective customers. Also, competitors in all of SJI's business lines may be able to provide superior or less costly products or services based upon currently available or newly developed technologies.
- Warm weather, high commodity costs, or customer conservation initiatives could result in reduced demand for some of SJI's energy products and services. While SJI's utility currently has a conservation incentive program clause that protects its revenues and gross margin against usage per customer that is lower than a set level, the clause is currently approved as a pilot program through 2013. Should this clause expire without replacement or extension, lower customer energy utilization levels would likely reduce SJI's net income.
- High natural gas prices could cause more of SJI's receivables to be uncollectible. Higher levels of uncollectibles from either residential or commercial customers would negatively impact SJI's income and could result in higher working capital requirements.
- SJI's net income could decrease if it is required to incur additional costs to comply with new governmental safety, health or environmental legislation. SJI is subject to extensive and changing federal and state laws and regulations that impact many aspects of its business; including the storage, transportation and distribution of natural gas, as well as the remediation of environmental contamination at former manufactured gas plant facilities.
- Climate change legislation could impact SJI's financial performance and condition. Climate change is receiving ever increasing attention from scientists and legislators alike. The debate is ongoing as to the extent to which our climate is changing, the potential causes of this change and its future impacts. Some attribute global warming to increased levels of greenhouse gases, which has led to significant legislative and regulatory efforts to limit greenhouse gas emissions. The outcome of federal and state actions to address global climate change could result in a variety of regulatory programs including additional charges to fund energy efficiency activities or other regulatory actions. These actions could affect the demand for natural gas and electricity, result in increased costs to our business and impact the prices we charge our customers. Because natural gas is a fossil fuel with low carbon content, it is possible that future carbon constraints could create additional demands for natural gas, both for production of electricity and direct use in homes and businesses. Any adoption by federal or state governments mandating a substantial reduction in greenhouse gas emissions could have far-reaching and significant impacts on the energy industry. We cannot predict the potential impact of such laws or regulations on our future consolidated financial condition, results of operations or cash flows.
- SJI's wholesale commodity marketing and retail electric businesses are exposed to the risk that counterparties that owe money or energy to SJI will not be able to meet their obligations for operational or financial reasons. SJI could be forced to buy or sell commodity at a loss as a result of such failure. Such a failure, if large enough, could also impact SJI's liquidity.
- Increasing interest rates will negatively impact the net income of SJI. Several of SJI's subsidiaries are capital intensive, resulting in the incurrence of significant amounts of debt financing. Almost all of the long-term debt of SJI and its subsidiaries is issued at fixed rates or has utilized interest rate swaps to mitigate changes in variable rates. However, new issues of long-term debt and all variable rate short-term borrowings are exposed to the impact of rising interest rates.
- SJI has guaranteed certain obligations of unconsolidated affiliates and is exposed to the risk that these affiliates will not be able to meet performance and financial commitments. SJI's unconsolidated affiliates develop and operate on-site energy related projects. SJI has guaranteed certain obligations of these affiliates in connection with the development and operation of the facilities. In the event that these projects do not meet specified levels of operating performance or are unable to meet certain financial obligations as they become due, SJI could be required to make payments related to these obligations.
- The inability to obtain capital, particularly short-term capital from commercial banks, could negatively impact the daily operations and financial performance of SJI. SJI uses short-term borrowings under committed and uncommitted credit facilities provided by commercial banks to supplement cash provided by operations, to support working capital

needs, and to finance capital expenditures, as incurred. SJG relies upon short-term borrowings issued under a commercial paper program supported by a committed bank credit facility to support working capital needs, and to finance capital expenditures, as incurred. If the customary sources of short-term capital were no longer available due to market conditions, SJI and its subsidiaries may not be able to meet its working capital and capital expenditure requirements and borrowing costs could increase.

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- A downgrade in either SJI's or SJG's credit ratings could negatively affect our ability to access adequate and cost effective capital. Our ability to obtain adequate and cost effective capital depends largely on our credit ratings, which are greatly influenced by financial condition and results of operations. If the rating agencies downgrade either SJI's or SJG's credit ratings, particularly below investment grade, our borrowing costs would increase. In addition, we would likely be required to pay higher interest rates in future financings and potential funding sources would likely decrease. To the extent that a decline in SJG's credit rating has a negative effect on SJI, SJI could be required to provide additional support to certain counterparties.
- Hedging activities of the company designed to protect against commodity price or interest rate risk may cause fluctuations in reported financial results and SJI's stock price could be adversely affected as a result. Although SJI enters into various contracts to hedge the value of energy assets, liabilities, firm commitments or forecasted transactions, the timing of the recognition of gains or losses on these economic hedges in accordance with accounting principles generally accepted in the United States of America does not always match up with the gains or losses on the items being hedged. The difference in accounting can result in volatility in reported results, even though the expected profit margin is essentially unchanged from the dates the transactions were consummated.
- The inability to obtain natural gas or electricity from suppliers would negatively impact the financial performance of SJI. Several of SJI's subsidiaries have businesses based upon the ability to deliver natural gas or electricity to customers. Disruption in the production or transportation to SJI from its suppliers could prevent SJI from completing sales to its customers.
- Transporting and storing natural gas involves numerous risks that may result in accidents and other operating risks and costs. SJI's gas distribution activities involve a variety of inherent hazards and operating risks, such as leaks, accidents, mechanical problems, natural disasters or terrorist activities which could cause substantial financial losses. In addition, these risks could result in loss of human life, significant damage to property, environmental pollution and impairment of operations, which in turn could lead to substantial losses. In accordance with customary industry practice, SJI maintains insurance against some, but not all, of these risks and losses. The occurrence of any of these events not fully covered by insurance could adversely affect SJI's financial position, results of operations and cash flows.
- Adverse results in legal proceedings could be detrimental to the financial condition of SJI. The outcomes of legal proceedings can be unpredictable and can result in adverse judgments.
- Renewable energy projects at Marina receive significant benefit from tax and regulatory incentives. A significant portion of the expected return on investment of these renewable energy projects is dependent upon federal investment tax credits (ITCs) and the future market for renewable energy credits (RECs). The benefits from ITCs are typically available when the project is placed in service while the benefits from RECs are produced during the entire life of the project. As a result, earnings from existing projects would be adversely affected without a liquid REC market. In addition, the return on investment from new projects may not be as attractive if ITCs are not available and/or a liquid REC market ceases to exist. Therefore, these projects are exposed to the risk that currently favorable tax and regulatory incentives expire or are adversely modified.
- Constraints in available pipeline capacity, particularly in the Marcellus Shale producing region, may negatively impact SJI's financial performance. Increasing natural gas production and/or pipeline transportation disruptions in the Marcellus region, where SJI has natural gas receipt requirements, may cause temporary take-away constraints resulting in higher transportation costs and the sale of shale gas at a loss.
- New legislation could have an impact on our ability to hedge risks associated with our business. The Dodd-Frank Act regulates derivative transactions, which include certain instruments used in our risk management activities. This legislation and any new regulations could increase the operational and transactional cost of derivatives contracts and affect the number and/or creditworthiness of available counterparties.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The principal property of SJI consists of SJG's gas transmission and distribution systems that include mains, service connections and meters. The transmission facilities carry the gas from the connections with Transco and Columbia to SJG's distribution systems for delivery to customers. As of December 31, 2012, there were approximately 122.7 miles of mains in the transmission systems and 6,142 miles of mains in the distribution systems.

SJG owns approximately 154 acres of land in Folsom, New Jersey which is the site of SJI's corporate headquarters. Approximately 140 acres of this property is deed restricted. SJG also has office and service buildings at six other locations in the territory. There is a liquefied natural gas storage and vaporization facility at one of these locations.

As of December 31, 2012, SJG's utility plant had a gross book value of $1.7 billion and a net book value, after accumulated depreciation, of $1.3 billion. In 2012, $156.0 million was spent on additions to utility plant and there were retirements of property having an aggregate gross book cost of $20.1 million.

Virtually all of SJG's transmission pipeline, distribution mains and service connections are under streets or highways or on the property of others. The transmission and distribution systems are maintained under franchises or permits or rights-of-way, many of which are perpetual. SJG's properties (other than property specifically excluded) are subject to a lien of mortgage under which its first mortgage bonds are outstanding. We believe these properties are well maintained and in good operating condition.

Nonutility property and equipment with a net book value of $292.4 million consists primarily of Marina's energy projects, in particular the thermal energy plant in Atlantic City, N.J.

Energy and Minerals Inc. (EMI) owns 235 acres of land in Vineland, New Jersey.

South Jersey Fuel, Inc., an inactive subsidiary, owns land in Deptford Township and owns real estate in Upper Township, New Jersey.

R&T Castellini, Inc., an inactive subsidiary, owns land and buildings in Vineland, New Jersey.

Item 3. Legal Proceedings

The Company is subject to claims arising in the ordinary course of business and other legal proceedings. The Company has been named in, among other actions, certain product liability claims related to our former sand mining subsidiary. We accrue liabilities related to these claims when we can reasonably estimate the amount or range of amounts of probable settlement costs or other charges for these claims. The Company has accrued approximately $3.1 million and $2.9 million related to all claims in the aggregate as of December 31, 2012 and 2011, respectively. Management does not believe that it is reasonably possible that there will be a material change in the Company's estimated liability in the near term and does not currently anticipate the disposition of any known claims that would have a material effect on the Company's financial position, results of operations or cash flows.

Item 4. Mine Safety Disclosures

Not Applicable

South Jersey Industries, Inc.
Part I

Item 4A. Executive Officers of the Registrant

Set forth below are the names, ages and positions of our executive officers along with their business experience during the past five years. All executive officers of SJI are elected annually and serve at the discretion of the Board of Directors. All information is as of the date of the filing of this report.

Name, age and position with the Company	Period Served
Edward J. Graham, Age 55	
Chairman	April 2005 - Present
Chief Executive Officer	February 2004 - Present
President	January 2003 - Present
David A. Kindlick, Age 58	
Chief Financial Officer	January 2002 - Present
Senior Vice President	January 2013 - Present
Vice President	June 1997 - December 2012
Jeffrey E. DuBois, Age 54	
Senior Vice President	January 2013 - Present
Vice President	January 2004 - December 2012
Michael J. Renna, Age 45	
Senior Vice President	January 2013 - Present
Vice President	January 2004 - December 2012
Kevin D. Patrick, Age 52	
Vice President	June 2007 - Present
Gina M. Merritt-Epps, Age 45	
General Counsel and Corporate Secretary	May 2009 - Present
Assistant General Counsel and Assistant Secretary	December 2007 - April 2009

PART II

Item 5. Market for the Registrant's Common Equity,

Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Price of Common Stock and Related Information

Quarter Ended	Market Price Per Share		Dividends	Quarter Ended	Market Price Per Share		Dividends
			Declared				Declared
2012	High	Low	Per Share	2011	High	Low	Per Share
March 31	$57.99	$49.55	$0.4025	March 31	$57.29	$51.89	$0.3650
June 30	$51.90	$46.52	$0.4025	June 30	$58.03	$50.64	$0.3650
September 30	$53.98	$50.50	$0.4025	September 30	$55.73	$42.85	$0.3650
December 31	$53.47	$45.81	$0.4425	December 31	$57.83	$47.33	$0.4025

These quotations are based on the list of composite transactions of the New York Stock Exchange. Our stock is traded on the New York Stock Exchange under the symbol SJI. We have declared and expect to continue to declare regular quarterly cash dividends. As of December 31, 2012, the latest available date, our records indicate there were 7,078 shareholders of record.

South Jersey Industries, Inc.
Part II

Stock Performance Graph

The performance graph below illustrates a five year comparison of cumulative total returns based on an initial investment of $100 in South Jersey Industries, Inc. common stock, as compared with the S&P 500 Stock Index and the S&P Utility Index for the period 2008 through 2012.

This performance chart assumes:

- $100 invested on December 31, 2007 in South Jersey Industries, Inc. common stock, in the S&P 500 Stock Index and in the S&P Utility Index; and
- All dividends are reinvested.

	Dec-07	Dec-08	Dec-09	Dec-10	Dec-11	Dec-12
S&P 500	$100	$63	$80	$92	$94	$109
S&P Utilities	$100	$71	$79	$84	$101	$102
SJI	$100	$114	$113	$161	$178	$162

Information required by this item is also found in Note 6 of the consolidated financial statements included under Item 8 of this report.

SJI has a stated goal of increasing its dividend by at least 6% to 7% annually.

In 2012, non-employee members of SJI's Board of Directors received an aggregate of 9,904 shares of restricted stock, valued at that time at $560,368, as part of their compensation for serving on the Board.

Issuer Purchases of Equity Securities - There were no purchases by SJI of its own common stock during the year ended December 31, 2012.

South Jersey Industries, Inc.
Part II

Item 6. Selected Financial Data

2012 HIGHLIGHTS
Five-Year Summary of Selected Financial Data
(In Thousands Where Applicable)

South Jersey Industries, Inc. and Subsidiaries
Year Ended December 31,

	2012	2011	2010	2009	2008
Operating Results:					
Operating Revenues	$706,280	$828,560	$925,067	$845,444	$961,977
Operating Income	$109,898	$121,607	$116,492	$111,110	$153,509
Income from Continuing Operations	$92,776	$89,859	$67,285	$58,532	$77,178
Discontinued Operations - Net (1)	(1,168)	(568)	(633)	(427)	(247)
Net Income	$91,608	$89,291	$66,652	$58,105	$76,931
Total Assets	$2,631,440	$2,247,510	$2,076,615	$1,782,008	$1,793,427
Capitalization:					
Equity	$736,214	$624,114	$570,097	$544,564	$516,448
Long-Term Debt	601,400	424,213	340,000	312,793	332,784
Total Capitalization	$1,337,614	$1,048,327	$910,097	$857,357	$849,232
Ratio of Operating Income to Fixed Charges (2)	5.1x	5.4x	5.3x	5.9x	6.0x
Diluted Earnings Per Common Share (Based on Average Diluted Shares Outstanding):					
Continuing Operations	$3.01	$2.99	$2.25	$1.96	$2.59
Discontinued Operations - Net (1)	(0.04)	(0.02)	(0.03)	(0.02)	(0.01)
Diluted Earnings Per Common Share	$2.97	$2.97	$2.22	$1.94	$2.58
Return on Average Equity (3)	13.6%	15.0%	12.1%	11.0%	15.5%
Share Data:					
Number of Shareholders of Record	7.1	7.1	7.1	7.3	7.5
Average Common Shares	30,744	30,000	29,861	29,785	29,707
Common Shares Outstanding at Year End	31,653	30,212	29,873	29,796	29,729

Dividend Reinvestment Plan:					
Number of Shareholders	4.8	4.4	4.9	5.1	5.1
Number of Participating Shares	2,462	2,193	2,682	2,072	2,102
Book Value at Year End	$23.26	$20.66	$19.08	$18.28	$17.33

South Jersey Industries, Inc.
Part II

Dividends Declared per Common Share	$1.65	$1.50	$1.36	$1.22	$1.11
Market Price at Year End	$50.33	$56.81	$52.82	$38.18	$39.85
Dividend Payout:					
From Continuing Operations	54.7 %	50.1 %	60.1 %	62.2 %	42.6 %
From Total Net Income	55.4 %	50.4 %	60.7 %	62.7 %	42.8 %
Market-to-Book Ratio	2.2x	2.7x	2.8x	2.1x	2.3x
Price Earnings Ratio (3)	16.7x	19.0x	23.4x	19.5x	15.4x
Consolidated Economic Earnings (4)					
Income from Continuing Operations	$92,776	$89,859	$67,285	$58,532	$77,178
Minus/Plus:					
Unrealized Mark-to-Market Losses/(Gains) on Derivatives and Realized (Gains)/Losses on Inventory Injection Hedges	(865)	(2,876)	13,698	12,723	(9,302)
Unrealized Loss on Property, Plant and Equipment	1,402	—	—	—	—
Economic Earnings	$93,313	$86,983	$80,983	$71,255	$67,876
Earnings per Share from Continuing Operations	$3.01	$2.99	$2.25	$1.96	$2.59
Minus/Plus:					
Unrealized Mark-to-Market Losses/(Gains) on Derivatives and Realized (Gains)/Losses on Inventory Injection Hedges	(0.03)	(0.10)	0.45	0.42	(0.32)
Unrealized Loss on Property, Plant and Equipment	0.05	—	—	—	—
Economic Earnings per Share	$3.03	$2.89	$2.70	$2.38	$2.27

(1) Represents discontinued business segments: sand mining and distribution operations sold in 1996 and fuel oil operations with related environmental liabilities in 1986 (See Note 3 to Consolidated Financial Statements).
(2) Calculated as Operating Income divided by Interest Charges.
(3) Calculated based on Income from Continuing Operations.
(4) This section includes the non-generally accepted accounting principles (“non-GAAP”) financial measures of Economic Earnings and Economic Earnings per share. See Management's Discussion and Analysis of Financial Condition and Results of Operations in Item 7 of this report for a discussion regarding the use of non-GAAP financial measures.

South Jersey Industries, Inc.
Part II

Item 7. Management's Discussion and Analysis of Financial Condition and
Results of Operations

OVERVIEW - South Jersey Industries, Inc. (SJI or the Company) is an energy services holding company that provides a variety of products and services through the following wholly owned subsidiaries:

South Jersey Gas Company (SJG)

SJG, a New Jersey corporation, is an operating public utility company engaged in the purchase, transmission and sale of natural gas for residential, commercial and industrial use. SJG also sells natural gas and pipeline transportation capacity (off-system sales) on a wholesale basis to various customers on the interstate pipeline system and transports natural gas purchased directly from producers or suppliers to their customers. SJG contributed approximately 63.6% of SJI's net income on a consolidated basis in 2012.

SJG's service territory covers approximately 2,500 square miles in the southern part of New Jersey. It includes 112 municipalities throughout Atlantic, Cape May, Cumberland and Salem Counties and portions of Burlington, Camden and Gloucester Counties, with an estimated permanent population of 1.2 million. SJG benefits from its proximity to Philadelphia, PA and Wilmington, DE on the western side of its service territory and Atlantic City, NJ and the popular shore communities on the eastern side. Continuing expansion of SJG's infrastructure throughout its seven-county region has fueled annual customer growth and creates opportunities for future extension into areas not yet served by natural gas. In the past, economic growth in Atlantic City and the surrounding region has been primarily driven by new and proposed gaming and non-gaming investments that emphasize destination style attractions. While many of these new projects were suspended or postponed due to the current economic environment, a new entertainment resort opened to the public in April 2012 and the city continues to benefit from additional planned construction activity, most notably the expansion of other casinos, the construction of a new conference center and other non-gaming development. Combining with the gaming industry catalyst is the ongoing transition of southern New Jersey's oceanfront communities from seasonal resorts to year round economies. Building expansions in the medical, hospitality and education sectors throughout the service territory have contributed to SJG's growth. In 2012, SJG serves approximately 67% of households within its territory with natural gas. SJG also serves southern New Jersey's diversified industrial base that includes processors of petroleum and agricultural products; chemical, glass and consumer goods manufacturers; and high technology industrial parks.

As of December 31, 2012, SJG served 357,306 residential, commercial and industrial customers in southern New Jersey, compared with 351,304 customers at December 31, 2011. No material part of SJG's business is dependent upon a single customer or a few customers. Gas sales, transportation and capacity release for 2012 amounted to 129.5 MMdts (million dekatherms), of which 55.8 MMdts were firm sales and transportation, 1.4MMdts were interruptible sales and transportation and 72.3 MMdts were off-system sales and capacity release. The breakdown of firm sales and transportation includes 37.4% residential, 18.5% commercial, 23.6% industrial, and 20.5% cogeneration and electric generation. At year-end 2012, SJG served 333,347 residential customers, 23,506 commercial customers and 453 industrial customers. This includes 2012 net additions of 5,669 residential customers and 337 commercial customers.

SJG makes wholesale gas sales to gas marketers for resale and ultimate delivery to end users. These “off-system” sales are made possible through the issuance of the Federal Energy Regulatory Commission (FERC) Orders No. 547 and 636. Order No. 547 issued a blanket certificate of public convenience and necessity authorizing all parties, which are not interstate pipelines, to make FERC jurisdictional gas sales for resale at negotiated rates, while Order No. 636 allowed SJG to deliver gas at delivery points on the interstate pipeline system other than its own city gate stations and release excess pipeline capacity to third parties. During 2012, off-system sales amounted to 8.3 MMdts and capacity release amounted to 64.0 MMdts.

Supplies of natural gas available to SJG that are in excess of the quantity required by those customers who use gas as their sole source of fuel (firm customers) make possible the sale and transportation of gas on an interruptible basis to commercial and industrial customers whose equipment is capable of using natural gas or other fuels, such as fuel oil and propane. The term “interruptible” is used in the sense that deliveries of natural gas may be terminated by SJG at any time if this action is necessary to meet the needs of higher priority customers as described in SJG's tariffs. In 2012, usage by interruptible customers, excluding off-system customers amounted to 1.4 MMdts, approximately 1.0% of the total throughput.

South Jersey Energy Solutions, LLC

SJI established South Jersey Energy Solutions, LLC, (SJES) as a direct subsidiary for the purpose of serving as a holding company for all of SJI's non-utility businesses. The following businesses are wholly owned subsidiaries of SJES:

South Jersey Energy Company (SJE)

SJE provides services for the acquisition and transportation of natural gas and electricity for retail end users and markets total energy management services. As of December 31, 2012, SJE marketed natural gas and electricity to approximately 7,400 commercial and industrial customers. SJE no longer sells commodity in the residential markets. Most customers served by SJE are located within New Jersey, northwestern Pennsylvania and New England. In 2012, SJE contributed approximately 8.1% of SJI's net income on a consolidated basis.

Marina Energy LLC (Marina)

Marina develops and operates energy-related projects. Marina's largest wholly owned operating project provides cooling, heating and emergency power to the Borgata Hotel Casino & Spa in Atlantic City, NJ. Marina also owns numerous solar generation projects and has a 50% equity interest in LVE Energy Partners, LLC (LVE) which has entered into a contract to design, build, own and operate a district energy system and central energy center for a planned resort in Las Vegas, Nevada.

Marina's other projects include a 50% equity interest in Energenic-US, LLC (Energenic). Energenic develops, owns and operates on-site energy projects such as thermal facilities, combined heat and power facilities, landfill gas-fired electric production facilities and solar projects. In 2012, Marina contributed approximately 30.2% of SJI's net income on a consolidated basis.

South Jersey Resources Group, LLC (SJRG)

SJRG markets natural gas storage, commodity and transportation assets on a wholesale basis. Customers include energy marketers, electric and gas utilities and natural gas producers. SJRG's marketing activities occur mainly in the mid-Atlantic, Appalachian and southern regions of the country.

SJRG also conducts price risk management activities by entering into a variety of physical and financial transactions including forward contracts, swap agreements, option contracts and futures contracts. In 2012, SJRG transacted 435.4 Bcf of natural gas. In 2012, SJRG incurred a loss which was approximately (1.4%) of SJI's net income on a consolidated basis.

South Jersey Energy Service Plus, LLC (SJESP)

SJESP services residential and small commercial HVAC systems, provides plumbing services, and services appliances under warranty via a subcontractor arrangement as well as on a time and materials basis. SJESP serves southern New Jersey where it is one of the largest local HVAC service company's with nearly 30 experienced, NATE certified technicians. SJESP sold the rights to renew the home appliance repair contracts to a provider of homeowner assistance services under an exclusive agreement that took effect in the third quarter of 2011. Under the terms of this agreement, SJESP received a fee for the sale of these rights. SJESP also receives a commission on all new and renewed service contracts and is paid a fee to service those warranty contracts. In 2012, SJESP incurred a loss which was less than (1%) of SJI's net income on a consolidated basis.

South Jersey Exploration, LLC (SJEX)

SJEX owns oil, gas and mineral rights in the Marcellus Shale region of Pennsylvania. SJEX was a wholly owned subsidiary of SJRG until November 2011, when it became a wholly owned subsidiary of SJES. SJEX remains part of SJI's wholesale energy operations. In 2012, SJEX contributed less than 1% of SJI's net income on a consolidated basis.

Other

SJI Services, LLC provides services such as information technology, human resources, corporate communications, materials purchasing and fleet management to SJI and its other subsidiaries.

Energy & Minerals, Inc. (EMI) principally manages liabilities associated with its discontinued operations of nonutility subsidiaries.

South Jersey Industries, Inc.
Part II

Primary Factors Affecting SJI's Business

SJI's stated long-term goals are to: 1) Grow Economic Earnings per share by an average of at least 6% to 7% per year; 2) Increase the dividend on common stock by at least 6% to 7% annually; and 3) Maintain a low-to-moderate risk platform. Management established those goals in conjunction with SJI's Board of Directors based upon a number of different internal and external factors that characterize and influence SJI's current and expected future activities.

The following is a summary of the primary factors we expect to have the greatest impact on SJI's performance and ability to achieve long-term goals going forward:

Business Model - In developing SJI's current business model, our focus has been on our core utility and natural extensions of that business. That focus enables us to concentrate on business activities that match our core competencies. Going forward we expect to pursue business opportunities that fit this model.

Customer Growth - Southern New Jersey, our primary area of operations, has not been immune to the issues impacting the new housing market nationally. However, net customers for SJG still grew 1.7% for 2012 as SJG increased our focus on customer conversions. In 2012, the 5,293 consumers converting their homes and businesses from other heating fuels, such as electric, propane or oil represented over 71.0% of the total new customer acquisitions for the year. In comparison, conversions over the past five years averaged 3,708 annually. Customers in our service territory typically base their decisions to convert on comparisons of fuel costs, environmental considerations and efficiencies. As such, SJG began a comprehensive partnership with the State's Office of Clean Energy to educate consumers on energy efficiency and to promote the rebates and incentives available to natural gas users.

Regulatory Environment - SJG is primarily regulated by the New Jersey Board of Public Utilities (BPU). The BPU sets the rates that SJG charges its rate-regulated customers for services provided and establishes the terms of service under which SJG operates. SJG expects the BPU to continue to set rates and establish terms of service that will enable SJG to obtain a fair and reasonable return on capital invested. The BPU approved a Conservation Incentive Program (CIP) effective October 1, 2006, discussed in greater detail under "Results of Operations", that protects SJG's net income from reductions in gas used by residential, commercial and small industrial customers. In addition, in March 2011 and May 2012, the BPU approved extensions of the Capital Investment Recovery Tracker (CIRT II and CIRT III, respectively), allowing SJG to accelerate $95.3 million of capital spending into 2011 and 2012 from future periods. Under CIRT II and CIRT III, SJG capitalizes a return on investments until they are recovered in rate base as utility plant in service.

Weather Conditions and Customer Usage Patterns - Usage patterns can be affected by a number of factors, such as wind, precipitation, temperature extremes and customer conservation. SJG's earnings are largely protected from fluctuations in temperatures by the CIP. The CIP has a stabilizing effect on utility earnings as SJG adjusts revenues when actual usage per customer experienced during an annual period varies from an established baseline usage per customer. Our nonutility retail marketing business is directly affected by weather conditions, as it does not have regulatory mechanisms that address weather volatility. The impact of different weather conditions on the earnings of our nonutility businesses is dependent on a range of different factors. Consequently, weather may impact the earnings of SJI's various subsidiaries in different, or even opposite, ways. Further, the profitability of individual subsidiaries may vary from year-to-year despite experiencing substantially similar weather conditions.

Changes in Natural Gas and Electricity Prices - The utility's gas costs are passed on directly to customers without any profit margin added by SJG. The price the utility charges its periodic customers is set annually, with a regulatory mechanism in place to make limited adjustments to that price during the course of a year. In the event that gas cost increases would justify customer price increases greater than those permitted under the regulatory mechanism, SJG can petition the BPU for an incremental rate increase. High prices can make it more difficult for SJG's customers to pay their bills and may result in elevated levels of bad-debt expense. Among our nonutility activities, the one most likely to be impacted by changes in natural gas prices is our wholesale gas marketing business. Wholesale gas marketing typically benefits from volatility in gas prices during different points in time. The actual price of the commodity does not typically have an impact on the performance of this business line. Our ability to add and retain customers at our retail marketing business is affected by the relationship between the price that the utility charges customers for gas or electric and the cost available in the market at specific points in time. However, retail marketing accounts for a very small portion of SJI's overall activities.

South Jersey Industries, Inc.
Part II

Energy Project Development - Marina Energy, LLC, SJI's energy project development business, focuses on designing, building, owning and/or operating energy production facilities on, or adjacent to, customer sites. That business is currently involved with several projects that are either operating, or are under development. Based upon our experience to date, market issues that impact the reliability and price of electricity supplied by utilities, and discussions that we are having regarding additional projects, we expect to continue to expand this business. However, the price of natural gas, as well as the availability of various tax incentives and rebates, has a direct effect on the economics of these projects. Further, our largest project opportunities to date have been and are expected to continue to be in the casino gaming industry. Consequently, the economic condition of that industry is important to the near term prospects for obtaining additional projects.

Changes in Interest Rates - SJI has operated in a relatively low interest rate environment over the past several years. Rising interest rates would raise the expense associated with existing variable-rate debt and all issuances of new debt. We have sought to mitigate the impact of a potential rising rate environment by directly issuing fixed-rate debt, or by entering into derivative transactions to hedge against rising interest rates.

Labor and Benefit Costs - Labor and benefit costs have a significant impact on SJI's profitability. Benefit costs, especially those related to pension and health care, have risen in recent years. We sought to manage these costs by revising health care plans offered to existing employees, capping postretirement health care benefits, and changing health care and pension packages offered to new hires. We expect savings from these changes to gradually increase as new hires replace retiring employees. In an effort to accelerate the realization of those benefits, we offered a voluntary separation program at the beginning of 2010 to our unionized employees. Our workforce totaled approximately 700 employees at the end of 2012, of which approximately 320 of that total are unionized.

Balance Sheet Strength - Our goal is to maintain a strong balance sheet with an average annual equity-to-capitalization ratio of 50%. Our average equity-to-capitalization ratio was 44% as calculated for the four quarters of 2012 as compared with 48% in 2011. A strong balance sheet permits us to maintain the financial flexibility necessary to take advantage of growth opportunities and to address volatile economic and commodity markets while maintaining a low-to-moderate risk platform.

CRITICAL ACCOUNTING POLICIES - ESTIMATES AND ASSUMPTIONS - As described in the notes to our consolidated financial statements, management must make estimates and assumptions that affect the amounts reported in the consolidated financial statements and related disclosures. Actual results could differ from those estimates. Five types of transactions presented in our consolidated financial statements require a significant amount of judgment and estimation. These relate to regulatory accounting, derivatives, environmental remediation costs, pension and other postretirement benefit costs, and revenue recognition.

Regulatory Accounting - SJI's largest subsidiary, SJG, maintains its accounts according to the Uniform System of Accounts as prescribed by the BPU. As a result of the ratemaking process, SJG is required to follow Financial Accounting Standards Board (FASB) ASC Topic 980 - “Regulated Operations.” SJG is required under Topic 980 to recognize the impact of regulatory decisions on its financial statements. SJG is required under its Basic Gas Supply Service (BGSS) clause to forecast its natural gas costs and customer consumption in setting its rates. Subject to BPU approval, SJG is able to recover or return the difference between gas cost recoveries and the actual costs of gas through a BGSS charge to customers. SJG records any over/under recoveries as a regulatory asset or liability on the consolidated balance sheets and reflects them in the BGSS charge to customers in subsequent years. SJG also enters into derivatives that are used to hedge natural gas purchases. The offset to the resulting derivative assets or liabilities is also recorded as a regulatory asset or liability on the consolidated balance sheets. See additional detailed discussions on Rates and Regulatory Actions in Note 10 to the consolidated financial statements.

Derivatives - SJI recognizes assets or liabilities for contracts that qualify as derivatives that are entered into by its subsidiaries when contracts are executed. We record contracts at their fair value in accordance with FASB ASC Topic 815 - "Derivatives and Hedging." We record changes in the fair value of the effective portion of derivatives qualifying as cash flow hedges, net of tax, in Accumulated Other Comprehensive Loss and recognize such changes in the income statement when the hedged item affects earnings. Changes in the fair value of derivatives not designated as hedges are recorded in earnings in the current period. Currently we do not designate energy-related derivative instruments as cash flow hedges. Beginning in July 2012, hedge accounting was discontinued for the remaining interest rate derivatives. As a result, unrealized gains and losses on these derivatives, that were previously included in Accumulated Other Comprehensive Loss on the consolidated balance sheets, are being reclassified into earnings over the remaining life of the derivative.

South Jersey Industries, Inc.
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Certain derivatives that result in the physical delivery of the commodity may meet the criteria to be accounted for as normal purchases and normal sales, if so designated, in which case the contract is not marked-to-market, but rather is accounted for when the commodity is delivered. Due to the application of regulatory accounting principles generally accepted in the United States of America (GAAP), derivatives related to SJG's gas purchases that are marked-to-market are recorded through the BGSS. SJG periodically enters into financial derivatives to hedge against forward price risk. These derivatives are recorded at fair value with an offset to regulatory assets and liabilities through SJG's BGSS, subject to BPU approval (See Notes 10 and 11 to the consolidated financial statements).

We adjust the fair value of the contracts each reporting period for changes in the market. As discussed in Notes 16 and 17 of the consolidated financial statements, energy-related derivative instruments are traded in both exchange-based and non-exchange-based markets. Exchange-based contracts are valued using unadjusted quoted market sources in active markets and are categorized in Level 1 in the fair value hierarchy established by FASB ASC Topic 820 - “Fair Value Measurements and Disclosures.” Certain non-exchange-based contracts are valued using indicative non-binding price quotations available through brokers or from over-the-counter, on-line exchanges and are categorized in Level 2. These price quotations reflect the average of the bid-ask mid-point prices and are obtained from sources that management believes provide the most liquid market. Management reviews and corroborates the price quotations with at least one additional source to ensure the prices are observable market information, which includes consideration of actual transaction volumes, market delivery points, bid-ask spreads and contract duration. Derivative instruments that are used to limit our exposure to changes in interest rates on variable-rate, long-term debt are valued using quoted prices on commonly quoted intervals, which are interpolated for periods different than the quoted intervals, as inputs to a market valuation model. Market inputs can generally be verified and model selection does not involve significant management judgment, as a result, these instruments are categorized in Level 2 in the fair value hierarchy. For non-exchange-based derivatives that trade in less liquid markets with limited pricing information, model inputs generally would include both observable and unobservable inputs. In instances where observable data is unavailable, management considers the assumptions that market participants would use in valuing the asset or liability. This includes assumptions about market risks such as liquidity, volatility and contract duration. Such instruments are categorized in Level 3 in the fair value hierarchy as the model inputs generally are not observable. Counterparty credit risk and the credit risk of SJI, are incorporated and considered in the valuation of all derivative instruments as appropriate. The effect of counterparty credit risk and the credit risk of SJI on the derivative valuations is not significant.

Significant Unobservable Inputs - Management uses the discounted cash flow model to value Level 3 physical and financial forwards, which calculates fair values based on forward market prices, original transaction prices, volumes, risk-free rate of return and credit spreads. Inputs to the valuation model are reviewed and revised as needed, based on historical information, updated market data, market liquidity and relationships, and changes in third party pricing sources. The validity of the fair values and changes in these values from period to period are examined and qualified against historical expectations by the risk management function. If any discrepancies are identified during this process, the fair values or the market pricing information is evaluated further and adjusted, if necessary.

Level 3 valuation methods for natural gas derivative contracts include utilizing another location in close proximity adjusted for certain pipeline charges to derive a basis value. The significant unobservable inputs used in the fair value measurement of certain natural gas contracts consist of forward prices developed based on industry standard methodologies. Significant increases (decreases) in these forward prices for purchases of natural gas would result in a directionally similar impact to the fair value measurement and for sales of natural gas would result in a directionally opposite impact to the fair value measurement. Level 3 valuation methods for electric represent the value of the contract marked to the forward wholesale curve, as provided by daily exchange quotes for delivered electricity. The significant unobservable inputs used in the fair value measurement of electric contracts consist of fixed contracted electrical load profiles; therefore no change in unobservable inputs would occur. The forward wholesale curve is updated daily. Management reviews and corroborates the price quotations to ensure the prices are observable which includes consideration of actual transaction volumes, market delivery points, bid-ask spreads and contract duration.

Environmental Remediation Costs -We estimate a range of future costs based on projected investigation and work plans using existing technologies. In preparing consolidated financial statements, SJI records liabilities for future costs using the lower end of the range because a single reliable estimation point is not feasible due to the amount of uncertainty involved in the nature of projected remediation efforts and the long period over which remediation efforts will continue. We update estimates each year to take into account past efforts, changes in work plans, remediation technologies, government regulations and site specific requirements (See Note 15 to the consolidated financial statements).

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Pension and Other Postretirement Benefit Costs - The costs of providing pension and other postretirement employee benefits are impacted by actual plan experience as well as assumptions of future experience. Employee demographics, plan contributions, investment performance, and assumptions concerning mortality, return on plan assets, discount rates and health care cost trends all have a significant impact on determining our projected benefit obligations. We evaluate these assumptions annually and adjust them accordingly. These adjustments could result in significant changes to the net periodic benefit costs of providing such benefits and the related liabilities recognized by SJI.

The combination of slowing equity markets and lower discount rates in 2011, which were used in determining plan costs in 2012, increased the cost of providing such plans in 2012. SJI took measures to manage this increase by making a $25.0 million pension plan contribution in January 2012; as such, the resulting financial impact on the company was not significant. Discount rates continued to decline in 2012 and are the primary cost driver used in determining plan costs in 2013. However, improvements in the equity markets during 2012 and a $12.7 million pension plan contribution in January 2013, are expected to offset the negative impact of declining discount rates. As such, the resulting financial impact on the Company is not expected to be significant in 2013.

Additional information regarding investment returns and assumptions can be found in Pension and Other Postretirement Benefits in Note 12 to the consolidated financial statements.

Revenue Recognition - Gas and electricity revenues are recognized in the period the commodity is delivered to customers. SJG, SJRG and SJE bill customers monthly. A majority of SJG and SJE customers have their meters read on a cycle basis throughout the month. For SJG and SJE retail customers that are not billed at the end of each month, we record an estimate to recognize unbilled revenues for gas/electricity delivered from the date of the last meter reading to the end of the month. SJG's and SJE's unbilled revenue for natural gas is estimated each month based on monthly deliveries into the system; unaccounted for natural gas based on historical results; customer-specific use factors, when available; actual temperatures during the period; and applicable customer rates. SJE's unbilled revenue for retail electricity is based on customer-specific use factors and applicable customer rates. We bill SJG customers at rates approved by the BPU. SJE and SJRG customers are billed at rates negotiated between the parties.

We recognize revenues related to SJESP's appliance service contracts on a monthly basis as work is completed or commissions are earned. Revenues related to services provided on a time and materials basis are recognized on a monthly basis as the services are provided.

Marina recognizes revenue on a monthly basis as services are provided and for on-site energy production that is delivered to its customers.

The BPU allows SJG to recover gas costs in rates through the BGSS price structure. SJG defers over/under recoveries of gas costs and includes them in subsequent adjustments to the BGSS rate. These adjustments result in over/under recoveries of gas costs being included in rates during future periods. As a result of these deferrals, utility revenue recognition does not directly translate to profitability. While SJG realizes profits on gas sales during the month of providing the utility service, significant shifts in revenue recognition may result from the various recovery clauses approved by the BPU. This revenue recognition process does not shift earnings between periods, as these clauses only provide for cost recovery on a dollar-for-dollar basis (See Notes 10 and 11 to the consolidated financial statements).

In January 2010, the BPU approved an extension of the CIP through September 2013. The CIP may be extended for a one year period in the absence of a Board order taking any affirmative action to the contrary. Each CIP year begins October 1 and ends September 30 of the subsequent year. On a monthly basis during the CIP year, SJG records adjustments to earnings based on weather and customer usage factors, as incurred. Subsequent to each year, SJG makes filings with the BPU to review and approve amounts recorded under the CIP. BPU approved cash inflows or outflows generally will not begin until the next CIP year and have no impact on earnings at that time.

NEW ACCOUNTING PRONOUNCEMENTS - See detailed discussions concerning New Accounting Pronouncements and their impact on SJI in Note 1 to the consolidated financial statements.

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RATES AND REGULATION - As a public utility, SJG is subject to regulation by the BPU. Additionally, the Natural Gas Policy Act, which was enacted in November 1978, contains provisions for Federal regulation of certain aspects of SJG's business. SJG is affected by Federal regulation with respect to transportation and pricing policies applicable to pipeline capacity from Transcontinental Gas Pipeline Corporation (SJG's major supplier), Columbia Gas Transmission Corporation and Dominion Transmission, Inc., since such services are provided under rates and terms established under the jurisdiction of the FERC. SJG's retail sales are made under rate schedules within a tariff filed with, and subject to the jurisdiction of, the BPU. These rate schedules provide primarily for either block rates or demand/commodity rate structures. SJG's primary rate mechanisms include base rates, the Basic Gas Supply Service Clause, Capital Investment Recovery Tracker, Energy Efficiency Tracker and the Conservation Incentive Program.

In September 2010, the BPU granted SJG a base rate increase of $42.1 million, which was predicated in part upon an 8.21% rate of return on rate base that included a 10.3% return on common equity. The $42.1 million includes $16.6 million of revenue previously recovered through the CIP and $6.8 million of revenues previously recovered through the CIRT, resulting in incremental revenue of $18.7 million. SJG was permitted to recover regulatory assets contained in its petition and is allowed to defer certain federally mandated pipeline integrity management program costs for recovery in its next base rate case. In addition, annual depreciation expense will be reduced by $1.2 million as a result of the amortization of excess cost of removal recoveries. The BPU also authorized a Phase II of the base rate proceeding to address the recovery of investment in CIRT not rolled into rate base in this case.

In April 2009, the BPU approved the Capital Investment Recovery Tracker (CIRT) an accelerated infrastructure investment program and an associated rate tracker, which allowed SJG to accelerate $103.0 million of capital spending into 2009 and 2010. The BPU authorized Phase II of its rate case proceeding to address the recovery of investments in CIRT not rolled into rate base in its September 2010 rate case settlement. The CIRT allows SJG to earn a return of, and return on, investment as the capital is spent. In March 2011, the BPU approved an extension of the Capital Investment Recovery Tracker (CIRT II) allowing SJG to accelerate $60.3 million of capital spending into 2011 and 2012. In May 2012, the BPU approved a modification and extension of CIRT II and CIRT III allowing SJG to accelerate an incremental $35.0 million of capital spending through December 2012. Under CIRT II and CIRT III, SJG capitalizes a return on investments until they are recovered in rate base as utility plant in service.

The Conservation Incentive Program (CIP) is a BPU approved pilot program that is designed to eliminate the link between SJG profits and the quantity of natural gas SJG sells, and to foster conservation efforts. With the CIP, SJG's profits are tied to the number of customers served and how efficiently SJG serves them, thus allowing SJG to focus on encouraging conservation and energy efficiency among its customers without negatively impacting net income. The CIP tracking mechanism adjusts earnings based on weather, and also adjusts SJG's earnings when actual usage per customer experienced during an annual period varies from an established baseline usage per customer. In January 2010, the BPU approved an extension of the CIP through September 2013. Under the terms of this settlement, the CIP may be extended for a one year period in the absence of a Board order taking any affirmative action to the contrary with regard to the pilot program.

Utility earnings are recognized during current periods based upon the application of the CIP. The cash impact of variations in customer usage will result in cash being collected from, or returned to, customers during the subsequent CIP year, which runs from October 1 to September 30.

The effects of the CIP on SJG's net income for the last three years and the associated weather comparisons were as follows ($'s in millions):

	2012	2011	2010

Net Income Benefit:			
CIP - Weather Related	$9.4	$5.6	$1.1
CIP - Usage Related	5.8	2.2	5.5
Total Net Income Benefit	$15.2	$7.8	$6.6
Weather Compared to 20-Year Average	17.7% warmer	10.0% warmer	2.2% warmer
Weather Compared to Prior Year	8.6% warmer	7.8% warmer	0.1% warmer

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As part of the CIP, SJG is required to implement additional conservation programs including customized customer communication and outreach efforts, targeted upgrade furnace efficiency packages, financing offers, and an outreach program to speak to local and state institutional constituents. SJG is also required to reduce gas supply and storage assets and their associated fees. Note that changes in fees associated with supply and storage assets have no effect on SJG's net income as these costs are passed through directly to customers on a dollar-for-dollar basis.

Earnings accrued and payments received under the CIP are limited to a level that will not cause SJG's return on equity to exceed 10.3% (excluding earnings from off-system gas sales and certain other tariff clauses) and the annualized savings attained from reducing gas supply and storage assets.

See additional detailed discussions on Rates and Regulatory Actions in Note 10 to the consolidated financial statements.

ENVIRONMENTAL REMEDIATION - See detailed discussion concerning Environmental Remediation in Note 15 to the consolidated financial statements.

COMPETITION - SJG's franchises are non-exclusive. Currently, no other utility provides retail gas distribution services within SJG's territory. SJG does not expect any other utilities to do so in the foreseeable future because of the extensive investment required for utility plant and related costs. SJG competes with oil, propane and electricity suppliers for residential, commercial and industrial users, with alternative fuel source providers (wind, solar and fuel cells) based upon price, convenience and environmental factors, and with other marketers/brokers in the selling of wholesale natural gas services. The market for natural gas commodity sales is subject to competition due to deregulation. SJG's competitive position was enhanced while maintaining margins by using an unbundled tariff. This tariff allows full cost-of-service recovery when transporting gas for SJG's customers. Under this tariff, SJG profits from transporting, rather than selling, the commodity. SJG's residential, commercial and industrial customers can choose their supplier, while SJG recovers the cost of service through transportation service (See Customer Choice Legislation below).

SJRG competes in the wholesale natural gas market against a wide array of competitors on a cost competitive, term of service, and reliability basis. SJRG has been a reliable energy provider in this arena for 17 years. There has been significant consolidation of energy wholesale operations and large financial institutions have also entered the marketplace. We expect this trend to continue in the near term, which could result in downward pressure on the margins available.

Marina competes with other companies that develop and operate on-site energy production. Marina also faces competition from customers' preferences for alternative technologies for energy production, as well as those customers that address their energy needs internally.

SJE competes with utilities and other third-party marketers to sell the unregulated natural gas and electricity commodity to customers. Marketers compete largely on price, which is driven by the commodity market. While the utilities are typically indifferent as to where customers get their gas or electricity, the price they set for the commodity they sell creates competition for SJE. Based on its market share, SJE is one of the largest marketers of natural gas in southern New Jersey as of December 31, 2012. In addition, similar to SJG, SJE faces competition from other energy products.

SJESP competes primarily with smaller, local contractors in southern New Jersey that service residential and commercial HVAC systems and provide major appliance repair and plumbing services. These contractors typically only serve their local communities and do not serve the entire southern part of New Jersey.

CUSTOMER CHOICE LEGISLATION - All residential natural gas customers in New Jersey can choose their natural gas commodity supplier under the terms of the “Electric Discount and Energy Competition Act of 1999." This bill created the framework and necessary time schedules for the restructuring of the state's electric and natural gas utilities. The Act established unbundling, where redesigned utility rate structures allow natural gas and electric consumers to choose their energy supplier. It also established time frames for instituting competitive services for customer account functions and for determining whether basic gas supply services should become competitive. Customers purchasing natural gas from a provider other than the local utility (the “marketer”) are charged for the gas costs by the marketer and charged for the transportation costs by the utility. The total number of customers in SJG's service territory purchasing natural gas from a marketer averaged 39,398, 37,829, and 30,152 during 2012, 2011 and 2010, respectively.

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RESULTS OF OPERATIONS:

SJI operates in several different reportable operating segments. Gas Utility Operations (SJG) consists primarily of natural gas distribution to residential, commercial and industrial customers. Wholesale Energy Operations include the activities of SJRG and SJEX. SJE is involved in both retail gas and retail electric activities. Retail Gas and Other Operations include natural gas acquisition and transportation service business lines. Retail Electric Operations consist of electricity acquisition and transportation to commercial and industrial customers. On-Site Energy Production consists of Marina's thermal energy facility and other energy-related projects. Appliance Service Operations includes SJESP's servicing of appliances under warranty via a subcontractor arrangement as well as on a time and materials basis. The Retail Energy Operations caption includes Retail Gas and Other, Retail Electric, On-Site Energy Production and Appliance Service Operations.

Net Income attributable to SJI for 2012 increased $2.3 million, or 2.6%, to $91.6 million compared to 2011 primarily as a result of the following:

- The income contribution from Marina increased $6.0 million to $27.6 million due primarily to the impact of the investment tax credit available on renewable energy facilities as compared to the prior year.
- The income contribution from SJE increased $5.5 million to $7.4 million due primarily to the change in unrealized gains and losses on forward financial contracts used to mitigate electric price risk as discussed in Operating Revenues - Nonutility below, partially offset by the expiration of a significant electric sales contract with a group of school boards.
- The income contribution from SJG increased $5.4 million to $58.2 million due primarily to an increase in CIRT-related earnings along with an increase in residential customers.
- The income contribution from SJRG decreased $11.3 million to a net loss of $1.3 million due primarily to the change in unrealized gains and losses on derivatives used by SJRG to mitigate natural gas commodity price risk, as discussed below.
- The income contribution from SJESP decreased $2.3 million to a net loss of less than $0.1 million due primarily to proceeds received in 2011 from a provider of homeowner assistance services in accordance with an agreement with the Company that gives them the exclusive right to renew the home appliance repair contracts at SJESP.

Net Income attributable to SJI for 2011 increased $22.6 million, or 34.0%, to $89.3 million compared to 2010 primarily as a result of the following:

- The income contribution from Marina increased $12.2 million to $21.6 million due primarily to the impact of the investment tax credit available on renewable energy facilities.
- The income contribution from SJG increased $9.0 million to $52.9 million due primarily to the settlement of the base rate case in September 2010.
- The income contribution from SJRG increased $6.5 million to $10.0 million due primarily to the change in unrealized gains and losses on derivatives used by SJRG to mitigate natural gas commodity price risk, as discussed below.
- The income contribution from SJESP increased $1.9 million to $2.2 million due primarily to proceeds received from a provider of homeowner assistance services, in accordance with an agreement with the Company that

gives them the exclusive right to renew the home appliance repair contracts at SJESP.

- The income contribution from SJE decreased $7.0 million to $1.8 million due primarily to the change in unrealized gains and losses on forward financial contracts used to mitigate price risk on electricity as discussed under Operating Revenues – Nonutility below.

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A significant portion of the volatility in operating results is due to the impact of the accounting methods associated with SJI's derivative activities. The Company uses derivatives to limit its exposure to market risk on transactions to buy, sell, transport and store natural gas and to buy and sell retail electricity. The Company also uses derivatives to limit its exposure to increasing interest rates on variable-rate debt.

The types of transactions that cause the most significant volatility in operating results are as follows:

- SJRG purchases and holds natural gas in storage to earn a profit margin from its ultimate sale in the future. SJRG uses derivatives to mitigate commodity price risk in order to substantially lock-in the profit margin that will ultimately be realized. However, gas stored in inventory is accounted for at the lower of average cost or market; the derivatives used to reduce the risk associated with a change in the value of the inventory are accounted for at fair value, with changes in fair value recorded in operating results in the period of change. As a result, earnings are subject to volatility as the market price of derivatives change, even when the underlying hedged value of the inventory is unchanged. Additional volatility in earnings is created when realized gains and losses on derivatives used to mitigate commodity price risk on expected future purchases of gas in storage are recognized in earnings when the derivatives settle but the cost of the related gas in storage is not recognized in earnings until the period of withdrawal. This volatility can be significant from period to period. Over time, gains or losses on the sale of gas in storage will be offset by losses or gains on the derivatives, resulting in the realization of the profit margin expected when the transactions were initiated.

- SJE uses forward contracts to mitigate commodity price risk on fixed price electric contracts with customers. In accordance with GAAP, the forward contracts are recorded at fair value, with changes in fair value recorded in earnings in the period of change. Several related customer contracts are not considered derivatives and therefore are not recorded in earnings until the electricity is delivered. As a result, earnings are subject to volatility as the market price of the forward contracts change, even when the underlying hedged value of the customer contract is unchanged. Over time, gains or losses on the sale of the fixed price electric under contract will be offset by losses or gains on the forward contracts, resulting in the realization of the profit margin expected when the transactions were initiated.

As a result, management also uses the non-generally accepted accounting principles (“non-GAAP”) financial measures of Economic Earnings, Economic Earnings per share, Non-Utility Economic Earnings, Wholesale Energy Economic Earnings and Retail Energy Economic Earnings when evaluating the results of operations for its nonutility operations. These non-GAAP financial measures should not be considered as an alternative to GAAP measures, such as net income, operating income, earnings per share from continuing operations or any other GAAP measure of liquidity or financial performance.

We define Economic Earnings as: Income from continuing operations, (1) less the change in unrealized gains and plus the change in unrealized losses, as applicable and in each case after tax, on all derivative transactions, and (2) less realized gains and plus realized losses, as applicable and in each case after tax, on all commodity derivative transactions attributed to expected purchases of gas in storage to match the recognition of these gains and losses with the recognition of the related cost of the gas in storage in the period of withdrawal, and (3) less the impact of transactions or contractual arrangements where the true economic impact will be realized in a future period.

Economic Earnings is a significant performance metric used by our management to indicate the amount and timing of income from continuing operations that we expect to earn after taking into account the impact of derivative instruments on the related transactions and transactions or contractual arrangements where the true economic impact will be realized in a future period. Specifically, we believe that this financial measure indicates to investors the profitability of the entire derivative related transaction and not just the portion that is subject to mark-to-market valuation under GAAP. Considering only the change in market value on the derivative side of the transaction can produce a false sense as to the ultimate profitability of the total transaction as no change in value is reflected for the non-derivative portion of the transaction.

Economic Earnings for 2012 increased $6.3 million, or 7.3%, to $93.3 million compared to 2011 primarily as a result of the following:

- The income contribution from Marina increased $6.1 million to $28.1 million due primarily to the impact of the investment tax credit available on renewable energy facilities as compared to the prior year.
- The income contribution from SJG increased $5.4 million to $58.2 million due primarily to an increase in CIRT-related earnings along with an increase in residential customers.
- The income contribution from SJESP decreased $2.3 million to a net loss of less than $0.1 million due primarily to proceeds received in 2011 from a provider of homeowner assistance services in accordance with an agreement with the Company that gives them the exclusive right to renew the home appliance repair contracts at SJESP.
- The income contribution from SJE decreased $2.2 million to $1.6 million due primarily to the expiration of a significant electric sales contract with a group of school boards.

Economic Earnings for 2011 increased $6.0 million, or 7.4%, to $87.0 million compared to 2010 primarily as a result of the following:

- The income contribution from Marina increased $10.9 million to $22.0 million due primarily to the impact of the investment tax credit available on renewable energy facilities.
- The income contribution from SJG increased $9.0 million to $52.9 million due primarily to the settlement of the base rate case in September 2010.
- The income contribution from SJESP increased $1.9 million to $2.2 million due primarily to proceeds received from a provider of homeowner assistance services, in accordance with an agreement with the Company that gives them the exclusive right to renew the home appliance repair contracts at SJESP.
- The income contribution from SJRG decreased $15.4 million to $4.9 million due primarily to tighter spreads attained on our storage and transportation assets.

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The following table presents a reconciliation of our income from continuing operations and earnings per share from continuing operations to Economic Earnings and Economic Earnings per share (in thousands except per share data):

	2012	2011	2010
Income from Continuing Operations	$92,776	$89,859	$67,285
Minus/Plus:			
Unrealized Mark-to-Market Losses/(Gains) on Derivatives	(854)	(2,815)	15,068
Realized (Gains)/Losses on Inventory Injection Hedges	(11)	(61)	(1,370)
Unrealized Loss on Property, Plant and Equipment	1,402	—	—
Economic Earnings	$93,313	$86,983	$80,983
Earnings per Share from Continuing Operations	$3.01	$2.99	$2.25
Minus/Plus:			
Unrealized Mark-to-Market Losses/(Gains) on Derivatives	(0.03)	(0.10)	0.50
Realized (Gains)/Losses on Inventory Injection Hedges	—	—	(0.05)
Unrealized Loss on Property, Plant and Equipment	0.05	—	—
Economic Earnings per Share	$3.03	$2.89	$2.70
Non-Utility Income from Continuing Operations	$34,535	$36,970	$23,361
Minus/Plus:			
Unrealized Mark-to-Market Losses/(Gains) on Derivatives	(854)	(2,815)	15,068
Realized (Gains)/Losses on Inventory Injection Hedges	(11)	(61)	(1,370)
Unrealized Loss on Property, Plant and Equipment	$1,402	$—	$—
Non-Utility Economic Earnings	$35,072	$34,094	$37,059
Wholesale Energy Income from Continuing Operations	$(1,210)	$10,960	$4,447
Minus/Plus:			
Unrealized Mark-to-Market Losses/(Gains) on Derivatives	5,900	(5,078)	18,141
Realized (Gains)/Losses on Inventory Injection Hedges	(11)	(61)	(1,370)
Wholesale Energy Economic Earnings	$4,679	$5,821	$21,218
Retail Energy Income from Continuing Operations	$35,745	$26,010	$18,914
Minus/Plus:			
Unrealized Mark-to-Market Losses/(Gains) on Derivatives	(6,754)	2,263	(3,073)
Unrealized Loss on Property, Plant and Equipment	1,402	—	—
Retail Energy Economic Earnings	$30,393	$28,273	$15,841

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The effect of derivative instruments not designated as hedging instruments under GAAP in the consolidated statements of income (see Note 16 to the consolidated financial statements) is as follows (gains (losses) in thousands):

	2012	2011	2010
(Losses) gains on energy related commodity contracts	$(193)	$5,377	$(22,624)
Gains (losses) on interest rate contracts	660	(149)	(641)
Total before income taxes	467	5,228	(23,265)
Income taxes (A)	(191)	(2,143)	9,539
Total after income taxes	276	3,085	(13,726)
Unrealized mark-to-market gains (losses) on derivatives held by affiliated companies, net of tax (A)	578	(270)	(1,342)
Total unrealized mark-to-market gains (losses) on derivatives	854	2,815	(15,068)
Realized gains (losses) on inventory injection hedges, net of tax (A)	11	61	1,370
Unrealized Loss on Property, Plant and Equipment	(1,402)	—	—
Total reconciling items between income from continuing operations and economic earnings	$(537)	$2,876	$(13,698)

(A) Determined using a combined statutory tax rate of 41%

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Throughput-Utility - The following table summarizes the composition of select gas utility data for the three years ended December 31 (in thousands, except for customer and degree day data):

	December 31, 2012			December 31, 2011			December 31, 2010		
Utility Throughput - dth:									
Firm Sales -									
Residential	18,586	14	%	20,332	16	%	22,962	21	%
Commercial	4,733	4	%	5,426	4	%	5,884	5	%
Industrial	258	1	%	319	—		292	—	
Cogeneration and electric generation	1,598	1	%	1,618	2	%	1,167	1	%
Firm Transportation -									
Residential	2,335	2	%	2,382	2	%	2,136	2	%
Commercial	5,587	4	%	5,715	4	%	6,043	6	%
Industrial	12,892	10	%	13,024	10	%	12,625	11	%
Cogeneration and electric generation	9,816	8	%	6,110	5	%	5,500	5	%
Total Firm Throughput	55,805	44	%	54,926	43	%	56,609	51	%
Interruptible Sales	2	—		13	—		52	—	
Interruptible Transportation	1,361	1	%	1,769	2	%	1,842	2	%
Off-System	8,318	6	%	8,009	6	%	6,034	5	%
Capacity Release	63,998	49	%	63,413	49	%	46,278	42	%
Total Throughput - Utility	129,484	100	%	128,130	100	%	110,815	100	%
Utility Operating Revenues:									
Firm Sales-									
Residential	$248,547	59	%	$232,457	56	%	$302,824	64	%
Commercial	53,726	13	%	58,122	14	%	67,967	14	%
Industrial	2,872	—		3,991	2	%	3,573	1	%
Cogeneration and electric generation	6,562	2	%	9,469	2	%	7,774	2	%
Firm Transportation -									
Residential	16,388	4	%	15,161	4	%	11,908	2	%
Commercial	24,217	6	%	22,500	5	%	21,989	5	%
Industrial	21,637	5	%	18,827	5	%	16,613	3	%
Cogeneration and electric generation	7,555	2	%	3,742	1	%	4,598	1	%
Total Firm Revenues	381,504	91	%	364,269	89	%	437,246	92	%
Interruptible Sales	52	—		230	—		770	—	
Interruptible Transportation	1,546	—		1,727	—		1,842	—	
Off-System	30,249	7	%	37,413	9	%	30,757	7	%
Capacity Release	7,322	2	%	7,534	2	%	4,156	1	%
Other	1,201	—		1,276	—		1,211	—	
	421,874	100	%	412,449	100	%	475,982	100	%
Less:									
Intercompany Sales	1,056			6,707			6,575		
Total Utility Operating Revenue	420,818			405,742			469,407		

Less:			
Cost of sales	187,655	181,158	259,807

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Conservation recoveries *	9,019			7,159			6,910		
Remediation Adjustment Clause recoveries *	7,823			6,579			6,863		
Energy Efficiency Tracker (EET) recoveries*	3,350			2,499			1,433		
Revenue taxes	5,974			8,022			8,607		
Utility Margin	$206,997			$200,325			$185,787		
Margin:									
Residential	$118,015	57	%	$124,882	62	%	$115,697	62	%
Commercial and industrial	51,048	25	%	52,356	26	%	44,705	24	%
Cogeneration and electric generation	5,062	2	%	3,235	2	%	2,957	2	%
Interruptible	83	—		136	—		177	—	
Off-system & capacity release	2,044	1	%	1,829	1	%	1,258	1	%
Other revenues	1,602	1	%	1,576	1	%	2,158	1	%
Margin before incentive mechanisms	177,854	86	%	184,014	92	%	166,952	90	%
CIRT mechanism	3,031	2	%	2,655	1	%	7,523	4	%
CIP mechanism	25,672	12	%	13,270	7	%	11,139	6	%
EET mechanism	440	—		386	—		173	—	
Utility Margin	$206,997	100	%	$200,325	100	%	$185,787	100	%
Number of Customers at Year End:									
Residential	333,347	93	%	327,678	93	%	324,246	93	%
Commercial	23,506	7	%	23,169	7	%	23,010	7	%
Industrial	453	—		457	—		469	—	
Total Customers	357,306	100	%	351,304	100	%	347,725	100	%
Annual Degree Days:	3,862			4,226			4,582		

* Represents expenses for which there is a corresponding credit in operating revenues. Therefore, such recoveries have no impact on our financial results.

Throughput - Utility - Total gas throughput increased 1.4 MMdts, or 1.1%, from 2011 to 2012. This increase is due to higher electric generation transportation throughput, which increased 3.7 MMdts, or 60.7%, as a result of the excessive heat during the summer months of 2012. As the third quarter of 2012 was one of the warmest on record in the region, higher electric consumption for air conditioning drove the demand for greater natural gas consumption by the region's electric producers. Partially offsetting this increase in throughput was lower consumption by residential and commercial customers. Residential and commercial firm sales decreased 1.7 MMdts and 0.7 MMdts, respectively, as a result of weather that was 8.6% warmer in 2012, compared with 2011.

Total gas throughput increased 17.3 MMdts, or 15.6%, from 2010 to 2011. This increase was realized primarily in the Capacity Release markets. Capacity Release increased 17.1 MMdts during 2011, as compared with 2010, as a result of increased opportunity for such sales. Additional capacity became available during the latter part of 2010 as capacity previously transferred out of SJG under the provisions of the Conservation Incentive Program (CIP) was returned to the utility. Firm throughput decreased 1.7 MMdts, or 3.0%, during 2011, compared with 2010, as a result of 7.8% warmer weather, partially offset by customer growth. SJG added 3,579 customers over the twelve month period ended December 31, 2011, which represents a growth rate of 1.0%.

Operating Revenues - Utility 2012 vs. 2011 - Revenues increased $15.1 million, or 3.7%, during 2012 compared with 2011 after eliminating intercompany transactions. Firm sales revenue increased $17.2 million, or 4.7%, during 2012 versus 2011, primarily as a result of two customer refunds in 2011, which reduced prior year revenue by $39.8 million (See Note 10 to the consolidated financial statements). There were no such refunds during 2012. In 2012, firm sales revenue was significantly impacted by weather that was 8.6% warmer than last year and lower natural gas costs. As a result, the change in revenue caused by the 2011 refunds was substantially offset by the impact of warm weather and lower gas costs on revenues during 2012. The average cost of natural gas purchased during 2012 was $4.56 per dt, representing an 23.2% decrease relative to the average cost of $5.94 per dt during 2011.

As previously stated under "Throughput-Utility," record warm weather during the summer season resulted in increased sales to area electric producers. This resulted in a $3.8 million increase in cogeneration and electric generation transportation revenue over 2011.

Off-System Sales (OSS) revenue decreased $7.2 million, or 19.1%, despite throughput that was relatively consistent from 2011 to 2012. The decrease was primarily due to lower natural gas prices in 2012. As can be seen in the table above, this reduction in revenue had no adverse impact on SJG's margin in 2012.

Operating Revenues - Utility 2011 vs. 2010 - Revenues decreased $63.7 million, or 13.6%, during 2011 compared with 2010 after eliminating intercompany transactions. Firm sales revenue decreased $73.0 million, or 16.7%, during 2011 versus 2010, as the result of lower natural gas costs, which precipitated two customer refunds in 2011 totaling $39.8 million, exclusive of sales tax which does not impact utility revenues. The average cost of natural gas purchased during 2011 was $5.94 per dt, representing an 11.3% decrease relative to the average cost of $6.70 per dt during 2010.

While changes in gas costs and BGSS recoveries may fluctuate from period to period, SJG does not profit from the sale of the commodity. Therefore, corresponding fluctuation in Operating Revenue-Utility or Cost of Sales-Utility have no impact on Company profitability, as further discussed under "Margin-Utility."

Warmer weather during 2011, primarily during the fourth quarter, also contributed to lower revenue. Weather was 7.8% warmer than 2010 and 10.0% warmer than normal.

Partially offsetting the negative impact of lower natural gas costs and warm weather on firm sales revenues was the impact of adding approximately 3,600 customers during 2011, representing 1% growth.

Off-system sales (OSS) revenue and capacity release revenue increased $6.7 million and $3.4 million, respectively, during 2011 vs. 2010, as both sales and capacity release volumetric throughput increased. As previously stated under "Throughput-Utility," this was made possible when additional capacity became available during the latter part of 2010, as capacity previously transferred out of SJG under the CIP was returned to SJG. As reflected in the Margin table above, the impact of the higher OSS and capacity release activity during 2011 did not have a material impact on the earnings of the Company, as SJG is required to share 85% of the profits of such activity with the ratepayers.

Operating Revenues - Nonutility 2012 vs. 2011 - Combined revenues for SJI's nonutility businesses, net of intercompany transactions, decreased $137.4 million, or 32.5%, in 2012, compared with 2011.

SJE's revenues from retail gas operations, net of intercompany transactions, decreased by $19.9 million, or 19.9%, in 2012, compared with 2011. Excluding the impact of the net change in unrealized gains/losses recorded on forward financial contracts of $(0.8) million due to price volatility, revenues decreased $20.7 million, or 20.7%. This decrease was due to a 31.0% decrease in the average monthly NYMEX settle price, along with the impact of SJE exiting the residential market in October of 2011 and significantly warmer weather experienced during 2012. SJE's residential contracts were at higher fixed prices reflective of market conditions from three years ago when the expired program was established. The majority of SJE's other natural gas customer contracts are market-priced. These decreases are partially offset by a 9.4% increase in overall volumes due to the purchase of a retail gas marketing book in central Pennsylvania that added over 350 commercial and small industrial customers in the third quarter of 2012.

As of December 31, SJE was serving the following number of retail gas customers:

	2012	2011
Commercial & Large Volume	2,174	1,662

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Sales volumes for the comparative period were as follows (in dekatherms):

	2012	2011
Residential	—	407,808
Commercial & Large Volume	20,475,114	18,252,903

Market conditions continue to make it difficult to be competitive with the pricing of the utility in the residential and small commercial markets. We continue to focus our marketing efforts on the pursuit of non-heat-sensitive commercial customers in an effort to mitigate price volatility and weather risk.

SJE's revenues from retail electric operations, net of intercompany transactions, decreased $61.1 million, or 30.6%, in 2012, compared with 2011. Excluding the impact of the net change in unrealized gains/losses recorded on forward financial contracts due to price volatility of $(12.2) million, revenues decreased $73.3 million or 36.2%. A summary of SJE's retail electric revenue is as follows (in millions):

	2012	2011	Change
SJE Retail Electric Revenue	$138.3	$199.4	$(61.1)
Add: Unrealized Losses (Subtract: Unrealized Gains)	(9.1)	3.1	(12.2)
SJE Retail Electric Revenue, Excluding Unrealized Losses (Gains)	$129.2	$202.5	$(73.3)

This decrease was mainly due to a 19.6% decrease in average monthly sales price which was driven by lower-priced fixed price contracts and lower Locational Marginal Price (LMP) per megawatt hour in 2012 compared with 2011. Volumes also decreased 21.9% for the comparative period mainly due to a significant school board contract that expired in the second quarter of 2012. SJE uses forward financial contracts to mitigate commodity price risk on fixed price electric contracts. In accordance with GAAP, the forward financial contracts are recorded at fair value, with changes in fair value recorded in earnings in the period of change. Some of the related customer contracts are not considered derivatives and therefore are not recorded in earnings until electricity is delivered. As a result, earnings are subject to volatility as the market price for the forward financial contracts change, even when the underlying hedged value of the contract is unchanged. Over time, gains or losses on the sale of the fixed price electricity under contract will be offset by losses or gains on the forward financial contracts, resulting in the realization of the profit margin expected when the transactions were initiated. SJE serves both fixed and market-priced customers.

SJRG's revenues from wholesale energy operations, net of intercompany transactions, decreased $50.8 million, or 75.2%, in 2012, compared with 2011. Excluding the impact of the net change in unrealized gains and losses recorded on forward financial contracts due to price volatility of $18.6 million and adjusting for the net change in realized gains and losses on all hedges attributed to inventory injection transactions of $0.1 million to align them with the related cost of inventory in the period of withdrawal, SJRG's revenues decreased $32.1 million. A summary of SJRG's revenue is as follows (in millions):

	2012	2011	Change
SJRG Revenue	$17.2	$68.0	$(50.8)
Add: Unrealized Losses (Subtract: Unrealized Gains)	10.0	(8.6)	18.6

Add: Realized Losses (Subtract: Realized Gains) on Inventory Injection Hedges	—	(0.1)	0.1
SJRG Revenue, Excluding Unrealized Losses (Gains) and Realized Losses (Gains) on Inventory Injection Hedges	$27.2	$59.3	$(32.1)

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This decrease in revenues is mainly due to a 71.6% decrease in sales of storage volumes, which are shown gross in the statement of operations, along with a 31.0% decrease in the average monthly NYMEX settle price. As discussed in Note 16 to the consolidated financial statements, revenues and expenses related to the energy trading activities of SJRG are presented on a net basis in Operating Revenues - Nonutility.

Revenues from on-site energy production at Marina, net of intercompany transactions, decreased $1.6 million, or 4.2%, in 2012 compared with 2011, due mainly to lower sales rates for chilled and hot water production at the thermal facility which were driven by lower underlying commodity rates and an asset sale that resulted in the termination of a large customer contract in August 2011. These decreases were partially offset by revenues from several new renewable energy projects that began operations in 2011 and 2012.

Revenues from appliance service operations at SJESP decreased $3.4 million, or 20.0%, in 2012, compared with 2011, due mainly to a decrease in customer warranty contract sales. SJESP sold the rights to renew the home appliance repair contracts to a provider of homeowner assistance services under an exclusive agreement that took effect in the third quarter of 2011. Under the terms of this agreement, SJESP received a fee for the sale of these rights (See Other Income and Expense). SJESP also receives a commission for all new and renewed service contracts and is paid a fee to service those warranty contracts.

Operating Revenues - Nonutility 2011 vs. 2010 - Combined revenues for SJI's nonutility businesses, net of intercompany transactions, decreased by $32.8 million, or 7.2%, in 2011, compared with 2010.

SJE's revenues from retail gas operations, net of intercompany transactions, decreased by $12.2 million, or 10.9%, in 2011, compared with 2010. Excluding the impact of the net change in unrealized gains/losses recorded on forward financial contracts of $0.2 million due to price volatility, revenues decreased $12.0 million. This decrease was due mainly to an 8.0% decrease in the average monthly NYMEX settle price and the impact of SJE exiting the residential market in October of 2011. SJE's residential contracts were at higher fixed prices reflective of market conditions from two years ago when the recently expired program was established. The majority of SJE's other natural gas customer contracts are market-priced. As of December 31, SJE was serving the following number of retail gas customers:

	2011	2010
Residential	—	7,177
Commercial & Large Volume	1,662	1,533

Sales volumes for the comparative period were as follows (in dekatherms):

	2011	2010
Residential	407,808	686,689
Commercial & Large Volume	18,252,903	17,633,243

Market conditions continue to make it difficult to be competitive in the residential and small commercial markets. We continue to focus our marketing efforts on the pursuit of non-heat-sensitive commercial customers in an effort to mitigate price volatility and weather risk.

SJE's revenues from retail electric operations, net of intercompany transactions, increased $2.9 million, or 1.5%, in 2011, compared with 2010. Excluding the impact of the net change in unrealized gains/losses recorded on forward financial contracts due to price volatility of $11.1 million, revenues increased $14.0 million or 7.4%. A summary of SJE's retail electric revenue is as follows (in millions):

	2011	2010	Change
SJE Retail Electric Revenue	$199.4	$196.5	$2.9
Add: Unrealized Losses (Subtract: Unrealized Gains)	3.1	(8.0)	11.1
SJE Retail Electric Revenue, Excluding Unrealized Losses (Gains)	$202.5	$188.5	$14.0

This increase was mainly due to a 11.4% increase in volumes which was partially offset by a 2.5% decrease in the average monthly Locational Marginal Price (LMP) per megawatt hour in 2011 compared with 2010. SJE uses forward financial contracts to mitigate commodity price risk on fixed price electric contracts. In accordance with GAAP, the forward financial contracts are recorded at fair value, with changes in fair value recorded in earnings in the period of change. Some of the related customer contracts are not considered derivatives and therefore are not recorded in earnings until electricity is delivered. As a result, earnings are subject to volatility as the market price for the forward financial contracts change, even when the underlying hedged value of the contract is unchanged. Over time, gains or losses on the sale of the fixed price electricity under contract will be offset by losses or gains on the forward financial contracts, resulting in the realization of the profit margin expected when the transactions were initiated. SJE serves both fixed and market-priced customers.

SJRG's revenues from wholesale energy operations, net of intercompany transactions, decreased $20.4 million, or 23.0%, in 2011, compared with 2010. Excluding the impact of the net change in unrealized gains/losses recorded on forward financial contracts of $(39.3) million due to price volatility and adjusting for the net change in realized gains and losses on all hedges attributed to inventory transactions of $2.2 million to align them with the related cost of inventory in the period of withdrawal, SJRG's revenues decreased $57.5 million. A summary of SJRG's revenue is as follows (in millions):

	2011	2010	Change
SJRG Revenue	$68.0	$88.4	$(20.4)
Add: Unrealized Losses (Subtract: Unrealized Gains)	(8.6)	30.7	(39.3)
Add: Realized Losses (Subtract: Realized Gains) on Inventory Injection Hedges	(0.1)	(2.3)	2.2
SJRG Revenue, Excluding Unrealized Losses (Gains) and Realized Losses (Gains) on Inventory Injection Hedges	$59.3	$116.8	$(57.5)

This decrease in revenues is mainly attributable to a 61.6% decrease in sales of storage volumes, which are shown gross in the statement of operations, along with an 8% decrease in the average monthly NYMEX settle price, partially offset by a 31.4% increase in total sales volumes. As discussed in Note 16 to the consolidated financial statements, revenues and expenses related to the energy trading activities of SJRG are presented on a net basis in Operating Revenues - Nonutility.

Revenues from on-site energy production at Marina, net of intercompany transactions, decreased $0.2 million, or 0.4%, in 2011 compared with 2010, due mainly to an asset sale in 2011 that resulted in the termination of a large customer contract, which was partially offset by several new solar projects that came on line in 2011. Thermal plant hot and chilled water revenues were relatively unchanged for the comparative period.

Revenues from appliance service operations at SJESP decreased $2.7 million, or 13.6%, in 2011, compared with 2010, due mainly to a decrease in customer warranty contract sales. SJESP sold the rights to renew the home appliance repair contracts to a provider of homeowner assistance services under an exclusive agreement that took effect in the third quarter of 2011. Under the terms of this agreement, SJESP received a fee for the sale of these rights (See Other Income and Expense). SJESP will also receive a commission for all new and renewed service contracts and be paid a fee to service those warranty contracts.

Margin - Utility - SJG's margin is defined as natural gas revenues less natural gas costs; volumetric and revenue based energy taxes; and regulatory rider expenses. We believe that margin provides a more meaningful basis for evaluating utility operations than revenues since natural gas costs, energy taxes and regulatory rider expenses are passed through to customers, and therefore, have no effect on margin. Natural gas costs are charged to operating expenses on the basis of therm sales at the prices approved by the New Jersey Board of Public Utilities through the BGSS tariff.

Total margin in 2012 increased $6.7 million, or 3.3%, from 2011 primarily due to customer additions and increased margins from cogeneration and electric generation due to the warmer temperatures noted above. SJG added 6,002 customers during 2012 representing growth of 1.7% over the prior year and a corresponding increase in margin.

The CIP protected $25.7 million of pre-tax margin in 2012 that would have been lost due to lower customer usage, compared to $13.3 million in 2011. Of these amounts, $15.8 million and $9.6 million were related to weather variations and $9.9 million and $3.7 million were related to other customer usage variations in 2012 and 2011, respectively.

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Total margin in 2011 increased $14.5 million, or 7.8%, from 2010 primarily due to a full year of the rate case settlement discussed above under "Rates and Regulation," customer additions and increased firm industrial customer usage. Approximately $6.8 million of revenues previously recovered through the CIRT were moved into base rates beginning in September 2010, see additional discussion in Note 10 to the consolidated financial statements.

The CIP protected $13.3 million of pre-tax margin in 2011 that would have been lost due to lower customer usage, compared to $11.1 million in 2010. Of these amounts, $9.6 million and $1.9 million were related to weather variations and $3.7 million and $9.2 million were related to other customer usage variations in 2011 and 2010, respectively.

Gross Margin - Nonutility - Gross margin for the nonutility businesses is defined as revenue less all costs that are directly related to the production, selling and delivery of the company's products and services. These costs primarily include natural gas and electric commodity costs as well as certain payroll and related benefits. On the statements of consolidated income, revenue is reflected in Operating Revenues - Nonutility and the costs are reflected in Cost of Sales - Nonutility. As discussed in Note 16 to the consolidated financial statements, revenues and expenses related to the energy trading activities of SJRG are presented on a net basis in Operating Revenues - Nonutility.

For 2012, combined gross margins for the nonutility businesses, net of intercompany transactions, decreased $3.7 million to $55.3 million compared with 2011. This decrease is primarily due to the following:

- Gross margin from the wholesale energy operations of SJRG decreased $17.0 million in 2012 compared with 2011. Excluding the impact of the net change in unrealized gains and losses recorded on forward financial contracts due to price volatility of $18.6 million and adjusting for the net change in realized gains and losses on all hedges attributed to inventory injection transactions of $0.1 million as discussed above, gross margin for SJRG increased $1.7 million. This increase is due mainly to strong margins from acquired capacity and optimization in 2012 compared to losses on transportation contracts in 2011 that occurred due to temporary take-away constraints. These increases are partially offset by the treatment of the costs attributable to injections of gas into storage, which are included in the carrying value of gas in storage when injections are made. SJRG has not injected significant amounts of gas into storage during 2012, and as a result, these costs have been expensed as incurred.

SJRG expects to continue to add incremental margin from marketing and related opportunities in the Marcellus region, capitalizing on its established presence in the area. Future margins could fluctuate significantly due to the volatile nature of wholesale gas prices. As of December 31, 2012, SJRG had 9.3 Bcf of storage and 530,701 dts/day of transportation under contract.

- Gross margin from the appliance service operations at SJESP decreased $0.8 million in 2012 compared with 2011 mainly due to lower customer warranty contract sales (See Operating Revenues - Nonutility). Gross margin as a percentage of Operating Revenues increased 2.1 percentage points in 2012 compared with 2011 mainly due to the significant decline in personnel costs that resulted from an initiative to right-size our workforce.

- Gross margin from SJE's retail electric operations increased $11.7 million in 2012, compared with 2011. Excluding the impact of the net change in unrealized gains/losses recorded on forward financial contracts due to price volatility of $(12.2) million as discussed above, gross margin decreased $0.5 million in 2012 compared with 2011 mainly due to a significant school board contract that expired in the second quarter of 2012 (See Operating Revenues - Nonutility). Excluding the impact of the unrealized gains/losses discussed above, gross margin as a percentage of Operating Revenues increased 1.9 percentage points in 2012 compared with 2011 mainly due to lower capacity, transmission and network service costs and the addition of numerous higher-margin customers over the past twelve months, which was partially offset by the expiration of the school board contract.

- Gross margin from on-site energy production at Marina increased $2.7 million in 2012 compared with 2011. Gross margin as a percentage of Operating Revenues increased 12.1 percentage points. This was due mainly to the impact of several solar projects coming on line in 2012, which was partially offset by an asset sale that resulted in the termination of a customer contract in 2011. Solar projects typically produce higher margins as compared to the margins produced by the terminated contract.

- Gross margin from SJE's retail gas and other operations remained relatively unchanged in 2012, compared with 2011. Excluding the impact of the net change in unrealized gains/losses recorded on forward financial contracts due to price volatility of $(0.8) million as discussed above, gross margin decreased $0.8 million in 2012, compared with 2011. Excluding the impact of the net change in unrealized gains/losses recorded on forward financial contracts as discussed above, gross margin as a percentage of Operating Revenues remained relatively unchanged in 2012, compared with 2011. The decrease in margin is mainly due to the warmer weather experienced in the first and fourth quarters of 2012, partially offset by the impact of acquiring a retail gas marketing book in the third quarter of 2012 that contained higher-margin customers (See Operating Revenues - Nonutility).

For 2011, combined gross margins for the nonutility businesses, net of intercompany transactions, decreased $1.7 million to $59.0 million compared with 2010. This decrease is primarily due to the following:

- Gross margin from the wholesale energy operations of SJRG increased $11.2 million in 2011 compared with 2010. Excluding the impact of the net change in unrealized gains and losses recorded on forward financial contracts of $(39.3) million and the net change in realized gains and losses on all hedges attributed to inventory transactions of $2.2 million as discussed above, gross margin for SJRG decreased $25.9 million due mainly to tighter spreads attained on our storage and transportation assets. Storage assets allow SJRG to lock in the differential between purchasing natural gas at low current prices and selling equivalent quantities at higher future prices. Gross margin is generated via seasonal pricing differentials. While this margin will be attained over the transaction cycle, the timing of physical injections and withdrawals and related hedge settlements can cause earnings fluctuations for accounting purposes due to the volatile nature of wholesale gas prices. Margins were also negatively impacted by increased production of natural gas in the Marcellus region where SJRG has committed to purchase minimum volumes at index-based prices. This increased production, coupled with pipeline disruptions and expansion delays, caused temporary take-away constraints throughout the region which caused a decrease in market prices. Market prices have improved as additional capacity was brought on line beginning in November of 2011.

Overall, SJRG's contribution to margin from storage and transportation assets has decreased due to market conditions and, as a result, SJRG has shed some of these assets. However, SJRG expects to continue to add incremental margin from marketing and related opportunities in the Marcellus region, capitalizing on its established presence in the area. Future margins could fluctuate significantly due to the volatile nature of wholesale gas prices. As of December 31, 2011, SJRG had 8.6 Bcf of storage and 194,282 dts/day of transportation under contract.

- Gross Margin from on-site energy production at Marina decreased $0.5 million in 2011 compared with 2010. This decrease was mainly due to higher electricity costs at the thermal plant and the loss of one customer (See Operating Revenues - Nonutility) that were partially offset by margins from new solar projects that came on line in 2011. Gross margin as a percentage of Operating Revenues did not change significantly in 2011 compared with 2010.

- Gross margin from SJE's retail gas and other operations decreased $0.5 million in 2011, compared with 2010. Excluding the impact of a $0.2 million change in unrealized gains/losses recorded on forward financial contracts as discussed above, gross margin decreased $0.3 million in 2011, compared with 2010, due mainly to the impact of SJE exiting the residential market (See Operating Revenues - Nonutility). Gross margins as a percentage of Operating Revenues did not change significantly in 2011, compared with 2010.

- Gross margin from SJE's retail electric operations decreased $9.8 million in 2011 compared with 2010. Excluding the impact of a $11.1million change in unrealized gains/losses recorded on forward financial contracts as discussed above, gross margin increased $1.3 million in 2011 compared with 2010. This increase was mainly due to volumetric growth(See Operating Revenues - Nonutility). Excluding the impact of the change in unrealized gains/losses, gross margin as a percentage of Operating Revenues did not change significantly in 2011 compared with 2010.

- Gross margin from the appliance service operations at SJESP decreased $1.9 million in 2011 compared with 2010 due mainly to lower customer warranty contract sales (See Operating Revenues - Nonutility). Gross margin as a percentage of Operating Revenues decreased 5.0 percentage points due to the significant decline in high-margin warranty contracts and residential installation jobs.

Operations Expense - A summary of net changes in operations expense follows (in thousands):

	2012 vs. 2011	2011 vs. 2010
Gas Utility Operations	$10,276	$888
Nonutility:		
Wholesale Energy Operations	1,454	1,145
Retail Gas and Other Operations	1,512	(57)
Retail Electric Operations	718	1,454
On-Site Energy Production	1,779	670
Appliance Service Operations	(2,138)	163
Total Nonutility	3,325	3,375
Intercompany Eliminations and Other	(859)	596
Total Operations Expense	$12,742	$4,859

Utility Operations expense increased $10.3 million during 2012, as compared with 2011. This is the result of increases in expense associated with uncollectible customer accounts receivable, along with moderate increases in corporate support, governance, compliance and employee compensation costs. Also contributing was increased spending under the New Jersey Clean Energy Program and Energy Efficiency Programs. Such costs are recovered on a dollar-for-dollar basis; therefore, SJG experienced an offsetting increase in revenues during the period.

Utility Operations expense increased $0.9 million during 2011, as compared with 2010. This is the result of increased spending under the New Jersey Clean Energy Program and Energy Efficiency Programs. Such costs are recovered on a dollar-for-dollar basis; therefore, SJG experienced an offsetting increase in revenues during the period.

Nonutility Operations expense increased $3.3 million and $3.4 million in 2012 and 2011, respectively, compared to the prior year due mainly to additional personnel at the retail gas and other operations segment, partially offset by a decrease in personnel at the appliance service operations segment, along with additional governance and compliance costs to support continued growth. Also contributing to the increase is a $2.4 million impairment charge due to a reduction in the expected cash flows to be received from a solar generating facility within the on-site energy production segment.

Other Operating Expenses - A summary of changes in other consolidated operating expenses (in thousands):

	2012 vs. 2011	2011 vs. 2010
Maintenance	$493	$1,572
Depreciation	$5,587	$1,731

Energy and Other Taxes	$(2,203)	$47

Maintenance - Maintenance expense increased $0.5 million during 2012 compared with 2011 primarily due to an increase in Remediation Adjustment Clause (RAC) expense amortization. Maintenance expense increased $1.6 million during 2011, compared with 2010 due to the BPU-approved amortization and recovery of previously deferred maintenance costs, primarily those associated with a federally mandated pipeline integrity management program.

Depreciation Expense - Depreciation increased $5.6 million and $1.7 million during 2012 and 2011, respectively, compared to the prior year due mainly to the increased investment in property, plant and equipment by SJG and Marina.

Energy and Other Taxes - Energy and Other Taxes decreased $2.2 million in 2012 compared with 2011 primarily due to a decrease in SJG's primary energy tax, the Transitional Energy Facilities Assessment, effective January 1, 2012. As this tax is passed through to customers, this decrease in expense had no impact on the financial results of the Company. The change in Energy and Other Taxes in 2011 compared with the prior year was not significant.

Other Income and Expense - Other income and expense decreased $4.5 million in 2012 compared with 2011 primarily due to proceeds received during 2011 from a provider of homeowner assistance services, in accordance with an agreement with the Company, that gives them the exclusive right to renew the home appliance repair contracts at SJESP. The Company also incurred a $1.1 million charge during the first quarter of 2012 at SJEX related to a reduction in expected cash flows to be received from certain shallow well investments in the Marcellus region. Other income and expense increased $11.1 million in 2011 compared to the prior year due to a) interest income on notes receivable from affiliates, and b) proceeds received from a provider of homeowner assistance services, in accordance with an agreement with the Company, that gives them the exclusive right to renew the home appliance repair contracts at SJESP.

Interest Charges - Interest charges decreased $5.1 million in 2012 compared with 2011 due primarily to the positive impact of retiring $35.0 million of SJG's higher priced long-term debt during 2012 and higher capitalization of interest cost on construction at SJG. These decreases are partially offset by the issuance of $115.0 million aggregate principal amount of Senior Notes at the end of the second quarter 2012, along with long-term debt issued by SJG as discussed in Note 14 to the consolidated financial statements. Interest charges increased $2.2 million in 2011 compared to the prior year. The increase in 2011 was due primarily to higher short-term borrowing levels and interest rates at our non-utility businesses in support of increased project development activity, and interest charges on long term debt that was issued during 2010 at SJG, taken over a full year in 2011.

Income Taxes - Income tax expense decreased $11.0 million in 2012 compared with 2011 primarily due to lower taxable income and a lower effective tax rate during 2012 as compared with 2011. The change in the effective tax rate is primarily due to the increase in the investment tax credits available on renewable energy facilities at Marina in 2012 as compared to 2011. Income tax expense decreased $6.3 million for 2011 as compared to 2010. Income tax expense decreased $11.2 million due to the change in the effective tax rate in 2011 as compared to 2010, which is due to increases in the investment tax credits available on renewable energy facilities at Marina. This was partially offset by an increase of $4.9 million due to higher pretax income in 2011 compared to 2010.

Equity in Earnings (Loss) of Affiliated Companies - Equity in earnings of affiliated companies increased $3.0 million for 2012 as compared to 2011, primarily due to new projects coming on line in 2012 and the improved operating performance of our renewable energy project fleet at affiliated companies. Equity in loss of affiliated companies decreased $2.2 million for 2011 as compared to 2010. This decrease in equity in loss of affiliated companies is primarily due to unrealized gains on interest rate swaps at LVE.

Discontinued Operations - The losses are primarily comprised of environmental remediation and product liability litigation associated with previously disposed of businesses.

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LIQUIDITY AND CAPITAL RESOURCES:

Liquidity needs are driven by factors that include natural gas commodity prices; the impact of weather on customer bills; lags in fully collecting gas costs from customers under the BGSS charge and other regulatory clauses; working capital needs of our energy trading and marketing activities; the timing of construction and remediation expenditures and related permanent financings; the timing of equity contributions to unconsolidated affiliates; mandated tax payment dates; both discretionary and required repayments of long-term debt; and the amounts and timing of dividend payments.

Cash Flows from Operating Activities - Liquidity needs are first met with net cash provided by operating activities. Net cash provided by operating activities totaled $117.8 million, $191.4 million and $159.1 million in 2012, 2011 and 2010, respectively. Net cash provided by operating activities varies from year-to-year primarily due to the impact of weather on customer demand and related gas purchases, customer usage factors related to conservation efforts and the price of the natural gas commodity, inventory utilization and gas cost recoveries. Net cash flow from operating activities declined in 2012 as compared to 2011. Factors contributing to the decline included changes in working capital requirements, a pension contribution and income tax refunds. Working capital requirements were higher at the end of 2012 than the prior year due to colder weather experienced at the end of 2012 and customer growth. An $18.7 million bill credit provided at the end of 2011 also reduced cash collections in 2012. Conversely, 2011 cash from operations benefited from storage gas sold at the end of 2010, the receivable for which was collected in 2011. Net cash provided by operating activities was also impacted by a $25.0 million pension contribution that occurred in January 2012. There were no pension contributions made by the Company in 2011. Finally, income tax refunds related to investment tax credits and bonus depreciation were higher in 2011 than 2012. Operating activities produced more net cash in 2011 as compared to 2010 primarily due to higher cash collections of non-utility customer accounts receivable balances, improvements in working capital needs as a result of milder winter temperatures during the fourth quarter of 2011, substantially lower natural gas prices, and a reduction in required tax payments during 2011. These benefits were partially offset by the impact of two BGSS bill credits posted to customer accounts and higher planned environmental remediation spending at SJG.

Cash Flows from Investing Activities - SJI has a continuing need for cash resources and capital, primarily to invest in new and replacement facilities and equipment. Net cash outflows for capital expenditures, which are primarily construction projects, for 2012, 2011 and 2010 amounted to $253.8 million, $193.1 million and $166.9 million, respectively. We estimate the net cash outflows for construction projects for 2013, 2014 and 2015 to be approximately $295.4 million, $253.1 million and $179.7 million, respectively. The increase in the 2012 capital expenditures was a direct result of SJG's CIRT program, which began in 2009. See additional details under “Rates and Regulation.” For capital expenditures, including those under SJG's CIRT, the Company will use short-term borrowings under lines of credit from commercial banks and the commercial paper program to finance capital expenditures as incurred. From time to time, the Company will refinance the short-term debt incurred to support capital expenditures with long-term debt.

In support of its risk management activities, the Company is required to maintain margin accounts with selected counterparties as collateral for its forward contracts, swap agreements, options contracts and futures contracts. These margin accounts are included in Restricted Investments or Margin Account Liability, depending upon the value of the related contracts (the change in the Margin Account Liability is reflected in cash flows from Operating Activities) on the consolidated balance sheets. The required amount of restricted investments changes on a daily basis due to fluctuations in the market value of the related outstanding contracts and are difficult to predict. Margin posted by the Company decreased by $0.8 million during 2012, increased by $10.3 million during 2011 and increased by $3.3 million during 2010.

During 2012, 2011 and 2010, the Company made investments in, and provided net advances to, unconsolidated affiliates of $94.0 million, $14.6 million and $100.9 million, respectively. The purpose of these investments and advances was to acquire The Energy Network, LLC (see Note 3 to the consolidated financial statements), to cover certain project related costs of LVE (see Note 15 to the consolidated financial statements), and to develop landfill gas-fired electric production facilities, solar and thermal energy projects.

Cash Flows from Financing Activities - Short-term borrowings from the commercial paper program and lines of credit from commercial banks are used to supplement cash flows from operations, to support working capital needs and to finance capital expenditures as incurred. From time to time, short-term debt incurred to finance capital expenditures is refinanced with long-term debt.

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Credit facilities and available liquidity as of December 31, 2012 were as follows (in thousands):

Company	Total Facility	Usage	Available Liquidity	Expiration Date
SJG:				
Commercial Paper Program/Revolving Credit Facility	$200,000	$102,100	$97,900	May 2015
Uncommitted Bank Lines (B)	10,000	—	10,000	August 2013
Total SJG	210,000	102,100	107,900	
SJI:				
Revolving Credit Facility	300,000	218,700	81,300	February 2018 (A)
Term Line of Credit (C)	50,000	50,000	—	November 2013
Total SJI	350,000	268,700	81,300	
Total	$560,000	$370,800	$189,200	

(A) Includes letters of credit outstanding in the amount of $31.9 million.

(B) SJG reduced the uncommitted bank lines by $10.0 million during 2012.

(C) In June 2012, SJI increased its term line of credit by $20.0 million, which matures in November 2013.

The SJG facilities are restricted as to use and availability specifically to SJG; however, if necessary the SJI facilities can also be used to support SJG's liquidity needs. All committed facilities contain one financial covenant limiting the ratio of indebtedness to total capitalization (as defined in the respective credit agreements), measured on a quarterly basis. SJI and SJG were in compliance with these covenants as of December 31, 2012. Borrowings under these credit facilities are at market rates. The weighted average interest rate on these borrowings, which changes daily, was 1.10%, 1.12% and 0.99% at December 31, 2012, 2011 and 2010, respectively. Based upon the existing credit facilities and a regular dialogue with our banks, we believe there will continue to be sufficient credit available to meet our business' future liquidity needs.

In February 2013, SJI amended its revolving credit facility with a syndicate of banks to increase the available credit by an aggregate $100.0 million, to a total of $400.0 million. The maturity was also extended to five years from the effective date of the amendment, to February 2018. See Note 18 to the consolidated financial statements.

During the third quarter of 2011, SJG began a commercial paper program under which SJG may issue short-term, unsecured promissory notes to qualified investors up to a maximum aggregate amount outstanding at any time of $200.0 million. The notes have fixed maturities which vary by note, but may not exceed 270 days from the date of issue. Proceeds from the notes are used for general corporate purposes. SJG uses the commercial paper program in tandem with the $200.0 million revolving credit facility and does not expect the principal amount of borrowings outstanding under the commercial paper program and the credit facility at any time to exceed an aggregate of $200.0 million.

SJI supplements its operating cash flow, commercial paper program and credit lines with both debt and equity capital. Over the years, SJG has used long-term debt, primarily in the form of First Mortgage Bonds and Medium Term Notes (MTN), secured by the same pool of utility assets, to finance its long-term borrowing needs. These needs are primarily capital expenditures for property, plant and equipment.

During the third quarter of 2011, SJG entered into an arrangement to issue $35.0 million aggregate principal amount of MTNs under a private placement to occur in April 2012 and repaid $25.0 million of First Mortgage Bonds.

In February 2012, SJG called its $35.0 million, 7.70% MTN's due April 2027 at par plus a 2.0% premium. The early redemption occurred concurrently with the issuance in April 2012 of $35.0 million, 3.74% Series D MTN's due April 2032 as discussed in Note 14 to the consolidated financial statements.

In June 2012 (as discussed in Note 14 to the consolidated financial statements), the Company issued $115.0 million aggregate principal amount of MTNs, consisting of the following: (a) $64.0 million aggregate principal amount of 2.39% Senior Notes due June 2015; (b) $16.0 million aggregate principal amount of 2.71% Senior Notes due June 2017; and (c) $35.0 million aggregate principal amount of 3.46% Senior Notes due June 2022.

In September 2012 (as discussed in Note 14 to the consolidated financial statements), SJG issued $50.0 million of 3.0% aggregate principal amount of MTN's due September 20, 2024. The notes purchase agreement also provided for the issuance of $35.0 million aggregate principal amount of its MTNs that were issued in November 2012.

No other long-term debt was issued during the years ended December 31, 2012 or 2011.

SJG's $150.0 million Medium Term Note (MTN) program that was approved by the BPU in September 2009 expired in September 2011. In December 2011, SJG received approval from the NJ BPU to issue up to $200.0 million in long-term debt by September 2014.

SJI raises equity capital through its Dividend Reinvestment Plan (DRP). Participants in SJI's DRP receive newly issued shares, with SJI offering a 2% discount on DRP investments as it has been considered to be the most cost effective way to raise equity capital. From April 2008 through April 2011, shares of common stock offered by the DRP were purchased in open market transactions. Beginning in May 2011, shares of common stock offered by the DRP have again been issued at a 2% discount directly by SJI from its authorized but unissued shares of common stock. Through the DRP, SJI raised $70.2 million and $13.4 million of equity capital by issuing 1.4 million and 0.3 million shares in 2012 and 2011, respectively. No shares were issued by SJI under the DRP in 2010.

SJI's capital structure was as follows:

	As of December 31,			
	2012		2011	
Equity	43.3	%	45.5	%
Long-Term Debt	36.8	%	31.1	%
Short-Term Debt	19.9	%	23.4	%
Total	100.0	%	100.0	%

The change in the SJI capital structure from 2011 to 2012 is primarily related to the issuance of long-term debt at SJI and SJG as discussed in Note 14 to the consolidated financial statements.

For 2012, 2011 and 2010, SJI paid quarterly dividends to its common shareholders. SJI has paid dividends on its common stock for 61 consecutive years and has increased that dividend each year for the last thirteen years. The Company currently looks to grow that dividend by at least 6% to 7% per year and has a targeted payout ratio of between 50% and 60% of Economic Earnings. In setting the dividend rate, the Board of Directors of SJI considers future earnings expectations, payout ratio, and dividend yield relative to those at peer companies as well as returns available on other income-oriented investments. However, there can be no assurance that the Company will be able to continue to increase the dividend, meet the targeted payout ratio or pay a dividend at all in the future.

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FINANCE OBLIGATION - During 2010, ACB Energy Partners LLC (ACB), a wholly-owned subsidiary of Energenic, of which Marina has a 50% equity interest, completed construction of a combined heat and power generating facility to serve, under an energy services agreement, a thermal plant owned by Marina. Construction period financing was provided by Marina. Due to its continuing involvement in the facility, Marina is considered the owner of the facility for accounting purposes. As a result, the Company included $23.6 million and $23.5 million of costs to construct the facility within Nonutility Property, Plant and Equipment on the consolidated balance sheets as of December 31, 2012 and 2011, respectively. In addition, the Company includes repayments from ACB to Marina on the construction loan within the Finance Obligation on the consolidated balance sheets. Marina does not have a fixed payment obligation to ACB; as a result, the Finance Obligation is classified as a noncurrent liability on the consolidated balance sheets. The costs to construct the facility and the repayments of the construction loan are amortized over the term of the energy services agreement. The impact on the consolidated statements of income is not significant. As a result, the Company recorded $21.6 million and $22.5 million, net of amortization, within Finance Obligation on the consolidated balance sheets at December 31, 2012 and 2011, respectively.

COMMITMENTS AND CONTINGENCIES:

SJI has a continuing need for cash resources and capital, primarily to invest in new and replacement facilities and equipment, and for environmental remediation costs. Cash outflows for capital expenditures for 2012, 2011 and 2010 amounted to $253.8 million, $193.1 million and $166.9 million, respectively. Management estimates net cash outflows for construction projects for 2013, 2014 and 2015 to be approximately $295.4 million, $253.1 million and $179.7 million, respectively. Costs for remediation projects, net of insurance reimbursements for 2012, 2011 and 2010 amounted to net cash outflows of $0.2 million, $13.6 million and $3.5 million, respectively. Total cash outflows for remediation projects are expected to be approximately $17.9 million, $22.6 million and $16.1 million for 2013, 2014 and 2015, respectively. As discussed in Notes 10 and 15 to the consolidated financial statements, certain environmental costs are subject to recovery from insurance carriers and ratepayers.

STANDBY LETTERS OF CREDIT — As of December 31, 2012, SJI provided $31.9 million of standby letters of credit through SJI’s revolving credit facility to enable SJE to market retail electricity and for various construction activities. The Company has also provided $87.6 million of additional letters of credit under separate facilities outside of the revolving credit facility to support variable-rate demand bonds issued through the New Jersey Economic Development Authority (NJEDA) to finance the expansion of SJG’s natural gas distribution system and to finance Marina's initial thermal plant project.

SJG and SJRG have certain commitments for both pipeline capacity and gas supply for which they pay fees regardless of usage. Those commitments as of December 31, 2012, average $50.4 million annually and total $361.7 million over the contracts' lives. Approximately 41.4% of the financial commitments under these contracts expire during the next five years. These contracts are included in the Company's contractual obligations below. We expect to renew each of these contracts under renewal provisions as provided in each contract. SJG recovers all prudently incurred fees through rates via the Basic Gas Supply Service clause.

In addition, in the normal course of business, SJG and SJRG have entered into long-term contracts for natural gas supplies. SJRG has committed to purchase a minimum of 465,700 dts/d and up to 700,000 dts/d of natural gas, from various suppliers, for terms ranging from three to ten years at index-based prices and has also committed to shorter term index deals of approximately 700,000 dts/d. SJG has committed to purchase a minimum of 6,250 dts/d and up to 25,000 dts/d of natural gas, from one supplier, for a term of eight years at index-based prices. The obligations for these purchases have not been included in the Company's contractual obligations discussed below because the actual volumes and prices are not fixed.

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The following table summarizes our contractual cash obligations and their applicable payment due dates as of December 31, 2012 (in thousands):

Contractual Cash Obligations	Total	Up to 1 Year	Years 2 & 3	Years 4 & 5	More than 5 Years
Long-Term Debt	$626,400	$25,000	$95,909	$59,818	$445,673
Interest on Long-Term Debt	304,987	25,873	45,201	46,147	187,766
Construction Obligations	29,999	29,999	—	—	—
Operating Leases	3,395	852	1,367	951	225
Commodity Supply Purchase Obligations	562,026	206,904	151,537	55,967	147,618
New Jersey Clean Energy Program	7,494	7,494	—	—	—
Other Purchase Obligations	118	118	—	—	—
Total Contractual Cash Obligations	$1,534,419	$296,240	$294,014	$162,883	$781,282

Interest on long-term debt in the table above includes the related interest obligations through maturity as well as the impact of all interest rate swap agreements. Expected environmental remediation costs, asset retirement obligations and the liability for unrecognized tax benefits are not included in the table above as the total obligation cannot be calculated due to the subjective nature of these costs and timing of anticipated payments. SJI made contributions to its employee pension plans totaling $25.0 million in January 2012 and $12.7 million in January 2013. However, future pension contributions beyond 2013 cannot be determined at this time. SJG's regulatory obligation to contribute $3.6 million annually to its postretirement benefit plans' trusts, as discussed in Note 12 to the consolidated financial statements, is also not included as its duration is indefinite.

Off-Balance Sheet Arrangements - An off-balance sheet arrangement is any contractual arrangement involving an unconsolidated entity under which the company has either made guarantees or has certain other interests or obligations.

The Company has recorded a liability of $1.9 million which is included in Other Noncurrent Liabilities with a corresponding increase in Investment in Affiliates on the consolidated balance sheets as of December 31, 2012 for the fair value of the following guarantees:

In April 2007, SJI guaranteed certain obligations of LVE Energy Partners, LLC (LVE) an unconsolidated joint venture in which Marina has a 50% equity interest. LVE entered into a 25-year contract with a resort developer to design, build, own and operate a district energy system and central energy center for a planned resort in Las Vegas, Nevada. LVE began construction of the facility in 2007 and expected to provide full energy service in 2010 when the resort was originally scheduled to be completed. LVE suspended construction of the district energy system and central energy center in January 2009 after the resort developer's August 2008 announcement that it was delaying the completion of construction of the resort due to the difficult environment in the capital markets and weak economic conditions. The resort developer had indicated that it was considering different strategies to move its project forward, including opening its project in phases and obtaining a partner, but that it was unlikely construction would resume during 2009. In November 2012, the resort developer, repeating previous disclosures, indicated again that it does not expect to resume construction on the project for three to five years. The resort developer stated that it remains committed to having a significant presence on the Las Vegas Strip as part of a long-term growth strategy and continues to view this site as a major strategic asset.

The district energy system and central energy center are being financed by LVE with debt that is non-recourse to SJI. The outstanding balance of LVE's bank debt is approximately $192.1 million as of December 31, 2012. As a result of the construction delay, the district energy system and central energy center were not completed by the end of 2010 as originally expected. Consequently, the full amount of LVE's debt became due and payable in December 2010. LVE intends to seek additional financing to complete the facility once construction of the resort resumes, however, as of December 31, 2010, LVE was in default under the financing agreements with the banks. The Energy Sales Agreement between LVE and the resort developer includes a payment obligation by the resort developer to pay certain fees and expenses to LVE. A portion of this payment obligation is guaranteed to LVE's lenders by the parent of the resort developer.

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In March 2011, LVE reached agreements with (a) the resort developer, that specified the payments to be made by the developer to LVE during the suspension period and provided the developer and its corporate parent with an option to purchase the assets of LVE, and (b) the banks that are financing the energy facilities to address the existing default under the financing agreements. The terms of the March 2011 agreement require the resort developer to pay certain fees and expenses to LVE on a monthly basis beginning in March 2011 until construction of the resort resumes or until the resort developer has exercised its option to purchase the energy facilities from LVE. The monthly payments that are being paid to LVE by the resort developer are expected to be sufficient to reimburse LVE for costs to maintain the energy facilities and to cover debt service costs over time. The resort developer has provided LVE with a $6.0 million letter of credit to support its monthly payment obligation.

The banks that are financing the energy facilities have agreed not to exercise their rights under the financing agreements resulting from the event of default discussed above through December 2013, provided that no additional events of default occur. SJI and its joint venture partner have provided a total of $10.0 million in letters of credit to the banks to support LVE’s obligations, which can be drawn upon by the banks at the end of the existing agreement in December 2013 or upon the occurrence of an event of default by LVE prior to December 2013.

As of December 31, 2012, the Company had a net liability of approximately $1.6 million included in Other Noncurrent Liabilities on the consolidated balance sheets related to this project, in addition to unsecured Notes Receivable – Affiliate of approximately $56.8 million due from LVE. As of December 31, 2012, SJI’s capital at risk is limited to its equity contributions, letters of credit and the unsecured notes receivable totaling approximately $72.5 million. During 2012, SJI provided support to LVE of approximately $2.2 million to cover interest and other project related costs.

As a result of the construction delay, management has evaluated the investment in LVE and concluded that the fair value of this investment continues to be in excess of the carrying value as of December 31, 2012.

SJI has guaranteed certain performance obligations of LVE under the operating agreements between LVE and the resort developer, up to $20.0 million each year for the term of the agreement, commencing with the first year of operations. SJI and its partner in this joint venture have entered into reimbursement agreements that secure reimbursement for SJI of a proportionate share of any payments made by SJI on this guarantee.

SJI has guaranteed certain obligations of WC Landfill Energy, LLC (WCLE) and BC Landfill Energy, LLC (BCLE), unconsolidated joint ventures in which Marina has a 50% equity interest through Energenic. WCLE and BCLE have entered into agreements through 2018 and 2027, respectively, with the respective county governments to lease and operate facilities that will produce electricity from landfill methane gas. Although unlikely, the maximum amount that SJI could be obligated for, in the event that WCLE and BCLE do not meet minimum specified levels of operating performance and no mitigating action is taken, or are unable to meet certain financial obligations as they become due, is approximately $4.2 million each year. SJI and its partner in these joint ventures have entered into reimbursement agreements that secure reimbursement for SJI of a proportionate share of any payments made by SJI on these guarantees. SJI holds variable interests in WCLE and BCLE but is not the primary beneficiary.

In February 2011, ACR Energy Partners, LLC (ACR), a wholly-owned subsidiary of Energenic, of which Marina has a 50% equity interest, entered into a 20 year contract with a developer to build, own and operate a central energy center and energy distribution system for a new hotel, casino and entertainment complex in Atlantic City, New Jersey. The complex commenced operations in April 2012 and as a result, ACR is providing full energy services to the complex. During the year ended December 31, 2012, Marina and its joint venture partner each made capital contributions to ACR, through Energenic, of $22.0 million. Marina and its joint venture partner have also agreed to provide a $5.0 million letter of credit to support certain operating performance obligations of ACR under the operating agreements between ACR and the developer. SJI and its partner in this joint venture have entered into reimbursement agreements that secure reimbursement for SJI of a proportionate share of any payments made by SJI to or on behalf of ACR.

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In May 2012, UMM Energy Partners, LLC (UMM), a wholly-owned subsidiary of Energenic, of which Marina has a 50% equity interest, entered into a 30 year contract with a public university to build, own and operate a combined heating, cooling and power system for its main campus in New Jersey. The system is expected to be completed during the second half of 2013. Marina and its joint venture partner are obligated to make capital contributions to UMM, through Energenic, totaling approximately $10.0 million. In addition, SJI has guaranteed certain obligations of UMM under the operating and lease agreements between UMM and the university, for the terms of the agreements, commencing with the first year of operations. SJI has guaranteed up to $2.2 million for the first year. This amount is adjusted each year based upon the Consumer Price Index. SJI has also guaranteed certain construction obligations of UMM during the construction period, the majority of which are supported by a surety bond. SJI and its partner in this joint venture have entered into reimbursement agreements that secure reimbursement for SJI of a proportionate share of any payments made by SJI on these guarantees.

As of December 31, 2012, SJI had issued $5.2 million of parental guarantees on behalf of an unconsolidated subsidiary. These guarantees generally expire within the next two years and were issued to enable our subsidiary to market retail natural gas.

PENDING LITIGATION - The Company is subject to claims arising in the ordinary course of business and other legal proceedings. The Company has been named in, among other actions, certain product liability claims related to our former sand mining subsidiary. We accrue liabilities related to these claims when we can reasonably estimate the amount or range of amounts of probable settlement costs or other charges for these claims. The Company has accrued approximately $3.1 million and $2.9 million related to all claims in the aggregate as of December 31, 2012 and 2011, respectively. Management does not believe that it is reasonably possible that there will be a material change in the Company's estimated liability in the near term and does not currently anticipate the disposition of any known claims that would have a material effect on the Company's financial position, results of operations or cash flows.